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Prime
Minister

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TO IMMEDIATE FCO

TELEGRAM NUMBER 713 OF 2 SEPTEMBER

INFO PRIORITY WASHINGTON, TREASURY, DOT, ECGD, BANK OF ENGLAND.

MIPT: PRESIDENT LOPEZ PORTILLO'S STATE OF THE NATION ADDRESS:
COMMENT

1. PRESIDENT LOPEZ PORTILLO'S DECISION AT ONE STROKE TO IMPOSE FULL EXCHANGE CONTROLS AND TO NATIONALISE PRIVATE MEXICAN BANKS REPRESENTS A DRAMATIC ATTEMPT TO RECOVER THE POLITICAL INITIATIVE IN MEXICO, TO RE-ESTABLISH HIS REPUTATION AS A LEADER (TAKING THE MANTLE OF PRESIDENT LAZARO CARDENAS WHO NATIONALISED THE OIL INDUSTRY IN THE 1930S) AND TO FIX MEXICAN FINANCIERS AND THEIR FOREIGN FRIENDS AS THE GUILTY MEN RESPONSIBLE FOR THE CURRENT ECONOMIC CRISIS.

2. THERE HAVE BEEN MURMURS FOR SOME TIME ABOUT THE POSSIBILITY OF SUCH MEASURES BUT THE DECISION CAME AS A SHOCK TO ALL (INCLUDING THE AMERICANS WHO HAVE BEEN WORKING CLOSELY WITH THE MINISTRY OF FINANCE AND THE BANK OF MEXICO).

THE PRESIDENT MAY WELL BELIEVE THAT THE BANKS WERE AT LEAST PARTLY RESPONSIBLE FOR THE LATEST RUN ON THE PESO, AND MUST KNOW THAT AT LEAST FOUR OF THE MAIN PRIVATE BANKS HAVE RECENTLY HAD DIFFICULTIES IN ROLLING OVER THEIR SHORT-TERM FUNDS. THE BANKS HAVE HITHERTO OPERATED UNDER A CONCESSION FROM THE GOVERNMENT WITHDRAWABLE AT WILL. AS PUBLIC SECTOR BANKS HAVE A SUBSTANTIAL SHARE OF THE MARKET AND THE CENTRAL BANK'S CONTROL OVER THE WHOLE SYSTEM IS STRONG, THE DECISION TO NATIONALISE MAY BE LESS STARTLING IN ITS EFFECTS THAN IT NOW LOOKS.

3. IN INTERNAL POLITICAL TERMS THE PRESIDENT MAY WELL SUCCEED IN HIS IMMEDIATE AIM. MEXICANS GENERALLY LIKE A BOLD AND RADICAL STROKE. THE PRIVATE BANKS ARE NOTORIOUSLY INEFFICIENT AND RAPACIOUS, AND BANKERS SYMBOLISE FLAGRANT WEALTH IN A COUNTRY WHERE EXTREMES OF RICHES AND POVERTY ARE STARK. MEXICANS ARE PREDISPOSED TO BLAME FOREIGNERS, ESPECIALLY AMERICANS, FOR THEIR ILLS, AND ARE CONSCIOUS OF THE INCREASING PENETRATION OF THE US DOLLAR INTO THEIR ECONOMY. THE ARGUMENT THAT THE GOVERNMENT WAS LOSING CONTROL OF ONE OF THE ESSENTIAL ASPECTS OF SOVEREIGNTY WILL HAVE MUCH APPEAL. SO WILL THE PRESIDENT'S STATEMENT THAT THE SAVINGS OF THE COUNTRY HAD BEEN EXTRACTED FOR USE ABROAD, AND THAT IN SEEKING NOW TO BORROW DOLLARS, MEXICANS WERE BEING ASKED TO BEG FOR THE CRUMBS FROM THEIR OWN BREAD. BY ACTING AS HE HAS, THE PRESIDENT WILL ALLY HIMSELF WITH THE TRADES UNION MOVEMENT WHICH HAD LONG BEEN ASKING FOR THE DECISIONS NOW TAKEN. THIS MAY BE THE PRICE FOR WAGE RESTRAINT.

