



Public Debt Strategy in Mexico

**3rd OECD-China Forum on Public
Debt Management and Government
Securities Markets**

September 2006, Beijing, China

UCP

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1. Debt Management Strategy Overview
2. Recent Liability Management Operations
3. Policy Guidelines and Concluding Remarks



Public debt management has been a key element of economic policy in recent years

The annual debt management strategy has followed three main guidelines:

- Finance the public deficit internally.
- Focus domestic financing on long-term fixed-rate securities
- Improve external financing conditions through a series of coordinated operations.

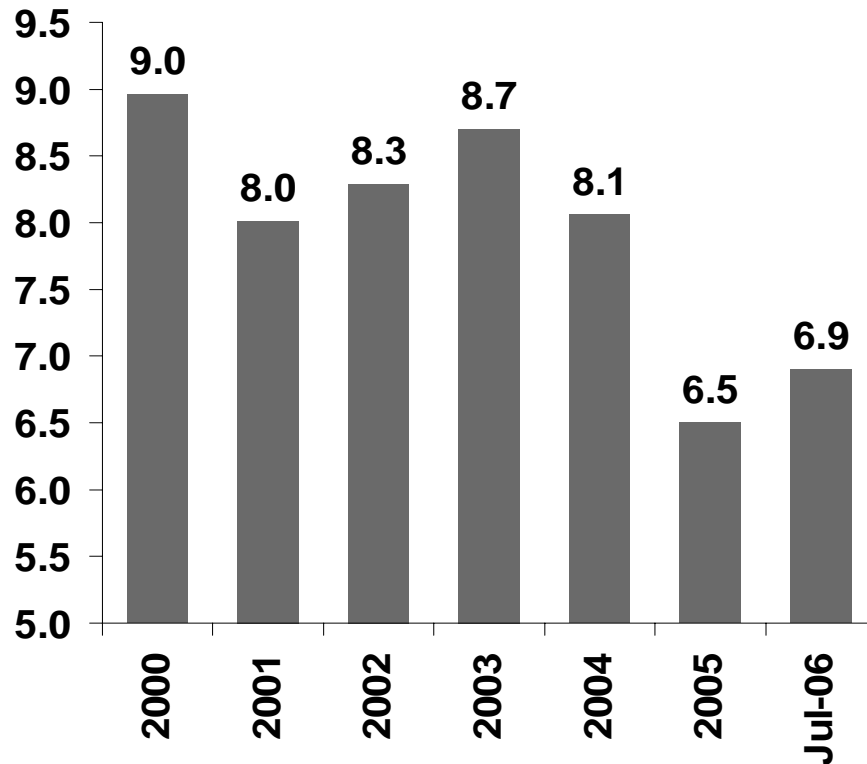


Main Achievements

- 1. A balanced composition of domestic and external debt**
- 2. Improved external debt structure**
- 3. Development of local debt markets**

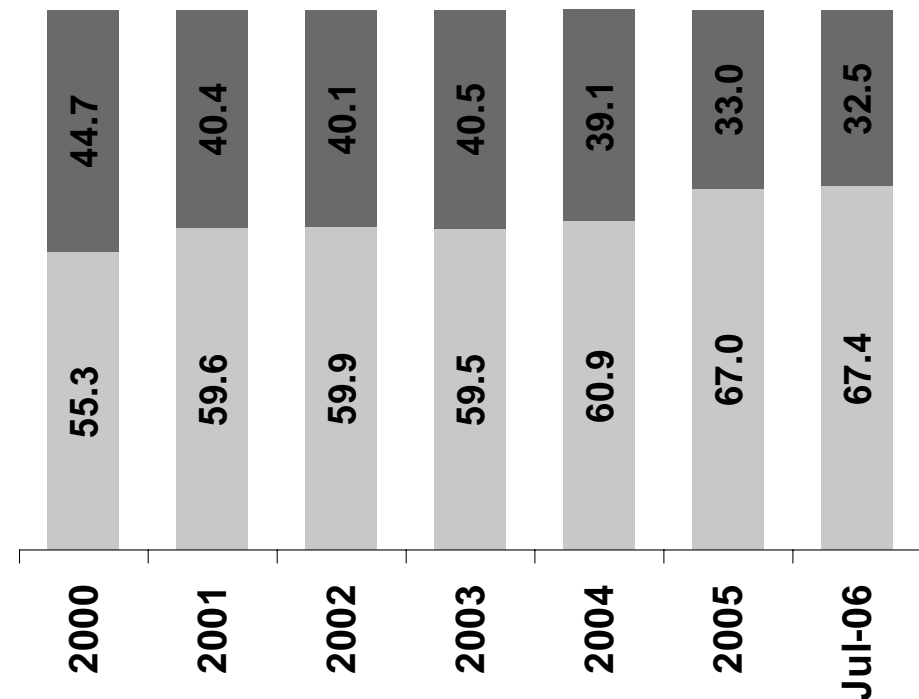
1. A balanced debt composition

Federal Government's Net External Debt
(% of GDP)



Source: SHCP

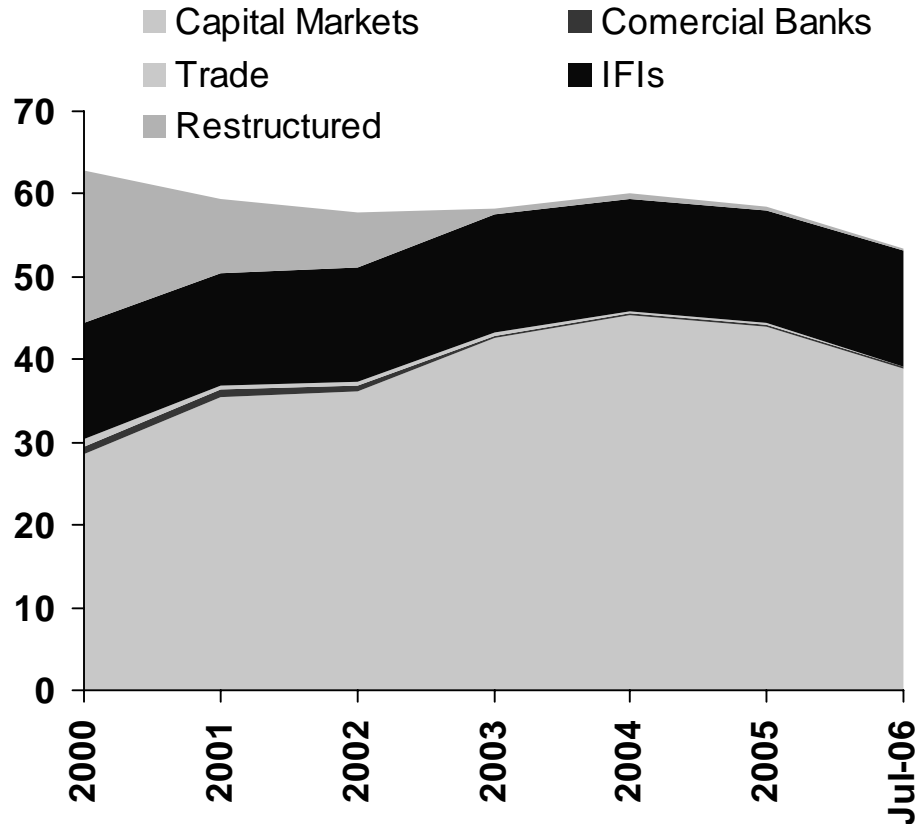
Federal Government's Net External Debt Composition
(%)



