

BANKING REGULATION IN MEXICO: LESSONS FROM FINANCIAL CRISES*

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ABSTRACT. This article first provides a survey of recent Mexican banking history. It then analyzes the causes that led to the peso crisis (1995) and the banking crisis that came after as well as the government response, the bank bailout, and the role of international financial organizations. Regulatory reforms of the Mexican financial system are also discussed. These provide the background for comparative analysis with the financial crisis (2007-2009) that initiated in the United States of America. Both crises are compared and contrasted, both in terms of the causes leading to them and the regulatory responses by the governments. Finally, by studying the similarities and differences, lessons are drawn from both cases.

KEY WORDS: *Banking regulation, Financial crisis, Bank bailouts, Mexican peso crisis, U.S. financial crisis.*

RESUMEN. *El presente artículo versa sobre la historia reciente del sistema bancario mexicano. Se analizan las causas que originaron la crisis del peso (1995) y la subsecuente crisis bancaria. También se analizan las medidas tomadas por el gobierno ante el fallo del sistema bancario, así como el papel desempeñado por las organizaciones financieras internacionales. Lo anterior sirve como telón de fondo para realizar un análisis comparado con la crisis financiera de los Estados Unidos (2007-2009). Ambos episodios son comparados en términos de las causas que los originaron, así como las medidas regulatorias impuestas por los respectivos gobiernos. Finalmente, del análisis del contraste entre las semejanzas y diferencias de ambos casos, se infieren recomendaciones generales para aplicar en casos similares.*

PALABRAS CLAVE: *regulación financiera, crisis financiera, rescate bancario, crisis del peso mexicano, crisis financiera estadounidense.*

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I. INTRODUCTION

Over the last decade, the impact of globalization on financial markets, specifically banking, has led to an increased need to understand financial systems throughout the world. This article seeks to examine the Mexican financial system, and specifically the banking sector. It first addresses the recent evolution of banking history in Mexico, covering recent significant events. In doing so, it follows the changes in economic policy, particularly in trade and investment, to analyze the effects of a more liberalized market in the banking sector. The second part of this article examines the Mexican Peso Crisis, the bank bailout, and the effects these events have had on regulation. In the third section, the global financial crisis of 2007-2009 is studied and compared with the Mexican experience of 1995. Finally, past and recent experiences are used to draw lessons from the different responses to financial crises.

II. THE EVOLUTION OF MEXICAN BANKING

In Mexico, the development and regulation of the banking sector have had several phases.¹ The recent history of Mexican banking, which will be ad-

¹ For an in depth analysis of the different phases in the development of Mexican banks, see KAREN B. SIGMOND, *MEXICAN BANKING LAWS, EVOLUTION INTO NAFTA AND THE GLOBAL ECONOMY*, VDM Verlag (2008).

dressed for purposes of this paper, begins with the expropriation of the banks in 1982. Several decades of expansion in banking from the 1940s-1960s, during the “Mexican Economic Miracle,” had led to robust growth in this sector.² The total assets of private institutions in the banking system “grew by 3,259 percent from 1940 to 1960, from 845.8 million pesos to 28, 412.9 million pesos.”³ However, the decade that followed brought inflation and a slowdown in the economy. Inflation went from 3.91% in 1970 to 24.79% in 1976.⁴ Other factors such as government overspending, a series of devaluations, and capital flight began to complicate the economic outlook at the end of the 1970s. In banking, a series of mergers took place,⁵ and despite the worsening economic conditions, “the profits of the four principal banks increased in pesos, more than 1156% from 1977 to 1982.”⁶ By 1982, the government was facing an economic crisis and someone had to be blamed. As capital flight increased, the government turned its attention to the banks. On September 1, 1982, 58 out of the 60 banks in Mexico were nationalized by the Mexican government.⁷

The José Lopez-Portillo (1976-1982) administration “nationalized its banking system to stem the flight of wealth from Mexico and to provide Mexicans with greater access to capital. President Lopez-Portillo contended that Mexico’s economic crisis had been exacerbated by the greed of private banks and the lack of central control over the nation’s banking system.”⁸ With this action, decades of banking development and expertise came to a screeching halt.

The next administration, Miguel de la Madrid (1982-1988), “faced the sobering prospect of inheriting the leadership of a country beset with economic problems so serious that they threatened to disrupt social order.”⁹ “As early as his second day in office, he sent a bill to the Congress to open a new ‘economic chapter’ in the constitution [...] But, only three months after the expropriation of private banks, this measure was seen as one following the

² See LEOPOLDO SOLÍS, *EVOLUCIÓN FINANCIERA DE MÉXICO (MEXICAN FINANCIAL EVOLUTION)* 43 (1967).

