MINISTRY OF FINANCE
MEXICO

November 6, 2003

THE EXECUTIVE SUBMITTED TO CONGRESS THE ECONOMIC PROGRAM FOR 2004

- Fiscal and monetary discipline has resulted in inflationary abatement while interest rates continue to fall. As a result, real wages and credit to the private sector have expanded. These have been the main determinants of the increase in personal consumption expenditures which has smoothed the downturn. Resilient consumption expenditures have resulted from an economic policy which aims to support a recovery of domestic sources of growth while preserving financial stability in Mexico.

- GDP growth for 2003 is expected at 1.5 per cent. This figure is lower than originally expected when the economic program for the year was published. The former, results from the lack of dynamism of manufacturing in the United States (US), and the reduction of Mexican exports' share in total US imports.

- The estimated public deficit for 2003, excluding the expenditures associated to the voluntary retirement program for public workers, is below the 0.5 per cent of GDP target set by Congress.

- Fiscal discipline will continue to be the backbone of the macroeconomic strategy in 2004. The fiscal deficit's target for the year will be 0.3 per cent of GDP, and estimated Public Sector Borrowing Requirements (PSBR) are 2.7 per cent of GDP.

- The macroeconomic framework for 2004 is prudent. Estimated GDP growth for 2004 is 3.1 per cent, December-December inflation is expected to be 3.0 per cent, and the current account deficit is anticipated at 16.4 billion USD.

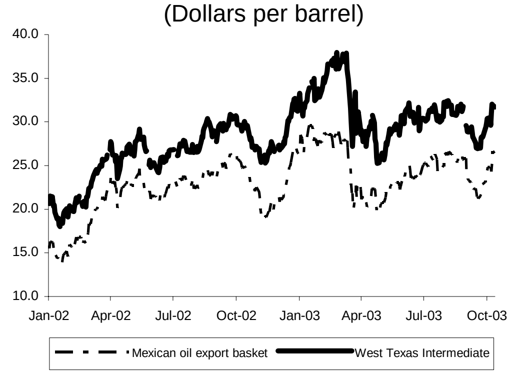
The International Economy in 2003

In spite of the moderate global recovery in 2003, global industrial production has lagged behind, not posting the growth rates that were anticipated earlier in the year.

The US economy is expected to grow at a 2.8 per cent rate in 2003, and to record an annual inflation slightly above 2 per cent. Some of the largest economies of the euro zone have stagnated, and even contracted; in 2003 the region will probably grow less than 1 per cent. The Japanese economy, in contrast, has registered a rebound but the structural issues in its financial and productive sectors, as well as the difficulty of eliminating deflation, generates uncertainty about the sustainability of the recovery.

Adjustments in international oil markets were lesser than anticipated after the first quarter of 2003, when geo-political uncertainty dissipated. As a result, oil prices were higher than anticipated at the beginning of the year.

OIL PRICES
(Dollars per barrel)



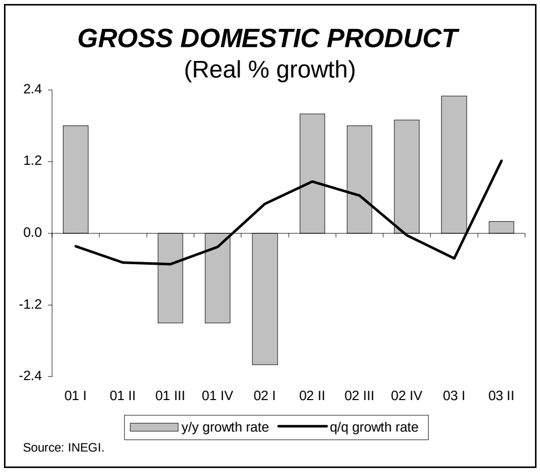
Source: Bloomberg and Pemex.

Ample global liquidity and the reduction of geopolitical risks resulted in a decrease in risk aversion in international financial markets during the second quarter of 2003. This willingness to buy risky assets resulted in a reduction of corporate as well as sovereign spreads. The BBB corporate spread and the Mexican EMBI+ spread contracted by over 100 basis points in the first ten months of 2003.