Source: SHCP

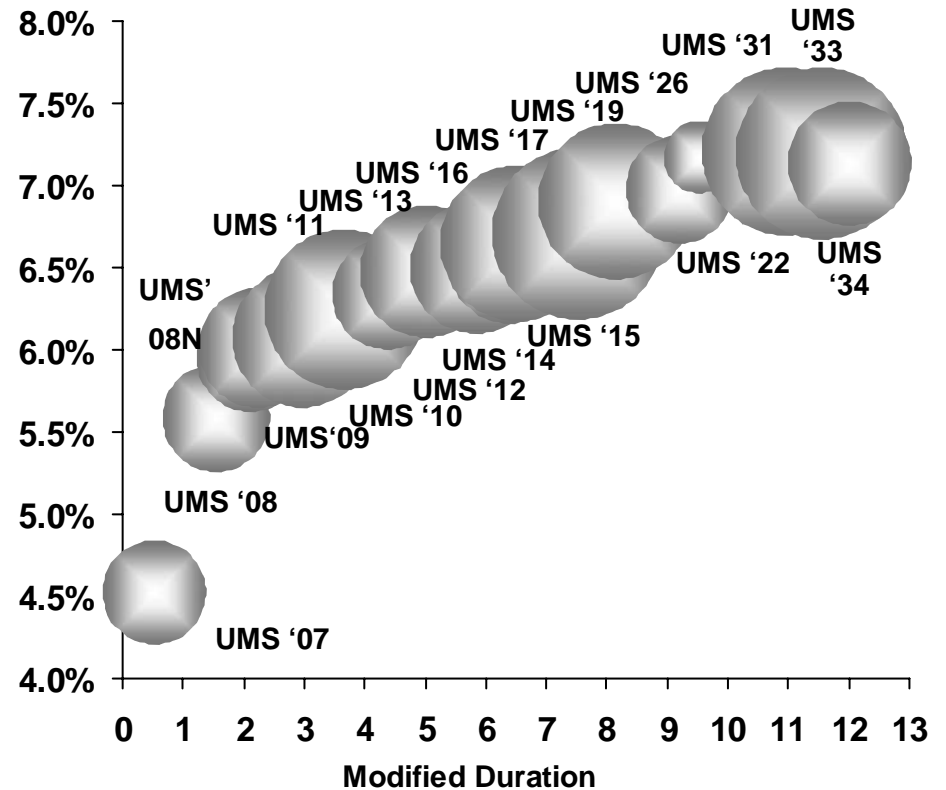
2. An improved structure of external debt

Federal Government's Gross External Debt
(Billion dollars)