³ Sigmond, *supra* note 1, at 39.

⁴ INSTITUTO NACIONAL DE ESTADÍSTICA, GEOGRAFÍA E INFORMÁTICA (INEGI, National Institute for Statistics, Geography and Informatics), <http://www.inegi.gob.mx/inegi/> (last visited May 10, 2010).

⁵ From 1975 to 1982, the number of banks dropped from 139 to 60. See SIGMOND, *supra* note 1, at 43.

⁶ Carlos M. Nalda, *Nafta, Foreign Investment, and the Mexican Banking System*, 26 *GEO. WASH. J. INTL’L, L & ECON.* 379, 385 (1992).

⁷ Decreto que Establece la Nacionalización de la Banca Privada (Nationalization Decree), *Diario Oficial de la Federación* [D.O.], Sept. 1, 1982 (Mex.).

⁸ Nalda, *supra* note 6, at 386.

⁹ MICHAEL C. MEYER & WILLIAM L. SHERMAN, *THE COURSE OF MEXICAN HISTORY*, 684 (Oxford University Press, 1995).

same ‘state-centered economic path.’”¹⁰ In regards to the nationalization of the banks, his hands were tied because of political reasons. The PRI had approved this action and a quick reversal of the decree would have had high political costs.¹¹ Thus, the necessary constitutional reforms and legal reforms were moved forward for a nationalized banking system. Articles 25 through 28 of the Constitution of the Mexican Republic were amended to make banking and credit services an activity reserved exclusively to the State. Laws were passed to implement the decree. Austerity measures were implemented, and banks were merged.¹² And, towards the second half of this administration, trade and investment regulation shifted from a protectionist, closed economy towards an outward looking economy with Mexico’s participation in the multilateral negotiations and its admission into the General Agreement on Tariffs and Trade (GATT).¹³ This set the stage for the next administration and a major shift for the banking sector.

The Carlos Salinas de Gortari administration (1988-94) completely shifted economic and trade policy in Mexico. The liberalization movement was put on fast track. Despite Salinas’ later arguments,¹⁴ many of the policy recommendations, known as the *Washington Consensus*, were implemented in Mexico during this period.¹⁵ Thus, with Mexico in GATT, Salinas looked to the possibility of a free trade agreement with its northern neighbors. During the negotiations of the North American Free Trade Agreement (NAFTA),¹⁶ many state-owned companies were put on sale, including the banks.¹⁷ However, Mexico was aware that it had to protect the recently privatized banking sec-

¹⁰ Francisco Valdés Ugalde, *The Changing Relationship between the State and the Economy in Mexico*, in CHANGING STRUCTURE OF MEXICO, POLITICAL, SOCIAL, AND ECONOMIC PERSPECTIVES 58 (Laura Randal, ed., Armonk: M. E., Sharpe, 1996).

¹¹ See Carlos Elizondo Mayer-Serra, *La expropiación bancaria veinte años después*, in CUANDO EL ESTADO SE HIZO BANQUERO. CONSECUENCIAS DE LA NACIONALIZACIÓN BANCARIA EN MÉXICO, 133 (Gustavo A. del Ángel et al. coords., Fondo de Cultura Económica, 2005).

¹² See SIGMOND, *supra* note 1, at 55.

¹³ See Charles T. DuMars, *Liberalization of Foreign Investment Policies in Mexico: Legal Changes Encouraging New Direct Foreign Investment*, 21 N.M.L. REV. 251, 255 (1990-1991).

¹⁴ See CARLOS SALINAS DE GORTARI, LA “DÉCADA PERDIDA” 1995-2006. NEOLIBERALISMO Y POPULISMO EN MÉXICO (Debolsillo, 2010).

¹⁵ John Williamson, *What Washington Means by Policy Reforms*, in LATIN AMERICAN ADJUSTMENT. HOW MUCH HAS HAPPENED? (John Williamson ed., Peterson Institute for International Economics, 2010), available at <http://www.iie.com/publications/papers/paper.cfm?ResearchID=486> (last visited Feb. 11, 2011). In this document, Williamson summarizes the 10 topics that “Washington” considered important, including: fiscal deficits (discipline); public expenditure priorities; tax reform; interest rates; exchange rate, trade policy; foreign direct investment; privatization; deregulation; and property rights. In response to the debt crisis of the 1980s, many Latin American countries, including Mexico, implemented reforms urged upon them by Washington in these key areas.

