

Mexican banking crisis paralyzes government

Gerardo Nebbia
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The arrest of banker Carlos Cabal in Melbourne, Australia on November 11 exemplifies the character of Mexico's current political crisis. Cabal is accused of having looted \$700 million from two of his banks during the administration of Carlos Salinas. He fled Mexico in September 1994 when the government seizure of his Grupo Financiero Union-Cremi, owner of Banco Union and Banca Cremi, was imminent. Cabal was a friend of Carlos Salinas and donated millions to the presidential campaign of current president Ernesto Zedillo.

With the help of friends in the Mexican government, he was able to elude the authorities for four years. During this period he lived in the United States, Spain, France, Italy and the Dominican Republic. All this time he was able to manage his considerable fortune with impunity.

Cabal and a handful of corrupt billionaires are being blamed for the bank scandal, which is now shaking Mexico. The government is proposing that the state assume \$55 billion of bank debt.

This crisis involves a state agency named FOBAPROA (Spanish acronym for Bank Fund to Protect Savings) which was established to relieve banks of problem loans. In reality a massive subsidy was given to the country's wealthy and well connected.

The government proposes that FOBAPROA be dismantled and that its portfolio of bank debt be absorbed by the state. In effect this would free the banks from a bad loan portfolio. The payment of this debt, plus interest, will require about 8 percent of GDP for a minimum of 10 years.

President Zedillo plans to pay the debt through increases in the Value Added Tax and cuts in social programs. The government has made a commitment with the International Monetary Fund and the US Treasury not to run deficits in excess of 1.25 percent of GDP. This means that the bank rescue would crowd out social spending, raise taxes on the middle class, and replace subsidies for the 42 million Mexican poor with subsidies to approximately 18 bankers and 25 multimillionaires.

The FOBAPROA scandal is connected to the liberalization of the economy. For the last of 18 years, the Mexican government has methodically dismantled economic structures that insulated the national economy from the world market. While these policies of import substitution were no panacea for Mexico's impoverished masses, their replacement by free-market laissez-faire policies is condemning millions to malnutrition and poverty.

It is estimated that 66 percent of Mexico's 90 million people are worse off than they were in 1986. Forty-seven percent are living under conditions of extreme poverty. On the other hand, the dismantling of national industries has produced a financial bonanza for a handful of billionaires. There is hunger in the rural

sector, where 79 percent of the population lives in extreme poverty.

The transfer of national industry to private capitalists has taken the form of an uncompensated expropriation of national assets by a corrupt financial mafia.

Cabal's trajectory is typical of many of those who took advantage of Salinas's privatization of commercial banks in 1991. The son of a grocery chain owner, he bought Banco Union and Banca Cremi,. He also acquired Florida-based Del Monte Fresh Produce for \$574 million in 1993, his largest of hundreds of business interests.

However in September 1994 the government, under pressure from the political opposition in the wake of the collapse of the Mexican economy, attempted to arrest Cabal, just as he was about to pay nearly \$1 billion to acquire giant Del Monte Food Corp. of San Francisco.

He was accused of making up to \$700 million in loans from his banks to companies he owned--to himself, in effect--thus driving Grupo Financiero Union-Cremi into insolvency. This proved to be the tip of the iceberg. Cabal's banks are suspected of making 250 'phantom loans,' each averaging \$5 million dollars. Four and a half billion dollars of his banks' fraudulent loans were absorbed into FOBAPROA.

Mexican workers, farmers and the urban middle class are being asked to pay for loans given to Cabal and others who bought many of those state enterprises. The result is that the Mexican people will wind up without either the industries and or the money derived from selling them off.

The FOBAPROA scandal is now the most important political issue to challenge the ruling Institutional Revolutionary Party (PRI). Its 70-year hold on political power shows signs of ending. Cabal's arrest threatens to further expose the ruling party's complicity with this illegal transfer of wealth to a handful of billionaires.

While the PRI holds a plurality in Congress, it requires the agreement of one of the two major political parties to get the rescue passed. Both the right-clerical PAN (National Action Party) and the left-populist PRD (Party of the Democratic Revolution) have denounced the rescue as an attempt to foist on the general population fraudulent loans that can no longer be repaid.

The PRD published a partial list of beneficiaries of the loans. The list indicated that many loans had gone to well-connected billionaires, involved kickbacks to the PRI, and in many cases found their way out of Mexico. The PRD then walked out of negotiations on the plan. Mexico City Mayor Cuauhtemoc Cardenas, who expects to win the presidential election in 2000 as the PRD candidate, claimed that none of the people that he has

appointed have had any run-in with the law.