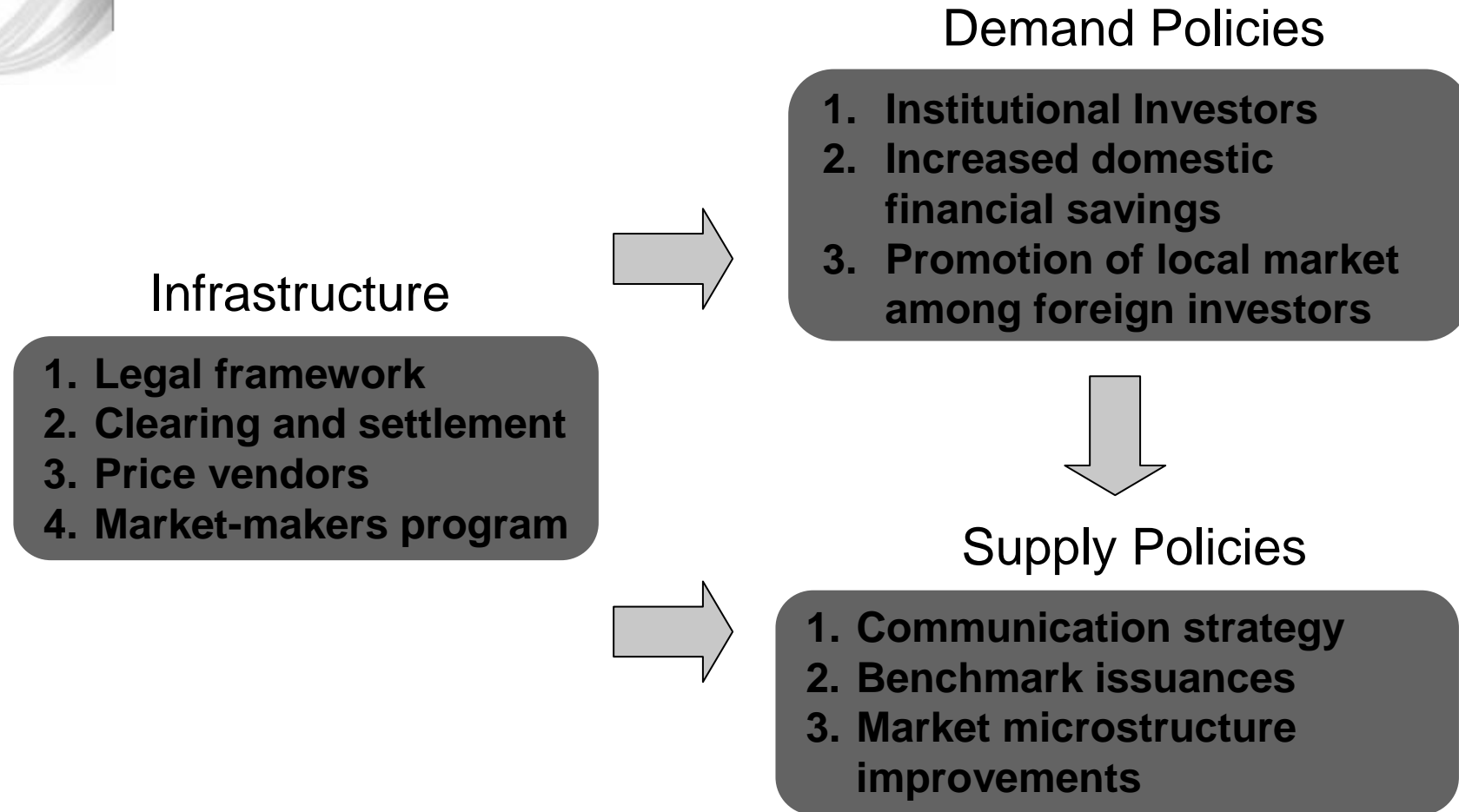
Source: SHCP

UMS Yield Curve



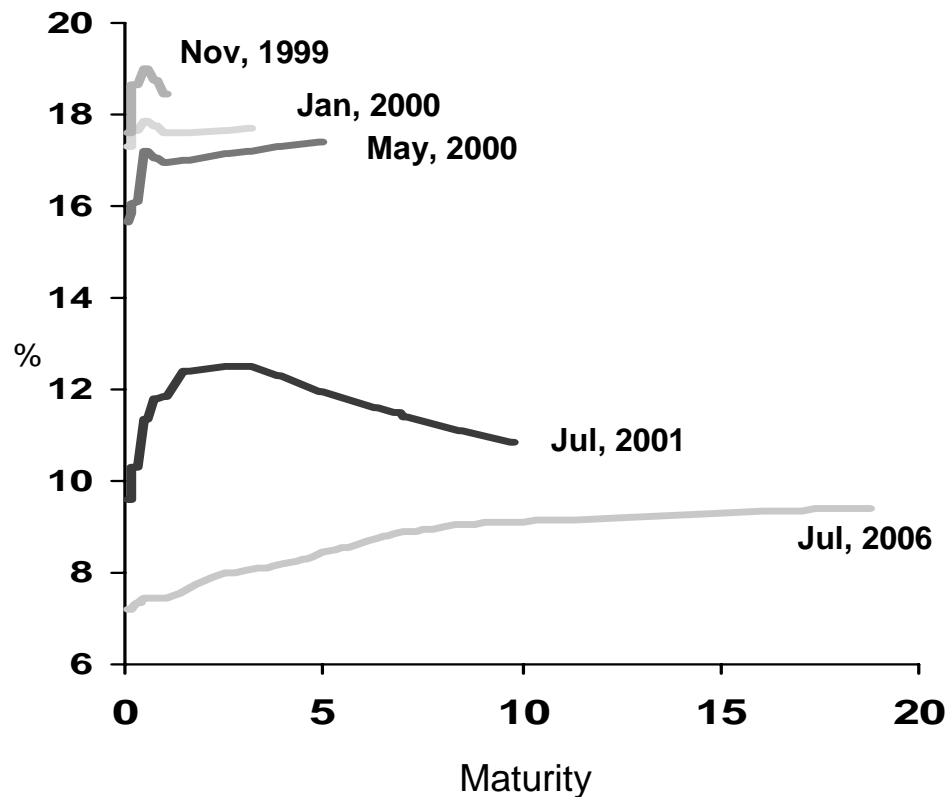
*/ The size of the bubble represents the amount issued.
Source: SHCP

3.- Development of local markets



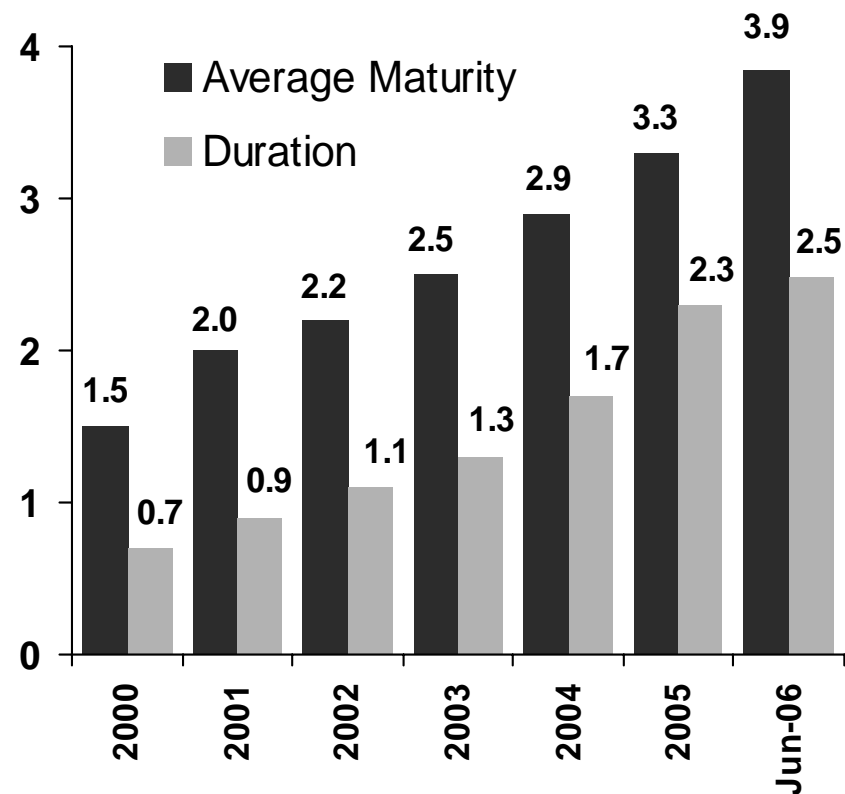
3.- Development of local markets

Yield Curve Evolution (%)



