



Foreign and Commonwealth Office

London SW1A 2AH

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11 July 1989

Dear Charles,

French Bicentenary: The Prime Minister's Meeting with the  
President of Mexico: 1530-1600, 13 July

Further to my letter of 10 July, you will wish to be aware of recent progress in Mexico's negotiations with the banks.

The positions of the Mexicans and their creditor banks have narrowed over the weekend. The Banks put a final offer to the Mexicans late last week of either a 35% discount on the existing debt, or a 6½% of interest rate on the debt's present face value, or new loans at an average of 25% of the banks' exposure base. These have been accepted in principle by the Mexicans, despite their making a last minute counter offer, which was firmly rejected by the banks. There are still areas of disagreement, both between the banks themselves and the Mexicans and the banks, on the rate of disbursement, and the banks' wish to revert to normal interest rates at some future date. It is not clear when the banks would decide to revert to a normal interest rate. It is now the US banks (rather than the UK institutions) that are proving difficult, and there is still a possibility that negotiations might break down. The Prime Minister could welcome the progress made in the negotiations as an important step in IMF and World Bank supported debt reduction operations, and could urge the early resolution of the remaining differences.

Quite separately, and in strict confidence, the US side at Rambouillet put forward suggestions for a Mexican bridging loan in which the Bank of England would be expected to take part. It is not clear whether this is strictly necessary; whether the security is adequate; or whether the Mexicans even know the details of the US

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proposal. If Salinas raises this, the Prime Minister might say that although she is aware of the proposal, it is primarily a matter for Central Banks, who are still discussing it.

I am copying this letter to Alex Allan (HM Treasury) and Trevor Woolley (Cabinet Office).

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MEXICO : CURRENT SITUATION

SUMMARY

1. SALINAS DOMINATES THE POLITICAL SCENE. STILL PURSUING AN ECONOMIC POLICY OF AUSTERITY. FOREIGN DEBT TALKS ARE DRAGGING ON, BUT AN AGREEMENT IS ULTIMATELY EXPECTED. THE POOR SHOWING OF CARDENAS IS MAKING THINGS EASIER FOR THE GOVERNMENT, ALTHOUGH THE RIGHT WING MAY DO WELL IN ONE OF THE STATE ELECTIONS. SALINAS IS WINNING THE WAR OF ATTRITION AGAINST THE TRADE UNIONS, AND HAS BEGUN A CAMPAIGN AGAINST DRUG TRAFFICKING. GOOD RELATIONS WITH THE UNITED STATES ARE BEING MAINTAINED, AND GREAT INTEREST SHOWN IN THE EC.

DETAIL

2. IN MY TELELETTER 014/1 OF 3 APRIL TO COLTMAN (MCAD) (COPIED TO CABINET OFFICE AND WASHINGTON) I SAID THAT SALINAS WAS PROVING TO BE A DECISIVE LEADER AND TO BE FIRMLY IN CHARGE. THIS IS EVEN MORE TRUE TODAY.

THE PRESIDENT

3. THE PRESIDENT IS NOW THE DOMINANT FIGURE. HE IS MORE INVOLVED IN BOTH POLICY AND ITS EXECUTION THAN HIS PREDECESSOR. HE IS FIRM AND DECISIVE, BUT PERHAPS A LITTLE IMPETUOUS. EVERY FEW WEEKS HE PRODUCES SOME NEW SURPRISE. THE ARREST A COUPLE OF MONTHS AGO OF FELIX, A NOTORIOUS DRUGS BARON, WAS GENERALLY POPULAR. WHEN THE TEACHERS TRADE UNION DEMANDED THE RETIREMENT OF JONGITUD, THEIR LEADER FOR MANY YEARS, HE TOLD HIM TO GO. MOST RECENTLY HE PUBLICLY DEMANDED, AND OBTAINED IN A MATTER OF DAYS, THE ARREST OF THOSE BELIEVED RESPONSIBLE FOR THE MURDER IN 1984 OF A WELL KNOWN POLITICAL JOURNALIST, BUENDIA. HIS PROBLEM NOW IS THAT HE IS ON A TREADMILL WHICH HE CANNOT APPARENTLY STOP : THE REGULARITY OF HIS COUPS LEADS THE PUBLIC TO EXPECT A NEW ONE EVERY MONTH.