¹⁶ North American Free Trade Agreement, U.S.-Can.-Mex., Dec. 17, 1992, 32 I.L.M. 289.

¹⁷ See LYNN V. FOSTER, A BRIEF HISTORY OF MEXICO (Book, 1997) (The biggest sales were the

tor. Consequently, Chapter 14 of NAFTA¹⁸ and the Foreign Investment Law (FIL) of 1993¹⁹ were restrictive of foreign investment in this sector. Nonetheless, Mexico sent clear signals to the international community that it was open for business and for investment. All indications pointed to an open economy that had gone beyond protectionism, to a market economy where the government's intervention would be reduced. Economic indicators looked promising and expectations were high. NAFTA was to be implemented on January 1, 1994, and assured a positive outlook for Mexico. Few expected what followed.

III. THE MEXICAN PESO CRISIS AND BANK BAILOUT (1994-1995)

The Peso Crisis and bank bailout that followed had many contributing factors to consider. This part will highlight some important elements of both. It will also survey the rescue package that resulted from this situation and the conditions placed by international loans that played a key role to establish a more regulated banking system. The adjustments made then could have, in large part, contributed to a stronger banking system better able to handle future shocks.

1. *The Peso Crisis*

The Peso Crisis must be studied from different perspectives. First, Mexico had initiated a series of economic reforms that placed it on the trade liberalization path since the late 1980s. The negotiation of a major trade agreement with the United States and Canada indicated that Mexico was ready to open up its markets. Negotiations proceeded for two years with improving economic data in Mexico being published.²⁰ Ultimately, NAFTA was signed on December 17, 1992. "The government had to find new ways to entice the capital inflows required for economic recovery and sustained growth."²¹

To demonstrate the success in attracting capital one can observe investor trends based on investor confidence. "Between 1983 and 1989, Mexico expe-

banks and the only telephone company (Telmex). Approximately 400 state-owned companies were put on sale).

¹⁸ According to NAFTA, the aggregate capital limit for commercial banks owned by foreign investors started at 8% in 1994 and the limit was to increase to 15% in 1999. See Section B of the Party's Schedule to Annex VII. See also discussion of restrictions in SIGMOND, *supra* note 1, at 83.

¹⁹ *Ley de Inversión Extranjera* [L.I.E.], [Foreign Investment Law], Diario Oficial de la Federación [D.O.], Dic. 27, 1993 (Mex.). To be discussed below.

²⁰ SIGMOND, *supra* note 1, at 62 (inflation rate went from 110.6 percent in 1983 to 7.5 percent in 1994); *id.* at 80-1 (foreign investment grew and the exchange rate was under control).

²¹ NORA LUSTIG, MEXICO, THE REMAKING OF AN ECONOMY 134 (The Brookings Institution, 1998).

rienced net capital outflows of \$15 billion, reflecting the impact of the 1982 Debt Crisis, but this reversed to net inflows of \$102 billion between 1990 and 1994, signaling the perceived effectiveness of its domestic and international actions.”²² Apparently, Mexico was on the right track and it became one of the leading places to invest. “In 1993, Mexico received \$31 billion of capital inflows —accounting for 20 percent of net capital flows to all LDCs [least developed countries].”²³ Investment flows speedily directed themselves into Mexico, but, other factors quickly changed that direction.

The other factors were not necessarily economic. Social and political factors quickly impacted the economy. The most relevant events are the following:

- 1) January 1, 1994, Guerilla Uprising: On the day that NAFTA was to take effect, “a relatively unknown guerrilla movement calling itself the [...] *Ejército Zapatista de Liberación Nacional, (EZLN)* [...] seized control of three cities...in the southern state of Chiapas.”²⁴ Political stability in Mexico was questioned by the international community.
- 2) March 23, 1994, the assassination of presidential candidate, Luis Donaldo Colosio, from the ruling party, PRI, during a campaign appearance in the border city of Tijuana, Baja California.²⁵
- 3) September 28, 1994, the murder of the Senate majority leader, José Francisco Ruiz Massieu.²⁶
- 4) The election year in which the opposition was gaining ground and social discontent was more present.