Foreign Direct Investment (FDI) flowing into emerging markets have been redirected towards Asia. Consequently, FDI flows into Latin American economies were lower than the amounts observed in recent years. Mexico, however, continued to attract a growing share of the FDI bound for Latin America.

Evolution of the Mexican Economy during 2003

GDP grew at an average rate of 1.2 per cent in the first half of 2003. The sub-par performance of economic activity is the result of lackluster industrial production, mainly in the manufacturing sector. In contrast, the performance of those economic sectors which are linked to domestic demand has been favorable. This rotation in the sources of growth is the result of a prudent policy framework which has strengthened domestic demand using prudent macroeconomic policies and microeconomic policy instruments.



GDP growth during the first half of the year resulted from domestic expenditure growth, primarily from private consumption and public investment. For that reason, the non-tradable goods sectors, which satisfy domestic demand, were better off in early 2003 than externally oriented sectors.

AGGREGATE SUPPLY AND DEMAND, 2002-2003 [1/]

(Real annual growth)

	Annual	Jan - Jun		2002				2003	
	2002	2002	2003	I	II	III	IV	I	II
Supply	1.1	-0.2	0.2	-2.8	2.4	2.6	2.1	1.9	-1.3
GDP	0.9	-0.1	1.2	-2.2	2.0	1.8	1.9	2.3	0.2
Imports	1.6	-0.5	-2.4	-4.5	3.5	4.8	2.5	0.8	-5.2
Demand	1.1	-0.2	0.2	-2.8	2.4	2.6	2.1	1.9	-1.3
Consumption	0.9	0.5	2.2	-1.5	2.5	1.7	0.8	3.3	1.1
Private	1.2	0.8	2.2	-1.6	3.1	2.0	1.2	3.6	0.9
Public	-1.3	-1.5	2.0	-1.1	-1.7	-0.8	-1.3	1.1	2.8
Capital Formation	-1.3	-2.1	-1.6	-6.9	2.8	-0.8	0.0	0.6	-3.6
Private	-2.8	-2.3	-4.6	-5.9	1.3	-1.5	-5.2	-1.7	-7.4
Public	7.3	-0.6	19.5	-13.2	13.8	3.6	18.6	16.7	22.1
Exports	1.4	-1.8	0.0	-6.7	3.1	6.0	3.4	3.9	-3.5

Source: INEGI.

As mentioned earlier, industrial activity in the US has not recovered as expected during the current economic expansion. Accordingly, the Mexican export market grew less than anticipated. Furthermore, the Mexican market share in US imports has fallen recently, contrasting with the performance of China. In this context, the expected growth rate of the Mexican economy for 2003 was reduced significantly.

ESTIMATES FO THE END OF 2003	
Gross Domestic Product	
Real growth (%)	1.5
Inflation	
Dec./Dec.	3.8
Current Account	
% of GDP	1.9

The estimated fiscal deficit for 2003, excluding expenditures related to the early retirement program for public employees approved by Congress in the Budget for the year, is below the 0.5 per cent of GDP target. If the additional expenditure related to the early retirement program is considered the fiscal deficit estimate is 0.6 per cent of GDP.

Fiscal revenues results estimated for 2003 are primarily explained by the following:

- Budgetary revenues are expected to be higher than anticipated, due to favorable developments in oil revenues, as well as to higher earnings from Public Entities under Direct Budgetary Control (PEDBC) unrelated to the oil industry.

- Non-oil tax revenues will be slightly lower than expected in the 2003 budget. Negative effects on revenues are explained by the Supreme Court's ruling on the substitutive tax to the salary credit and from the modifications of several fiscal laws approved by Congress for 2003. In contrast, the revenue form the value-added tax is expected to increase 8.4 per cent in real terms, exceeding the budgeted amount by almost 25 billion pesos.

- Non-tax revenues are expected to overshoot the programmed amount as a result of higher-than-expected non-recurrent revenues.