ECONOMY

4. AT PRESENT SALINAS IS GOING THROUGH A DIFFICULT PERIOD. CONTRARY TO HIS EARLIER HOPES, HE FACED A RENEGOTIATION OF THE ECONOMIC PACT



WITHOUT HAVING MUCH TO SHOW FROM THE EXTERNAL DEBT NEGOTIATIONS. IT IS A SIGN OF HIS PERSONAL AUTHORITY THAT HIS GOVERNMENT WERE NEVERTHELESS ABLE TO FORCE THROUGH A FURTHER EIGHT MONTHS EXTENSION. THE SUCCESS OF THE PACT IN REDUCING INFLATION TO 18 % NO DOUBT HELPED. BUT HE STILL FACES THE DEBT PROBLEM.

5. WITH CONSIDERABLE AMERICAN HELP THE MEXICANS HAVE GOT THROUGH THE IFI'S AND THE PARIS CLUB. DESPITE CONTINUING AMERICAN HELP THEY ARE HAVING GREAT DIFFICULTY IN REACHING AGREEMENT WITH THE COMMERCIAL BANKS. THE BRITISH, EUROPEAN, AND JAPANESE BANKS ARE ALLEGEDLY PROVING THE MOST INTRANSIGENT. SALINAS MAY RAISE THE MATTER WITH THE PRIME MINISTER NEXT WEEK IN PARIS, IF NO ADVANCE HAS BEEN MADE IN THE MEAN TIME.

#### CURRENT POLITICAL SITUATION

6. ON 2 JULY ELECTIONS WERE HELD IN FOUR STATES, THE MOST IMPORTANT BEING MICHOACAN, ( FOR THE STATE ASSEMBLY) AND BAJA CALIFORNIA NORTE (FOR GOVERNOR). MICHOACAN IS THE HOME STATE OF CARDENAS WHERE HE POLLED THREE TIMES AS MANY VOTES AS SALINAS A YEAR AGO. IT IS AN INDICATION OF HIS LOSS OF MOMENTUM, AND THE PROBLEMS HIS NEW PARTY STILL FACES, THAT THE PRI SAY THEY WILL WIN. OUR SECOND SECRETARY, WHO WAS IN THE AREA ON VOTING DAY, SAYS THAT NOT JUST ONE BUT THREE LEFT WING CANDIDATES ARE STANDING FOR ALL SEATS. I EXPECT THE PRI TO RETAIN CONTROL OF THE STATE CONGRESS ALTHOUGH THERE WILL UNDOUBTEDLY BE ACCUSATIONS OF FRAUD FROM THE OPPOSITION. IN BAJA CALIFORNIA NORTE THE PAN ( RIGHT WING) ARE FIELDING A STRONG CANDIDATE WHO COULD WIN. IF SO, HE WOULD BE THE FIRST OPPOSITION STATE GOVERNOR. THE RESULTS WILL BE ANNOUNCED ON 9 JULY. IF THE PAN BELIEVE THAT THE VOTES HAVE BEEN RIGGED TO GIVE THE PRI CANDIDATE AN UNFAIR VICTORY, THEY SAY THEY WILL BLOCK THE BORDER CROSSING POINTS INTO THE UNITED STATES. THIS WOULD BE WHILE SALINAS WAS IN PARIS, AND COULD THUS BE A SOURCE OF EMBARRASSMENT FOR HIM.