The impact of the above events was felt immediately. In 1994, “[...] Mexico’s foreign currency reserves dropped from a high of \$29.3 billion at the end of February to \$25.9 billion at the end of March to \$17.7 billion by the end of April.”²⁷ The outflows of capital were rapid and Mexico sought the assistance of the United States. “On March 24, U.S. authorities agreed to make a short-term credit facility available to Mexico, and the peso was allowed to depreciate approximately 1 percent against the dollar, combining with a 7 percent devaluation that had taken place in the month preceding the assassination.”²⁸ In April, the North American Financial Group was established. This group included the finance ministers and central banks of the United States, Canada and Mexico, and in a trilateral agreement it made available to Mexico

²² Douglas W. Arner, *The Mexican Peso Crisis: Implications for the Regulation of Financial Markets*, 2 NAFTA L. & BUS. AM. REV. 28, 34 (1996).

²³ *Id.*

²⁴ BURTON KIRKWOOD, *THE HISTORY OF MEXICO* 209 (Greenwood Publishing Group, 2000).

²⁵ MEYER, *supra* note 9, at 700.

²⁶ KIRKWOOD, *supra* note 24, at 210.

²⁷ ARNER, *supra* note 22, at 34.

²⁸ *Id.*

a short-term credit facility of \$6 billion from the U.S. and \$1 billion from Canada.²⁹ Internally, the Bank of Mexico increased domestic interest rates from 10.1 percent on March 23 to 17.8 percent in April on short-term peso-denominated Mexican government notes (*celes*) in order to reduce the outflow of capital.³⁰ “To compound the problem, an unexpected rise in U.S. interest rates took place over 1994: the average of the three-month T-bill rate went from 3.02 percent to 5.64 percent between January and December.”³¹

By the end of 1994, with a new president, Ernesto Zedillo Ponce de León (1994-2000), and capital leaving rapidly, it was clear that Mexico was headed for a crisis. The initial actions, or inactions, by the new administration further complicated events. The president’s consideration of military action against the EZLN movement caused further uncertainty and he was informed that because of the Chiapas situation, investors moved about one billion dollars out of Mexico in a single day.³² The peso was devaluated on December 20th³³ which caused more reserve loss and finally the Mexican government was forced to freely float its currency on December 22nd.³⁴ Mexico was about to default on its dollar-indexed and dollar-denominated debt. The economy plummeted.

Mexico’s response was to turn to the international community for assistance. Its new NAFTA partner, the United States, with the push of President William Clinton moved quickly to assemble a loan-guarantee package for Mexico. On January 12, 1995, Clinton proposed a \$40 billion loan package as Mexico continued on its free fall.³⁵ However, he did not have support from Congress. Consequently, on January 31st, Clinton announced a \$51 billion rescue plan for Mexico.³⁶ He was able to accomplish this under his executive authority and the plan consisted of the following: the U.S. Treasury line of credit was extended to \$20 billion, by means of the U.S. Exchange Rate Stabilization Fund; a \$10 billion increase in the IMF standby agreement was announced, for a total of \$17.8 billion; the pledge made by the BIS was doubled to \$10 billion; and \$3 billion from commercial banks was confirmed.³⁷ The package raised controversy, particularly the \$20 billion for the U.S. Exchange Rate Stabilization Fund and the \$10 billion from the IMF. Debate ensued

²⁹ *Id.*

³⁰ *Id.* at 35.

³¹ Carlos M. Urzúa, *Five Decades of Relation between the World Bank and México*, in 2 THE WORLD BANK: ITS FIRST HALF CENTURY 100 (D. Kapar & Webb comps., Washington: Brookings Institution Press, 1997).

³² *Id.* at 101.

³³ Arner, *supra* note 22, at 35.

³⁴ *Id.*

³⁵ SIDNEY WEINTRAUB, FINANCIAL DECISION MAKING IN MEXICO, TO BET A NATION 117 (University of Pittsburgh Press, 2000).

³⁶ Urzúa, *supra* note 31, at 102.

³⁷ *Id.* at 106.

because four-fifths of the Fund was committed and, according to the rules, it surpassed the IMF credit limit of \$7.2 billion.³⁸ Despite the disagreement, the plan was endorsed.

International assistance came with a price. Mexico had to meet certain conditions, such as developing an economic plan. On March 9, 1995, Mexico released this new plan, with the goals to “restore financial stability, strengthen public finances and the banking sector, regain confidence, and reinforce the groundwork for long-term sustainable growth.”³⁹ Some conditions are mentioned below.