Programmable expenditures in 2003:

- Are expected surpass the approved amount by 59.2 billion pesos, primarily resulting from additional expenditures triggered by higher revenues, as well as by the early retirement program for public sector employees. Additional expenditures were directed to cover: the energy costs of electricity generation; infrastructure for States and Municipalities; deposits in the oil-stabilization fund; to capitalize a state owned development bank (BANOBRAS); and, to increase the expenditure cap of those public entities and dependencies which generated additional revenues. All of the aforementioned additional expenditures were carried out in accordance to the Budget approved by Congress for 2003.

- The fiscal expenditures linked to social development, poverty reduction and productive infrastructure benefited the most. Furthermore, resources directed to states and municipalities through revenues sharing, transfers (items 25 and 33), decentralized expenditure agreements, and the Program to Support the Strengthening of Federal Entities (PAFEF) increased 1.5 per cent in real terms.

In 2003, the Public Sector Borrowing Requirements are expected to be equivalent to 3.0 per cent of GDP, including the expenditure associated to the early retirement program for public employees.

PUBLIC SECTOR BORROWING REQUIREMENTS, 2002-2003 (% OF GDP)				
	2002	2003		
		Approved	Estimate	Difference
I. Traditional Public Sector Deficit */	**1.2**	**0.5**	**0.6**	**0.1**
A. Budgetary Revenues	22.6	22.4	23.3	0.9
Oil related	6.7	7.1	7.8	0.7
Non-oil related	15.9	15.4	15.5	0.2
Tax related	10.0	10.2	10.1	-0.1
Non-tax related	1.8	1.2	1.3	0.1
Entities and enterprises	4.0	3.9	4.1	0.1
B. Net Budgetary Expenditures	23.9	22.9	23.9	1.0
Programmable expenditures*/	17.3	16.5	17.4	0.8
Non programmable expenditures	6.6	6.4	6.5	0.2
Financing costs	2.9	2.8	2.9	0.1
Revenues sharing	3.5	3.4	3.3	-0.2
Adefas and others	0.2	0.1	0.3	0.2
C. Budgetary	-0.1	0.0	0.0	0.0
II. Adjustments	**1.4**	**2.5**	**2.4**	**0.0**
PIDIREGAS	0.8	1.4	1.3	-0.1
IPAB	0.5	0.3	0.3	0.0
Budgetary adjustments	0.2	0.1	0.1	0.0
Debtor support programs	-0.1	0.0	0.0	0.0
FARAC	0.4	0.2	0.1	-0.1
Financial intermediation	-0.4	0.4	0.6	0.2
III. PSBR (I+II)	**2.6**	**3.0**	**3.0**	**0.0**
Excluding Non-Recurrent Revenues	**3.4**	**3.4**	**3.6**	**0.2**

*/ Estimated figures for the close of 2003 include expenditures related to the Voluntary Retirement Program.

Policy Guidelines for 2004

The main challenge for 2004 will be generating the macroeconomic conditions for a recovery and increase formal employment. In order to achieve that, it will be necessary to push through the agenda of structural reforms and to consolidate the macroeconomic stability achieved so far.

Regarding the structural reform agenda, it should be noted that the efforts should concentrate on achieving the necessary consensus to advance in the fiscal, electric, and pension reforms. Additionally, the Mexican government will continue to consolidate its trade openness, through the simplification and modernization of customs, as well as through better trade infrastructure.

On the subject of consolidating the macroeconomic stability attained, it is worth mentioning the following issues related to fiscal policy:

- Prudent and disciplined fiscal management will reduce uncertainty and will generate incentives for investment projects by corporations and individuals. Incentives to invest will result from fiscal policy actions which help inflationary abatement, reduce crowding out in domestic financial markets, avoid interest rate increases, and give certainty to business earnings forecasts.

- The reorientation of fiscal expenditure will benefit those productive projects which, by nature, have the largest impact on payrolls.

Fiscal policy will reaffirm its commitment to gradually reducing the fiscal deficit, by setting a 0.3 per cent of GDP target for 2004. Nevertheless, non-recurrent and oil revenues continue to play an important role in the Mexican fiscal accounts. Public expenditure would have to be adjusted if these non-recurrent revenues fail to materialize in the amounts that have been budgeted.