#### MODERNISATION

7. SALINAS' POLICY OF MODERNISATION IS MAKING LITTLE HEADWAY ON POLITICAL REFORM. THE CONSULTATIONS ABOUT ELECTORAL REFORM WITH THE OPPOSITION HAVE GOT NOWHERE, AND THE OPPOSITION CLAIM THAT THE PRI ARE NOT PREPARED TO MAKE EVEN THE MINIMUM NECESSARY CONCESSIONS. DISCUSSIONS ARE TO BE RESUMED IN CONGRESS AT THE END OF NEXT MONTH. AS FAR AS THE ECONOMY IS CONCERNED MODERNISATION IS TAKING THE FORM OF A DRIVE FOR EFFICIENCY. AT PRESENT THE EFFECT IS FELT MOST IN THE LABOUR SECTOR AND IN THE CAMPAIGN AGAINST CORRUPTION, ALTHOUGH THE LATTER HAS MORE THAN PURELY ECONOMIC CONSEQUENCES.



## THE TRADE UNIONS

8. IN THOSE INDUSTRIES WHERE PRI TRADE UNIONS ARE PREDOMINANT, PARTICULARLY IN THE PARASTATALS, WORKERS HAVE TRADITIONALLY BEEN PAID FOR THEIR POLITICAL SUPPORT. NOW SALINAS WANTS ALL WORKERS TO BE PAID ACCORDING TO THEIR PRODUCTIVITY. THIS IS UPSETTING THE LONG ESTABLISHED SYSTEM OF CAIQUES (STRONG MEN) AND PATRONAGE WHICH CHARACTERISES THE PRI IN ALL ITS ASPECTS INCLUDING LABOUR RELATIONS. IT IS ALSO UNDERMINING THE CTM, THE TRADE UNION SECTOR OF THE PRI. IT IS THUS ULTIMATELY HELPING TO UNDERMINE THE SYSTEM OF A ONE PARTY CORPORATE STATE. IN THE SHORT TERM IT MUST ALSO LEAD TO INCREASED UNEMPLOYMENT.

9. SALINAS HAS AVOIDED DIRECT CONFRONTATION WITH THE UNION MOVEMENT SO FAR, ALTHOUGH HE WENT THROUGH A DIFFICULT PERIOD WITH THE TEACHERS AND MEXICO CITY BUS DRIVERS IN APRIL/MAY, AND THE LEADER OF THE CTM, VELASQUEZ, REFUSED TO SIGN THE RECENT MINIMUM WAGE AGREEMENT BECAUSE HE BELIEVED THE INCREASE SHOULD BE 10 PERCENT NOT 6 PERCENT. THE PETROL WORKERS, DEPRIVED OF THEIR FORMER LEADER AND COWED BY THE KNOWLEDGE OF THE FORCE WHICH SALINAS HAS SHOWN HIMSELF PREPARED TO USE, ARE SLOWLY BEING FORCED TO MAKE THEIR OPERATIONS MORE EFFICIENT. THE TELEPHONE UNION, WITH THE THREAT OF PRIVATISATION HANGING OVER THEIR HEADS, AND HAVING SEEN WHAT HAS HAPPENED TO OTHERS, HAVE NEGOTIATED A SHORT TERM EFFICIENCY AGREEMENT WITH MANAGEMENT AND SEEM LIKELY TO NEGOTIATE A FURTHER ONE. WORKERS IN AT LEAST ONE STEEL PLANT ARE BEING FORCED TO FACE UP TO THE FACT THAT THERE IS NOT WORK FOR ALL AND THAT A SIZEABLE MINORITY WILL HAVE TO BE LAID OFF. IN THE PRIVATE SECTOR WORKERS ARE DOING WELL IN THOSE INDUSTRIES WITH PLENTY OF ORDERS, AND MANY SKILLED WORKERS ARE EARNING GOOD MONEY. THE INDEPENDENT TRADE UNION AT THE VOLKSWAGEN PLANT WENT ON STRIKE ON 1 JULY AND IN A FEW HOURS WERE GRANTED AN IMMEDIATE RISE OF 19 PERCENT, WHICH IS 3 PERCENT MORE THAN OTHER CAR COMPANIES HAVE GIVEN THEIR WORKERS. BUT MOST MEXICANS ARE FEELING THE PINCH AFTER OVER 18 MONTHS OF THE PACT.