Source: SHCP

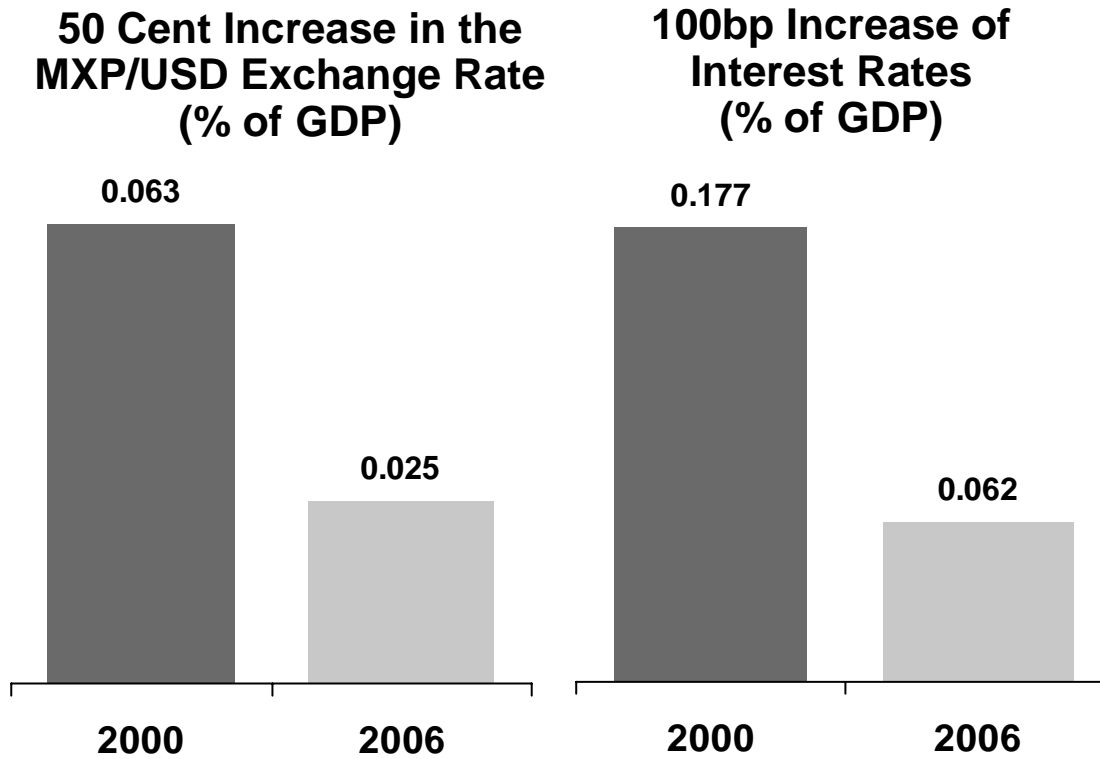
Average Maturity and Duration (years)