For that reason, the Expenditure Budget of the Mexican Federation contemplates expenditure adjustment mechanisms that would become binding if public revenues evolve differently from what has been budgeted. These mechanisms adjust expenditures while preserving it in strategic areas such as education, health, equal opportunities, rural development and infrastructure.

The PSBR estimated for 2004 are equivalent to 2.7 per cent of GDP considering the following:

- An annual increase in investment through PIDIREGAS of more than 28 percent in real terms.

- An increase in the resources available for financing the private sector through development banks and funds, prioritizing mortgage financing.

- A reduction in IPAB and FARAC financing requirements.

Estimated public sector revenues for 2004, excluding financial intermediation, amount to 22.5 percent of GDP. The former is explained by:

- A significant decline in oil-related revenues due to a fall in international oil prices.

- A 0.2 percent of GDP decline in tax revenues explained by the reduction in tariffs related to the various trade treaties the Country has signed, as well as the elimination of the substitutive tax to the salary credit.

Regarding Programmable expenditures:

- These will decline by 4.0 percent in real terms with respect to the end of 2003.
- However, within programmable expenditures, social spending will be prioritized, experiencing a one percent real annual increase.

Overall public sector fixed capital investment ("impulsed investment") will total 3.7 percent of GDP, mainly concentrating on infrastructure provision.

ESTIMATION OF PUBLIC FINANCES FOR 2003-2004					
	Millions of pesos		% of GDP		Real.
	2003	2004	2003	2004	Growth
Economic Balance excluding VRP [1]	**-26,918.6**	**-24,093.0**	**-0.4**	**-0.3**	**-14.1**
Economic Balance including VRP [1]	**-37,918.6**	**-24,093.0**	**-0.6**	**-0.3**	**-39.0**
Non-budgetary balance	1,092.8	0.0	0.0	0.0	0.0
Budgetary balance	-39,011.4	-24,093.0	-0.6	-0.3	-40.7
Budgetary revenues	1,538,421.4	1,594,562.4	23.3	22.5	-0.5
Oil-related	514,467.7	502,988.7	7.8	7.1	-6.2
Federal Government	358,475.2	350,001.5	5.4	4.9	-6.3
PEMEX	155,992.5	152,987.2	2.4	2.2	-5.9
Non-oil related	1,023,953.7	1,091,573.7	15.5	15.4	2.3
Federal Government	755,128.2	804,050.5	11.4	11.3	2.2
Tax	667,627.7	703,543.0	10.1	9.9	1.1
Non-tax	87,500.5	100,507.5	1.3	1.4	10.2
Entities and enterprises [2]	268,825.5	287,523.2	4.1	4.1	2.6
Expenditures	1,577,432.8	1,618,655.4	23.9	22.8	-1.5
Programmable [3]	1,147,026.8	1,147,405.0	17.4	16.2	-4.0
Differed payments	-18,421.3	-18,400.0	-0.3	-0.3	-4.1
Programmable accrued expenditures	1,165,448.1	1,165,805.0	17.7	16.5	-4.0
Non programmable	430,406.0	471,250.4	6.5	6.7	5.1
Financing costs	194,532.6	216,908.2	2.9	3.1	7.0
Revenues sharing	215,336.2	239,830.4	3.3	3.4	6.9
Adefas and others	20,537.2	14,511.8	0.3	0.2	-32.2
Public Sector Financing Costs [4]	**195,362.2**	**217,737.8**	**3.0**	**3.1**	**7.0**
Primary Economic Surplus	**157,443.6**	**193,644.7**	**2.4**	**2.7**	**18.0**

1/ VRP stands for Voluntary Retirement Program.
2/ For the purpose of comparison figures for 2003 exclude revenues and expenditures related to LOTENAL and CAPUFE.
3/ Figures for 2003 include payments related to the Voluntary Retirement Program.
4/ Includes the financing costs of public budgetary debt and Public Entities under Indirect Budgetary Control (PEIBC).