## CORRUPTION

10. I BELIEVE THAT SALINAS' CAMPAIGN AGAINST CORRUPTION IS AIMED AS MUCH AS ANYTHING AGAINST INEFFICIENCY. THE ACTION HE TOOK AGAINST THE OIL WORKERS LEADER LAST JANUARY, FOR EXAMPLE, HAD AS ITS ULTIMATE AIM THE END OF CORRUPT INEFFICIENCY IN THE OIL FIELDS. A MAJOR SOURCE OF CORRUPTION, IF ONLY BECAUSE OF THE VAST SUMS OF MONEY INVOLVED, IS DRUG TRAFFICKING.

## DRUG TRAFFICKING



11. THE CAMPAIGN AGAINST DRUG TRAFFICKING GOES FURTHER THAN A MERE EFFICIENCY DRIVE. THERE IS ALWAYS THE POSSIBILITY OF THE DRUG TRAFFICKERS CREATING A STATE WITHIN A STATE. THE ARREST OF FELIX WAS A BOLD STEP IN THE RIGHT DIRECTION, BUT THE RAMIFICATIONS SEEM INCALCULABLE. IT IS NOT YET CLEAR WHETHER THIS ARREST IS CONNECTED TO THE BUENDIA CASE, WHICH DATES BACK TO 1984, BUT IT SEEMS THAT BUENDIA HAD INFORMATION ABOUT DRUG TRAFFICKING WHICH IMPLICATED PEOPLE IN HIGH PLACES. WHATEVER THE TRUTH OF THE MATTER, IT IS CLEAR THAT THERE WAS A MAJOR COVER UP DURING THE LAST FEW YEARS OF THE PREVIOUS PRESIDENCY. THE FINGER POINTS TO BARTLETT, MINISTER OF THE INTERIOR UNDER DE LA MADRID AND NOW MINISTER OF PUBLIC EDUCATION. IT ALSO POINTS TO THE FORMER MINISTER OF DEFENCE, GENERAL AREVALO, BECAUSE THE ARMY ALSO APPEAR TO HAVE BEEN HEAVILY INVOLVED IN DRUG TRAFFICKING. INEVITABLY IT ALSO POINTS TO FORMER PRESIDENT DE LA MADRID WHO MUST EVENTUALLY HAVE DISCOVERED WHAT HAD HAPPENED. THERE ARE TWO QUESTIONS TO WHICH WE DO NOT YET KNOW THE ANSWERS. TO WHAT EXTENT AMONG THE PRI LEADERSHIP DOES INVOLVEMENT GO? AND WHAT WILL SALINAS DO IF EVERYTHING IS DISCLOSED? THE CONSEQUENCES COULD BE SERIOUS BOTH FOR THE PARTY AND FOR THE GOVERNMENT.