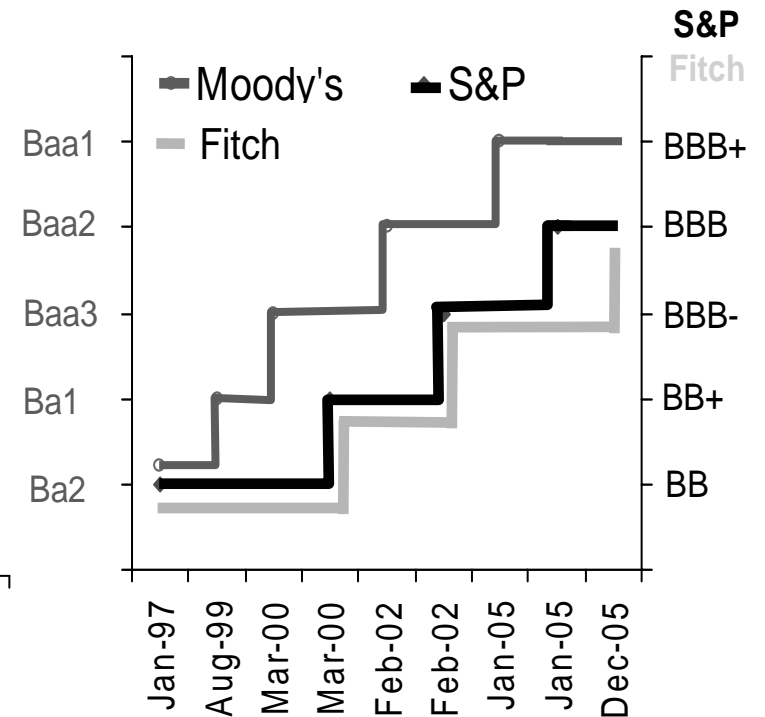
Source: SHCP

The vulnerability of public finances to unfavorable shocks has been reduced

Sensitivity of the Financing Cost of the Federal Government Debt

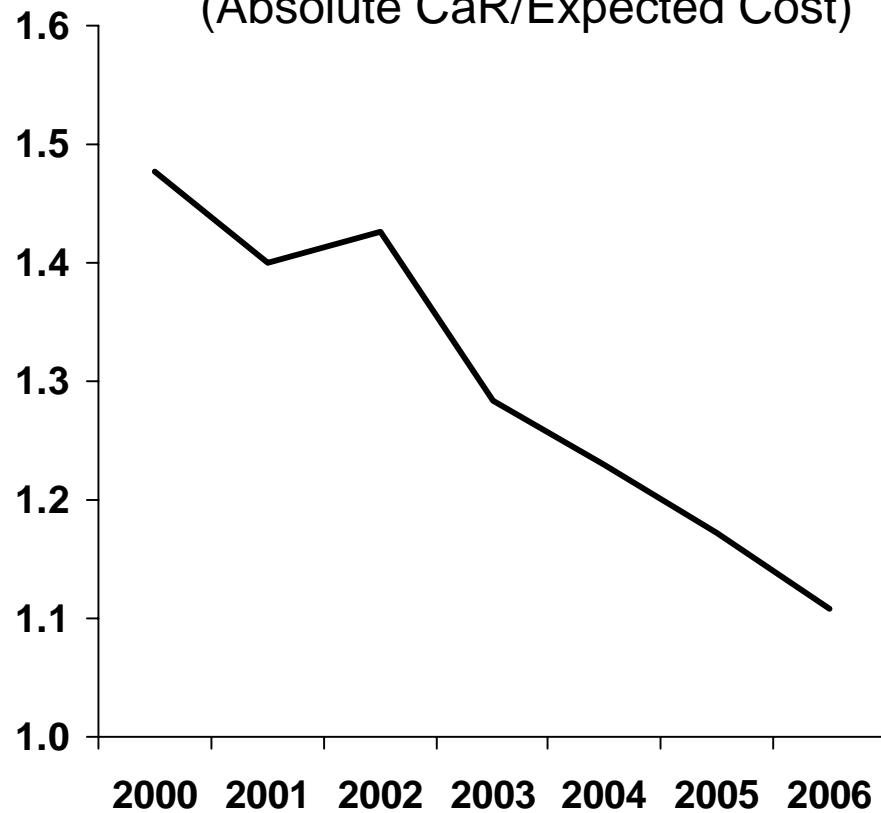


Ratings of Long-Term External Debt

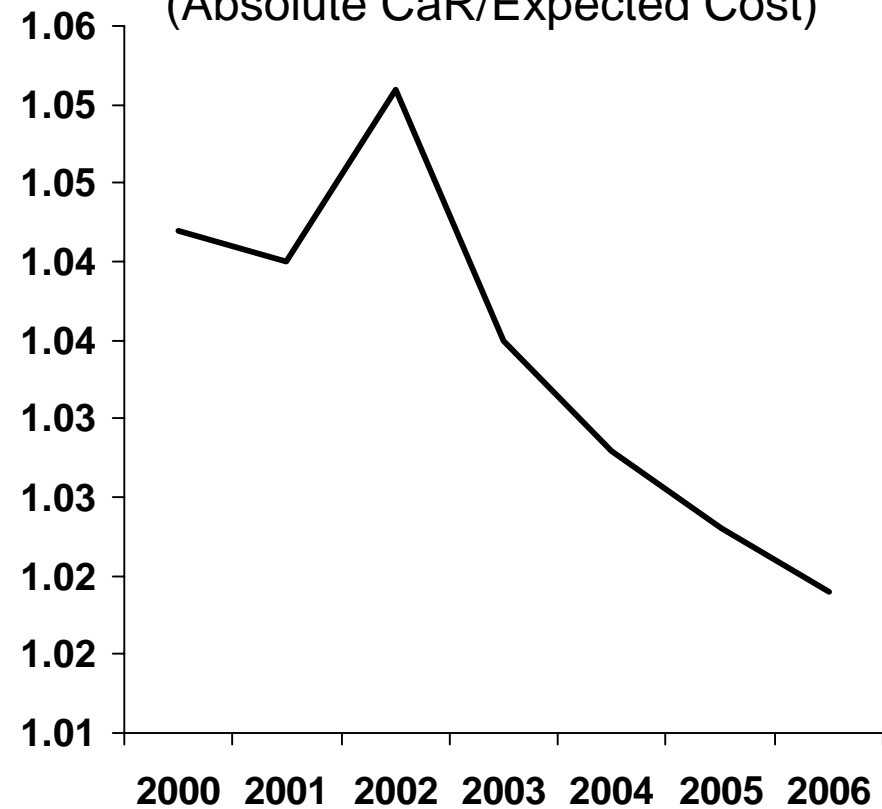


Risk measures have continued to decline

**Federal Government Debt:
Interest Rate CaR**
(Absolute CaR/Expected Cost)



**Federal Government Debt:
ExRate CaR**
(Absolute CaR/Expected Cost)





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A series of operations aimed at reducing the financing cost of public debt and maintaining an adequate risk level were carried out in 2005 and 2006

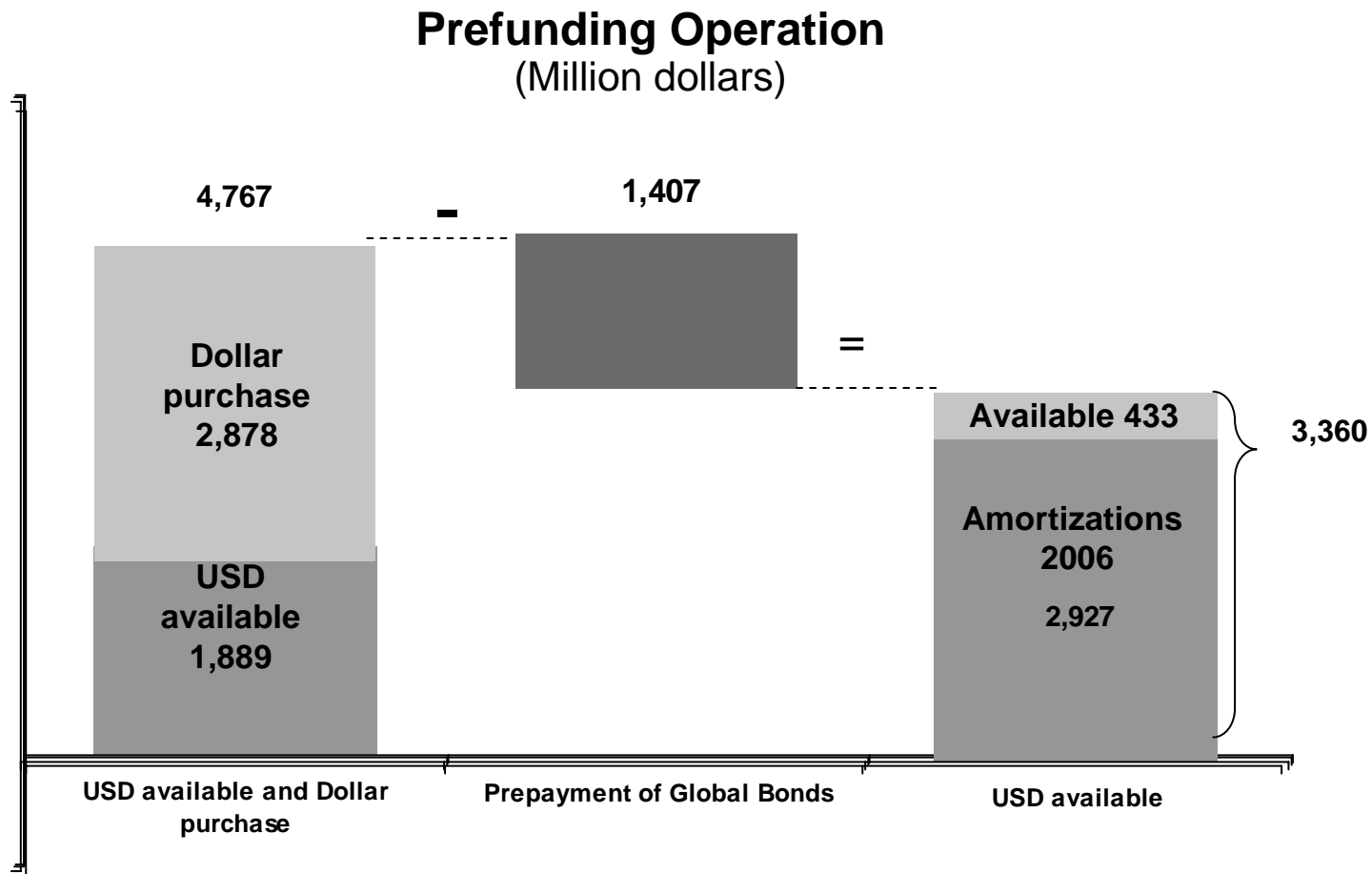
2005

- 1 Purchase of Dollars from the CB and Global Bonds Buyback**
- 2 First Issue of Debt Exchange Warrants (dollars)**