Regarding public debt policy, the following is being proposed:

- Take advantage of favorable domestic market conditions to improve the composition of public debt, decreasing reliance on external financing. In particular, for the first time in recent Mexican history, the economic program presented by the

Executive proposes to reduce net external indebtedness by US 500 million in 2004.

- Continue with the liability management strategy, that seeks to improve the terms, structure and composition of public debt, as well as to broaden the investor base.

Economic Perspectives for 2004

The macroeconomic framework for 2004 is based on the following international assumptions:

- Real US GDP growth of 3.8 percent, and a real 4.0 percent expansion of manufacturing production in the same country.

- An average oil price of 20 US dollars per barrel.

The international oil price is expected to decline from its relatively high current levels during 2004. An orderly adjustment in the price is foreseen, given expectations of a marginally larger international oil supply with respect to demand; as well as continued supply adjustments by OPEC in order to assure that prices will remain within their target limits.

Additionally, an adequate availability of external financing for emerging markets is expected, given higher levels of global economic growth.

The economic policy strategy is geared towards strengthening internal sources of growth, the reactivation of investment spending, and to the continued expansion of consumption. The real annual expansion rate of GDP is expected at 3.1 percent.

AGGREGATE SUPPLY AND DEMAND, 2003-2004 e/						
	Real Annual Growth		Composition %		Contribution to Growth	
	2003	2004	2003	2004	2003	2004
Supply	0.9	3.3	136.6	136.8	1.2	4.4
GDP	**1.5**	**3.1**	**100.0**	**100.0**	**1.5**	**3.1**
Imports	-1.0	3.7	36.6	36.8	-0.4	1.4
Demand	0.9	3.3	136.6	136.8	1.2	4.3
Consumption	2.3	3.2	81.5	81.6	1.9	2.6
Private	2.3	3.6	72.0	72.3	1.6	2.6
Public	2.4	0.0	9.6	9.3	0.2	0.0
Capital Formation 1/	0.5	4.0	19.1	19.3	0.1	0.8
Private	-1.0	5.1	15.7	16.0	-0.2	0.8
Public	7.9	-1.0	3.4	3.2	0.2	0.0
Exports	-0.3	4.3	33.6	34.0	-0.1	1.4

1/ Does not include changes on inventories.
e/ Estimated
Source: SHCP.

Regarding external risks, it is worth highlighting the following:

- A significantly lower rate of economic activity in the US.
- Increased external competition, accompanied by a lower impact of US recovery on national manufacturing exports.
- A lower than expected international oil price.
- An unforeseen increase in international interest rates, accompanied by a deterioration of capital market access for emerging markets.

In the domestic front, risks include:

- Deterioration in the industrial cycle link between Mexico and the United States.
- A slower than expected recovery in investment spending by the private sector.
- Declining economic growth expectations, resulting from stagnation in the structural reform front.

Medium Term Evolution of Public Finances

Economic Outlook for 2004-2007

The assumptions used for developing the macroeconomic framework are detailed below:

SUPPORT VARIABLES, 2002-2007						
	2002	**2003*/**	**2004**	**2005**	**2006**	**2007**
US GDP (real % growth)	2.4	2.8	3.8	3.3	3.4	3.5
US Industrial Production (real % growth y/y)	-0.8	0.2	4.0	4.0	5.0	5.0
US Inflation (% annual variation)	2.4	2.1	1.8	2.5	2.5	2.5
LIBOR 3 month (Annual average rate)	1.8	1.2	2.5	3.5	4.5	5.5
Oil price (Annual average price)	21.5	24.2	20.0	16.7	17.1	17.5

*/ Estimates from 2003 onwards
Source: SHCP.

The expected economic growth rate for the 2005-2007 period is 4.4 percent, as well as a moderate increase in the current account deficit.

MACROECONOMIC VARIABLES, 2002-2007						
	2002	2003*/	2004	2005	2006	2007
Gross Domestic Product						
Real annual growth	0.9	1.5	3.1	4.2	4.5	4.6
Inflation						
Dec / Dec	5.7	3.8	3.0	3.0	3.0	3.0
Interest rate						
Nominal rate	7.1	6.5	6.5	5.9	6.7	7.1
Real accumulated rate	1.5	2.7	3.6	3.0	3.7	4.3
Current account						
% of GDP	-2.2	-1.9	-2.6	-2.7	-2.8	-3.0

*/ Estimates from 2003 onwards
Source: SHCP.