#### FOREIGN POLICY

12. TO ACHIEVE HIS AIMS FOR THE ECONOMY SALINAS NEEDS THE HELP AND CO-OPERATION OF THE UNITED STATES GOVERNMENT. GOOD BILATERAL RELATIONS ARE THEREFORE ESSENTIAL. THE DRIVE AGAINST DRUG TRAFFICKING HAS HELPED GREATLY. FOR THEIR PART THE AMERICANS, CONCERNED AT THE RESULT OF THE MEXICAN PRESIDENTIAL ELECTIONS LAST YEAR, ARE ALSO CLEARLY TAKING THE RELATIONSHIP SERIOUSLY. THEY ARE BEING HELPFUL WHEREVER THEY CAN, EG. OVER THE FOREIGN DEBT NEGOTIATIONS. THE SALINAS/BUSH RELATIONSHIP CONTINUES TO BE CLOSE: THEY SPEAK ON THE PHONE (EG. AT THE TIME OF THE PANAMA ELECTIONS): SALINAS IS DUE TO VISIT WASHINGTON IN OCTOBER. AT A LOWER LEVEL SOLANA HAS BEEN TO WASHINGTON AND BAKER IS DUE HERE NEXT MONTH. THE LEFTWING ARE STILL HOSTILE TO THE UNITED STATES AND THE MEXICAN GOVERNMENT'S RECENT STATEMENT ON PANAMA, BELIEVED TO HAVE BEEN DESIGNED TO PLEASE THE US, LED TO A SIT-IN IN THE FOREIGN MINISTER'S OFFICE. SO ALTHOUGH RELATIONS ARE GOOD AT GOVERNMENT LEVEL THERE IS STILL CONSIDERABLE SUSPICION AND HOSTILITY TOWARDS THE UNITED STATES IN THIS COUNTRY.

13. MEXICO IS SHOWING INCREASING INTEREST IN THE EUROPEAN COMMUNITY AND A DEGREE OF CONCERN ABOUT THE EFFECTS OF 1992 ON TRADE: THE PRIME MINISTER MAY EXPECT TO BE QUESTIONED ABOUT THIS. THE MEXICANS CONTINUE TO PAY LIP SERVICE TO LATIN AMERICAN SOLIDARITY, BUT THEY ARE PREPARED TO GO IT ALONE WHEN THEIR OWN INTERESTS ARE SO



SERVED, EG. OVER THE EXTERNAL DEBT. CENTRAL AMERICA IS LOW IN THEIR LIST OF PRIORITIES. THE POSSIBILITIES OF TRADE WITH AND INVESTMENT FROM OTHER PACIFIC RIM COUNTRIES IS INCREASING AND THE JAPANESE ARE SHOWING GREAT INTEREST IN BOTH.

## ANGLO-MEXICAN RELATIONS

14. UNDER THE NEW ADMINISTRATION RELATIONS CONTINUE TO BE GOOD IF LACKING IN SUBSTANCE. THANKS TO MR EGGAR'S INTEREST AND INVOLVEMENT WE ARE PURSUING ACTIVELY THE DRAFTING OF A TREATY ON CO-OPERATION AGAINST DRUG TRAFFICKING: WE BELIEVE SALINAS MAY WISH TO DISCUSS THIS WITH THE PRIME MINISTER. BRITISH EXPORTS ARE STEADY, BUT OUR COMPETITORS ARE DOING BETTER: IT IS DIFFICULT TO SAY WHY, BUT SOME OF OUR EXPORTS MAY BE COMING VIA THE UNITED STATES, OR BE PRODUCED BY BRITISH OWNED SUBSIDIARIES IN THE UNITED STATES, AND DO NOT THEREFORE APPEAR IN THE STATISTICS.

## INTERIM ASSESSMENT

15. SALINAS APPEARS TO BE ON TOP OF HIS JOB AT THE MOMENT. HE IS CONTINUING TO MAINTAIN AN AUSTERITY PROGRAMME BUT HE MUST LET UP SOON: THE PEOPLE CAN ONLY PUT UP WITH SO MUCH. A SUCCESSFUL CONCLUSION TO THE DEBT NEGOTIATIONS WOULD ENABLE HIM TO CONSIDER SOME RELAXATION. MEANWHILE, IN THE ATTEMPT TO OPEN UP THE ECONOMY AND MAKE IT MORE EFFICIENT, THE ROLE OF THE STATE IS GRADUALLY BEING WHITTLED AWAY. THE CAMPAIGN AGAINST DRUG TRAFFICKING COULD UNEARTH SOME SKELETONS WHICH MIGHT SERIOUSLY DAMAGE THE PRI'S REPUTATION, BUT THE POOR SHOWING OF THE OPPOSITION, IN PARTICULAR OF CARDENAS, MAKES IT EASIER FOR SALINAS TO TAKE RISKS.

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