2006

- 3 Second Issue of Debt Exchange Warrants (euros)**
- 4 Bond Repurchase Offer and Placement of New Global Bond**
- 5 Prepayment of Debt with International Financial Institutions**

1. Purchase of Dollars from the CB and Global Bonds Buyback



2. Debt Exchange Warrants (dollars)

- ✓ This was the first-ever stand alone, cross-currency debt exchange warrant offering from a sovereign issuer.
- ✓ There was a demand for US\$11.5 billion, while the announced original offer was US\$1.5 billion. The issue size was increased to US\$2.5 billion.
- ✓ This transaction provided an efficient, frictionless mechanism to facilitate and accelerate two of the main debt objectives:
 - Reduce the share of debt in foreign currency
 - Promote an orderly development of the local market by increasing supply when market conditions are favorable

| Warrant Series | XW-5 | XW-10 | XW-20 |
|------------------|--|--|--|
| Old Bonds: | UMS 2007 UMS 2008 UMS 2009 UMS 2010 UMS 2011 | UMS 2012 UMS 2013 UMS 2014 UMS 2016 | UMS 2019 UMS 2022 UMS 2026 UMS 2031 UMS 2033 |
| Exchanged Bonds: | Mbono 2011 | Mbono 2014 | Mbono 2024 |
| Exercise Date | November 9, 2006 | October 10, 2006 | September 1, 2006 |

3. Debt Exchange Warrants (euros)

- ✓ Mexico issued warrants in euros in March 2006. The operation generated EUR€1.5 billion in demand, 2.5 times the EUR€600 million allocated.

| | |
|-----------------------------|--|
| Warrant Series: | XW-E |
| Old Bonds: | UMS EUR 2008 UMS EUR 2010 UMS EUR 2013 UMS ITL 2007 UMS ITL 2013 UMS ITL 2017 UMS DEM 2008 UMS DEM 2009 |
| Exchanged Securities | Mbono 2013 Mbono 2023 |
| Exercise Date: | Nov. 22, 2006 |

4. Bonds Repurchase and Placement of New Global Bond

- A new bond for US\$3 billion maturing in 2017 was issued. The operation was linked to an offer to repurchase bonds previously issued in international markets.
- The repurchase offer faced a demand for US\$11.7 billion.
- The operation increases the liquidity of sovereign debt in international markets, generated NPV savings, and increased the efficiency of the USD yield curve.

| USD bonds | Market Value (million dollars) | Non-USD bonds | Market Value (millions, orig cy) |
|-----------|-----------------------------------|---------------|-------------------------------------|
| UMS 2007 | 292.3 | ITL 2007 | 21.1 |
| UMS 2008 | 243.1 | EUR 2008 | 143.2 |
| UMS 2008 | 303.0 | DEM 2008 | 40.5 |
| UMS 2009 | 411.6 | DEM 2009 | 73.4 |
| UMS 2012 | 262.3 | EUR 2010 | 92.1 |
| UMS 2013 | 271.0 | ITL 2013 | 41.9 |
| UMS 2015 | 472.6 | EUR 2013 | 29.3 |
| UMS 2019 | 44.8 | ITL 2017 | 9.9 |
| UMS 2022 | 17.8 | GBP 2024 | 26.8 |
| UMS 2031 | 109.4 | | |

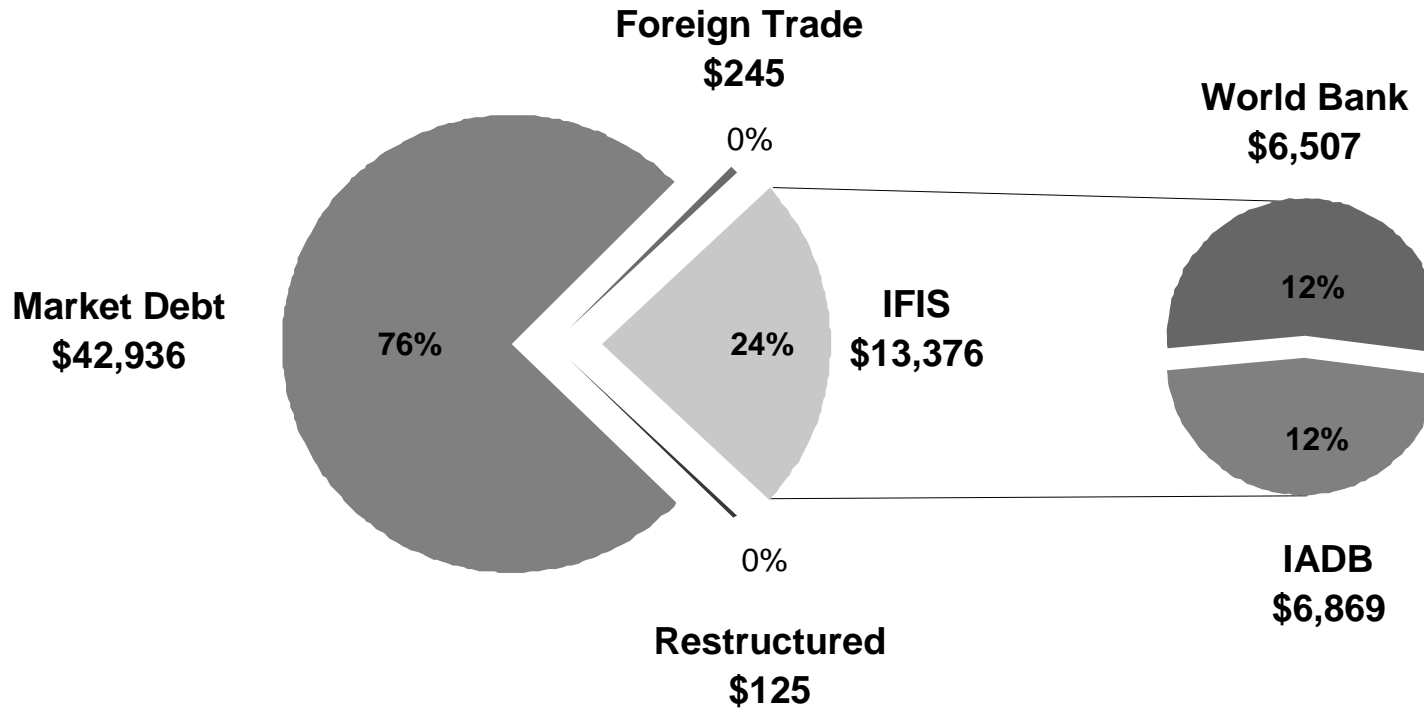


5. Prepayment of Debt with International Financial Institutions

- ✓ The Ministry of Finance will prepay several loans from the Inter-American Development Bank and the World Bank for an approximate amount of USD 9 billion.
- ✓ In order to carry out the prepayment, the Federal Government will purchase US dollars from the Central Bank's international reserve.
- ✓ The funds came from issuing securities in the local market with similar characteristics to the Central Bank's monetary regulation bonds (floating coupon rate).
- ✓ An equivalent amount of BREMS will be retired by the Central Bank in a concurrent transaction.