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4. BUT THESE FAVOURABLE EFFECTS FOR THE PRESIDENT MAY NOT LAST. THE MEXICANS HAVE A PROFOUND AND WELL-JUSTIFIED DISTRUST OF ALL GOVERNMENT ACTIVITIES AND NATIONALISED INDUSTRIES, AND THE IDEA OF A NATIONALISED BANKING SYSTEM WILL NOT INSPIRE CONFIDENCE, AT LEAST AMONG THOSE WHO HOLD BANK ACCOUNTS. THE PRESIDENT SHOWED HIMSELF AWARE OF THIS IN HIS SPEECH. MANY WILL FEAR THAT THE NEXT STEP WILL BE TO EXTEND THE CONTROL OF THE STATE OVER INDUSTRY THROUGH THE MONOPOLY OF LOAN CAPITAL AND THE ACQUISITION OF THE PRIVATE BANKS' LARGE STAKE IN INDUSTRY, COMMERCE AND TOURISM. MANY WILL ASK WHY THE GOVERNMENT COULD NOT HAVE SOLVED THE PROBLEM EARLIER BY LESS DRASTIC MEANS: TO TAKE MEASURES OF THIS KIND IN THE LAST THREE MONTHS OF A SIX-YEAR ADMINISTRATION LOOKS LIKE DESPERATION RATHER THAN WISDOM. MANY WILL BE AWARE OF THE PRACTICAL DIFFICULTIES, HITHERTO JUDGED INSURMOUNTABLE, IN ENFORCING EXCHANGE CONTROL, PARTICULARLY IN BORDER AREAS. IN THE PRESENT CYNICAL ATMOSPHERE MANY BELIEVE THAT AMONG THE MAIN CULPRITS FOR THE FLIGHT OUT OF PESOS ARE THE MEMBERS OF THE LOPEZ PORTILLO FAMILY AND THE POLITICIANS OF THE RULING PARTY. THE IMPLICATIONS FOR BUSINESS AND THE ECONOMY AS A WHOLE CANNOT NOW BE ASSESSED, BUT BY PERPETUATING THE CONFUSION AND UNCERTAINTY REFERRED TO IN MY TELNO 707, THE SITUATION COULD BE MADE WORSE RATHER THAN BETTER.
5. THE INTERNATIONAL IMPLICATIONS ARE SO FAR REMOTE FOR MOST MEXICANS. NO DOUBT THE PRESIDENT HAS CALCULATED THAT MEXICO IS TOO IMPORTANT IN THE WORLD ECONOMY FOR ANYONE, INCLUDING ITS CREDITORS AND THE INTERNATIONAL MONETARY FUND, TO ALLOW IT TO GO BUST. THE INTERNATIONAL FINANCIAL COMMUNITY HAS TOO BIG A STAKE IN THE COUNTRY. I GATHER THAT AT ONE POINT IN THE NEGOTIATIONS IN WASHINGTON LAST WEEK, THE MEXICAN MINISTER OF FINANCE THREATENED TO WITHDRAW AND TO DECLARE MEXICO IN DEFAULT IF CERTAIN CONDITIONS WERE PRESSED UPON HIM.
6. THROUGHOUT THE PRESIDENT'S SPEECH RAN A STRONG UNDER-CURRENT OF RESENTMENT AGAINST THE UNITED STATES. THIS WAS PARTICULARLY EVIDENT IN THE SECTION ON FOREIGN AFFAIRS. HIS PRIVATE SECRETARY RECENTLY TOLD ME HOW STRONGLY HE FEELS ON THE SUBJECT. THE PRESIDENT'S DECISIONS OF TODAY ARE NOT ONLY AN ATTEMPT TO RECOVER AUTHORITY AT HOME BUT ALSO AN ACT OF DEFIANCE AGAINST FOREIGNERS, ESPECIALLY AMERICANS, WHO IN HIS JUDGEMENT HAVE BEEN TRYING TO SUBORN MEXICAN SOVEREIGNTY.
7. A MAJOR UNCERTAINTY IS THE ATTITUDE OF PRESIDENT-ELECT DE LA MADRID, WHO SAT IMPASSIVELY THROUGH THE SPEECH. IT IS HARD TO BELIEVE THAT HE CAN HAVE WELCOMED POPULIST DECISIONS WHICH WILL GRAVELY COMPLICATE HIS OWN TASK WHEN HE TAKES OVER ON 1 DECEMBER.
8. FCO PLEASE ADVANCE TO ATKINSON (TREASURY), OWEN (DOT), HALL (ECGD) AND GILCHRIST (BANK OF ENGLAND).

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