Public Finance Perspectives for 2004-2007

Adequate public finance management resulted in the fulfillment of the fiscal objectives set forth in the Pronafide and the Economic Policy Guidelines for 2002 and 2003. Responsible fiscal policy, especially under an adverse macroeconomic situation, improved the perception of economic agents about the future evolution of public finances as well as on the main financial variables.

Medium Term Financial Pressures

This section describes and analyzes the main expenditure and revenue pressures, with the purpose of determining the necessary adjustments to achieve the objectives set forth in terms of fiscal results and public indebtedness.

On the revenue side:

- A decline in oil-related and non-recurrent revenues is expected, with respect to the levels recorded during 2003.

On the expenditure side:

- The expected increase in expenditures related to pensions, to Pidiregas projects and to personnel services.

Considering the decline in public sector revenues and increased expenditures in a joint manner, we conclude that public finances will undergo pressures equivalent to an amount between 1.5 and 2.0 percent of GDP as compared to the year 2003.

Considering the fundamental social expenditures the Federal Government will be forced to face these pressures are even higher. Between these social expenditures we can highlight the following:

- Expenditures necessary to cover the deficiencies in the health sector mentioned in the General Health Law (Ley General de Salud), and in particular, those public resources destined to the Public Health Insurance (Seguro de Salud Popular)

- Resources channeled to the Oportunidades program.

- The amount of resources required to meet the 8 percent of GDP destined to the education sector by 2006, which were set by Congress.

- The funds required for rural development.

- To meet a series of accumulated shortfalls in public infrastructure.

Based on the analysis of medium term fiscal perspectives, it is necessary to carry out an adjustment to the tax structure in order to increase public sector revenues, to restructure and increase available funds in order to satisfy the needs in terms of social and investment expenditures, as well as to solidify the fiscal stance.

In case a fiscal reform that increases available resources is not carried out, the authorities will be forced to choose between carrying out expenditure cuts, or increasing public debt. In the first case, the government will need to: a) reduce the amount of resources available for social public spending, b) carrying out cuts on investment on education and infrastructure provision, and c) cutting back on the quality and availability of some public services. On the other hand, in case authorities decide to increase indebtedness, conditions in financial markets will deteriorate, generating increases in interest rates, currency devaluations, increased restrictions on the availability of financing, volatility in financial markets, deteriorating real wages, increases in the unemployment rate, and a significant deterioration in growth, income distribution and poverty, which, paradoxically, will be accompanied by lower public expenditures.

Because of the reasons detailed above, the Executive has sent a Fiscal Reform proposal to Congress for its consideration. The objective of the Fiscal Reform is to provide the Government with the resources necessary to meet the countries social and economic needs, while promoting economic development and employment creation.

Annex

MACROECONOMIC FRAMEWORK, 2003-2004 e/		
	2003	**2004**
Gross Domestic Product		
Real % growth	1.5	3.1
Nominal (billion pesos)	6,595.8	7,086.2
GDP deflator	5.6	4.2
Inflation		
Dec./Dec.	3.8	3.0
Nominal exchange rate */		
Average	10.7	11.2
Interest Rates (28 day Cetes)		
Average Nominal, %	6.5	6.5
Real, %	2.7	3.6
Current Account		
Millions of dollars	-11,847.0	-16,419.9
% of GDP	-1.9	-2.6
Public Balance		
% of GDP	-0.5	-0.3
Support Variables:		
US GDP		
Real % growth	2.6	3.6
US Industrial Production		
Real % growth	0.2	4.0
US Inflation		
Dec./Dec.	2.1	1.8
Oil (Mexican basket)		
Average price (dls / Barrel.)	24.2	20.0
Average export platform (mb/d)	1,849	1,959
Foreign interest rate		
LIBOR, %	1.2	2.5

e/ Estimated.