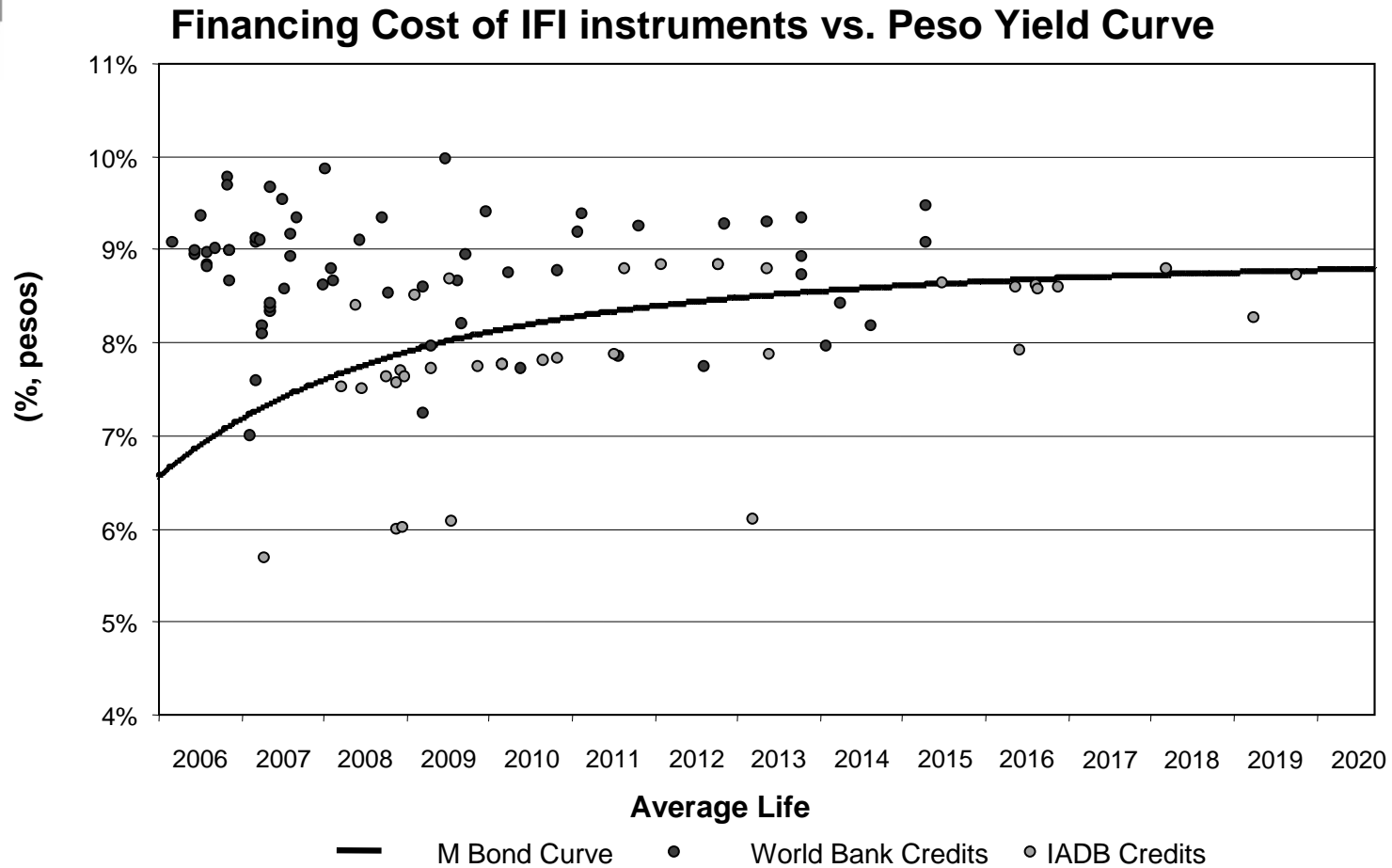
5. Prepayment of Debt with International Financial Institutions

Federal Government External Debt
(millions of dollars)