The PAN is divided on this issue. One sector is demanding that Guillermo Ortiz and Pedro Zamora, high officials of the Mexican Central Bank, be impeached and removed from office as a price for its support. They are also demanding complete accountability and punishment for those who committed fraud. Another section of the PAN, under pressure from the banks themselves, is more agreeable to the PRI plan. There is fear among the PAN leaders that to associate too closely with the PRI will lead to electoral disasters.

There are divisions in the PRI on this as well. A 'reform' faction is demanding an end to the free market economics of Salinas and Zedillo and a return to the economic policies of the past. All this has resulted in a political paralysis. Initially, the matter was to be resolved by November 15. Now the agreement has been pushed back into January 1999.

Implicit in the positions of both the PAN and PRD is that the problem is mainly one of corruption, not policy. As the details of the scandal come to light it is apparent that deals were being made behind the backs of the Congress and in violation of the Mexican constitution. However, this is not just a Mexican phenomenon. The process of dismantling state-protected national economies has involved handing over a great deal of the national wealth to various mafias--this has been the case throughout Latin America, in Southeast Asia, China and the former Soviet Union.

In each case a corrupt elite grabs hold of the national wealth and puts it at the disposal of international financial capital. Guillermo Ortiz, for example, is a darling of Wall Street. He has been the object of praise by US Department of Treasury Secretary Rubin. His advice is sought after in Southeast Asia. Both Carlos Cabal and Mexico's last president, Carlos Salinas, were also highly regarded by international capital. Salinas is now in self-imposed exile in Dublin and Havana, facing arrest if he returns to Mexico.

FOBAPROA was a government-sponsored trust fund created in 1990 under the Law of Institutions of Credit. In 1995 the Mexican Treasury Department (SHCP) and Mexico's central bank activated FOBAPROA to absorb bad loans made by Mexican banks and businesses. This was a response to the crisis of 1994, when the economy entered a depression from which it has yet to recover. FOBAPROA was meant to inject liquidity into an ailing financial sector.

As a result of the TESOBONO collapse in 1994, and the flight of \$30 billion from Mexico's banking system to banks in the US and other countries, FOBAPROA gave the banks 552 billion pesos in loan guarantees. At the exchange rate of the time (6 pesos/dollar) that was the equivalent of \$90 billion.

The funds were provided to the banks on condition that they 'guarantee prompt repayment, with bank shares, government bonds or with any other asset that is deemed to satisfy the required guarantee.' However, the money was transferred to individuals, without the required collateral, behind the back of the compliant Mexican Congress. In some cases it appears that the funds that were used to buy commercial banks were borrowed from those same banks, a high-stake form of check kiting.

Among the bad loans that FOBAPROA assumed were those connected to the purchase of the state telephone and gas

distribution system, steel and petrochemical plants, highways, railroads, ports, airlines, television stations and satellite systems.

Another element was added to the crisis last month when the Mexican Supreme Court granted the banks the right to charge interest on top of interests, when borrowers are unable to make the payments on time. In effect, the banks would be adding the late interests to the principal, at prevailing rates. By a vote of 8 to 3 the Supreme Court reversed a 100-year-old ban on this practice. Six million small debtors in arrears will be affected by the decision.

The decision brought many middle class Mexicans into the streets. El Barzón, an association of debtors connected to the PRD, has been organizing occupations of city halls and protests at the Supreme Court. The Congress is unable to simply rubberstamp Zedillo's decisions and has been compelled to demand an accounting.

The Mexican banking authorities have allowed interest rates to rise. Real interest rates are hovering at almost 20 percent. This is affecting credit card holders and many industries. It is contributing to the bankruptcy of agriculture and paralyzing home sales. At the same time the peso is being gradually devalued, making food and raw material imports more expensive every day. The financial sector is being rescued by bankrupting the real economy.

This has meant that, in addition to the nonperforming loans already in FOBAPROA, Mexican banks hold new ones. In some banks as many of 20 percent of the loans are nonperforming. One of the FOBAPROA rescue options is that small new bad loans be traded for the big old ones, hoping that a larger percentage of the former will be recoverable. The most optimistic forecasts predict that 60 percent of the \$55 billion will never be recovered.

According to a recent report from the American Federal Reserve Board, the dollar outflow from Mexico so far this year is the largest in Latin America, \$38 billion, exceeding that from Brazil. Since 1994, \$200 billion has left Mexico, mainly headed to US banks, but also to banks in the Cayman Islands and in Europe.

Some Mexican economists have suggested that, in the face of this 'dollarization' of Mexican savings, the peso be abandoned and Mexico adopt the dollar as its currency, openly recognizing the controlling influence of the US Federal Reserve Board and the country's subordination to Washington and to the movement of financial capital around the world.

See Also:

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