Source: SHCP

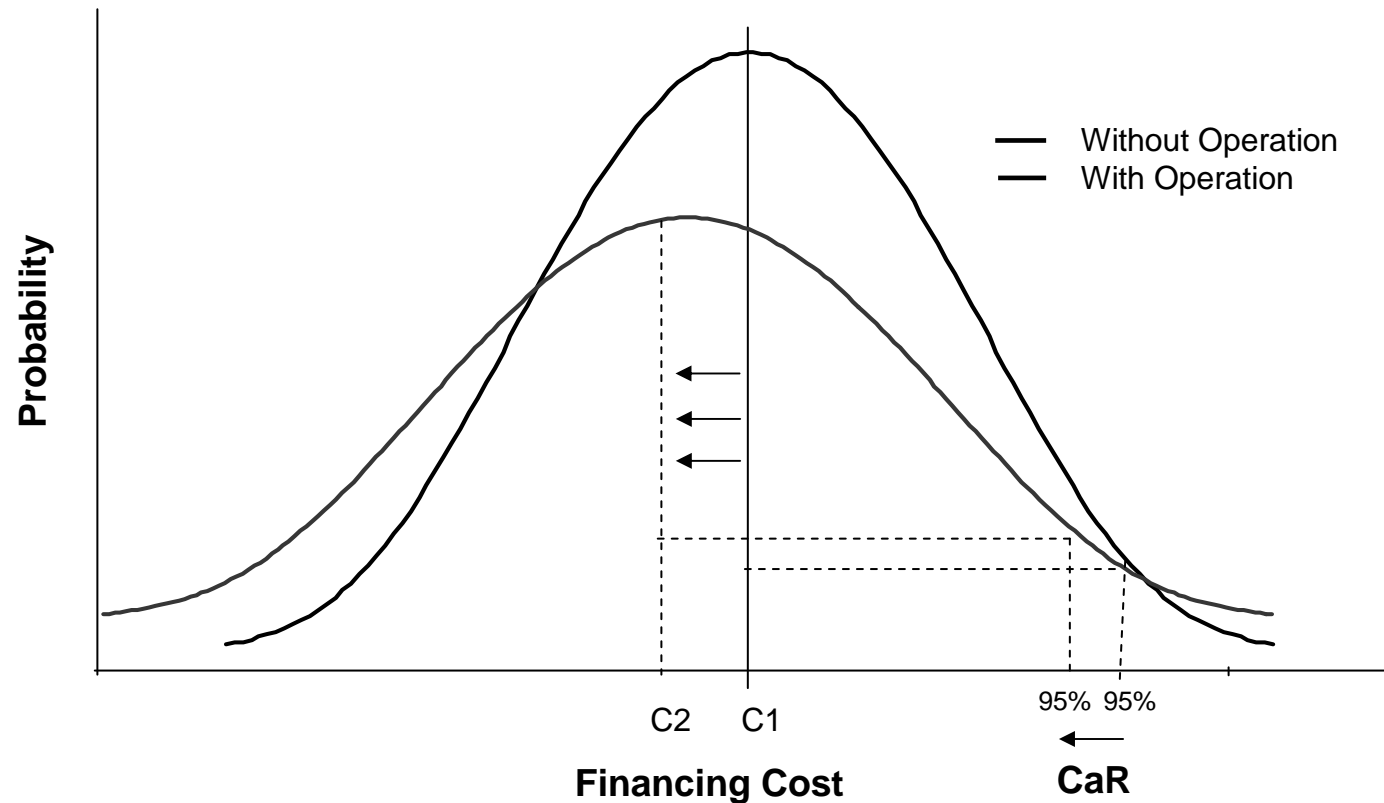
5. Prepayment of Debt with International Financial Institutions



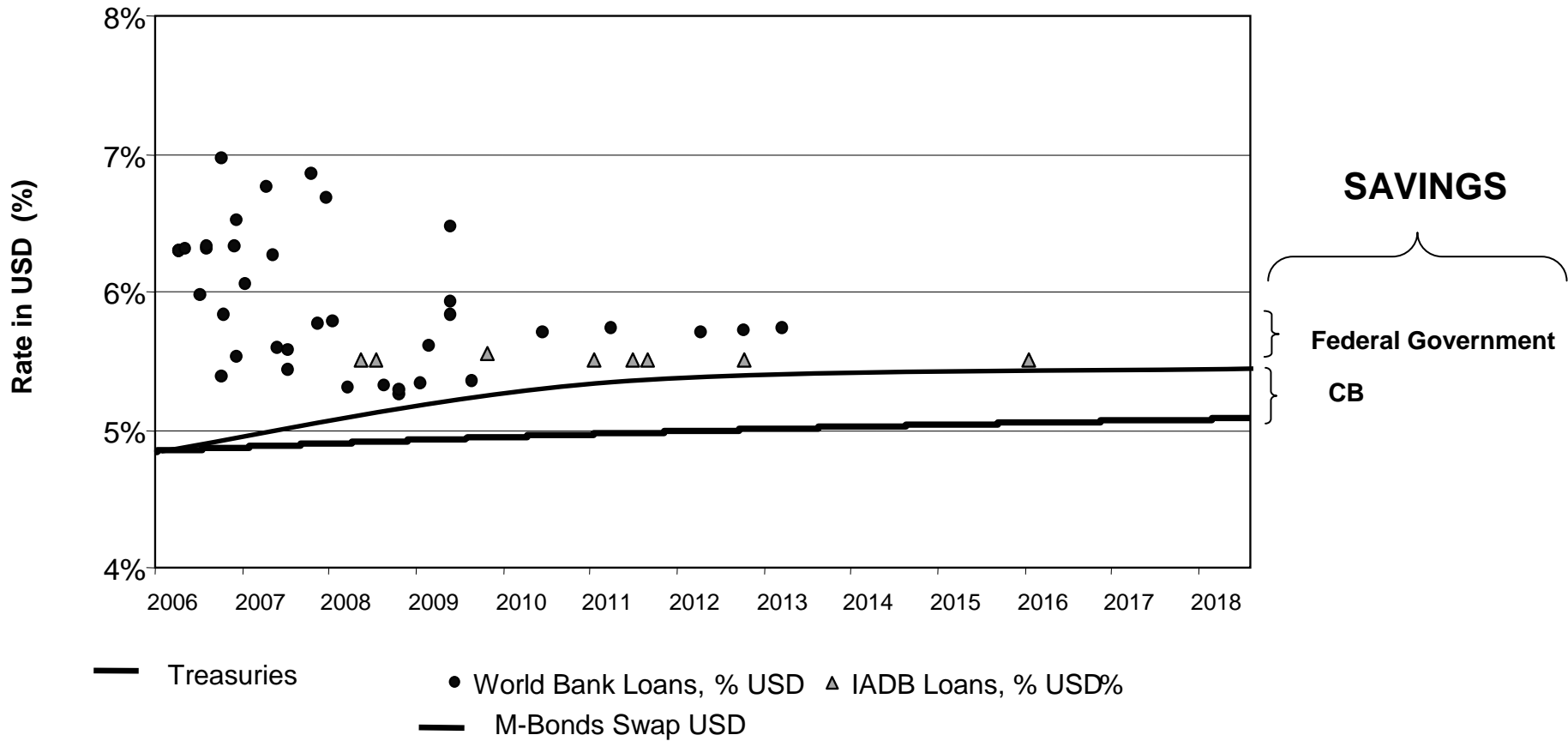
Outstanding amounts by February 28, 2006. Yield curves as of April 24, 2006.

5. Prepayment of Debt with International Financial Institutions

Distribution of Financing Cost
(Density function)



5. Prepayment of Debt with International Financial Institutions





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Public Debt Policy Guidelines

- The public debt management strategy followed in the last years has promoted macroeconomic and financial stability by reducing the vulnerability of public finances to adverse shocks.
- Liability management operations have been aimed at minimizing long-term financing costs and maintaining an adequate level of risk.
- Public debt policy will continue to pursue these broad guidelines, while focusing on the following:
 - 30-year peso-denominated bond
 - Strengthening benchmark references in the dollar and euro yield curves, while reducing external debt
 - Promoting a liquid repo and securities lending market in order to continue developing the local market
 - Keep strengthening the institutional framework for public debt management



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