Ultimately, the peso crisis and the need for international assistance did bring some lessons. “The main lessons of the recent Peso Crisis of 1994-1995 are that responsible financial and government leaders on both sides of the border failed to provide reasonable foresight, judgment, and supervision.”⁴⁰ The Mexican government failed to foresee that the flow of incoming capital could easily change its direction, as it did, and “in the United States, little attention was paid to these risks, as Wall Street and other financial interests got involved in the speculative fever of a Mexican and ‘emerging markets’ investment boom.”⁴¹ Both the U.S. government and the Mexican government failed to supervise. “Top U.S. financial and trade officials largely left Mexico-U.S. trade investment flows to the marketplace, and to the Mexican government’s policy-makers.”⁴² The consequences of such failure led to high unemployment, inflation, a sharp increase in non-performing loans and finally to the banking crisis and the bailout that followed.

2. *The Banking Crisis and Bailout*

In retrospect, in 1995, given the conditions of the peso crisis and the recent privatization of the banks, a perfect storm was brewing for a banking crisis. The exact causes leading to it are still subject of debate. However, some authors contend that the privatization of the banks produced disastrous results. “Some observers, particularly those who were directly involved in the 1991 sale of the banks, attribute the collapse of the banking system to a macroeconomic shock in 1994-1995, whose features included a balance of payment crisis, the collapse of the exchange rate, and the skyrocketing of interest rates.”⁴³ Nevertheless, “a second, competing view, argues that the macro

³⁸ *Id.* at 109.

³⁹ Arner, *supra* note 22, at 40.

⁴⁰ William A. Lovett, *Lessons from the Recent Peso Crisis in Mexico*, 4 TUL. J. INT’L & COMP. L. 143, 149 (1996).

⁴¹ *Id.*

⁴² *Id.*

⁴³ Stephen Haber & Shawn Kantor, *Getting Privatization Wrong: The Mexican Banking System 1991-2003*, in WORLD BANK DOCUMENTS, Nov. 10, 2003, www.worldbank.org.

shock of 1994-1995 only hastened the collapse of a banking system that was already in serious trouble. In this view the design of Mexico's bank privatization was fundamentally flawed."⁴⁴ Stephen Haber and Shaw Kantor concur with the second view and claim that "even had there been no peso crisis of 1994-1995, the Mexican banking system would have collapsed."⁴⁵

According to Haber and Kantor, the collapse was forthcoming for several reasons. The banks were already amassing large portfolios of non-performing loans, whose collateral proved to be unrecoverable; banking institutions were undercapitalized as well as inefficient, and did not operate according to international standards.⁴⁶ They trace the flaws of the privatization process to three inter-related features of Mexico's political economy: The first factor, limitless discretion of the government, generated a high risk environment for bankers, because one president could expropriate at will and the next could then privatize the banks. The second component, the government's desire to maximize revenues, led to two governmental strategies that would later become a problem. One strategy was to signal to potential bidders that they would not have to operate in a highly competitive environment and the other was the structure of the auction rules themselves.⁴⁷ "Experience in banking was not a factor in deciding how to allocate banks to private investors."⁴⁸ Winners were decided only on the price offered by bidders. Additionally, Mexico's accounting rules were not in conformity with internationally accepted accounting standards, which made the market value of the banks higher. Lastly, the third factor, government's low capacity to enforce contract and property rights, also led to deficiencies. Investors in the banking sector had overpaid and wanted to recover their investments, but, as they "quickly found out, they neither had mechanisms to assess the credit worthiness of borrowers nor did they have the ability to enforce their contract rights once loans went bad [...]."⁴⁹ An inefficient judicial system contributed to more risks for bankers. Default risk could not be assessed because there was no private credit reporting in Mexico. All of these factors created a high risk environment.

In addition to this, the banks themselves piled on more risks. Aggressive competition among banks, specifically in loans, also contributed to the problem. For example, the loans for housing and real-estate from December 1991 to December 1994 nearly tripled.⁵⁰ Non-performing loans increased as well. "In December 1991 the ratio of non-performing to total loans was 3.6 percent. By December 1992 the ratio had climbed to 4.7 percent, and by De-

⁴⁴ *Id.*

⁴⁵ *Id.* at 18.

⁴⁶ *Id.* at 2.

⁴⁷ *Id.*

⁴⁸ *Id.* at 7.

⁴⁹ *Id.* at 11.

⁵⁰ *Id.* at 13.

cember 1994 had reached 6.1 percent.⁵¹ Aggravating this situation was the inability of bankers to repossess the collateral on past due loans due to the lack of enforcement of property rights. Finally, the exchange rate collapsed in December 1994, capital flight was rampant, and banks could no longer sustain the pressure. The banks failed.

The 1995 banking crisis was similar to other banking crises. Common characteristics were: “a massive expansion of credit in a short period of time, poor bank management, supervisory and regulatory loopholes, and a shock (both domestic and external).”⁵² Sidaoui claims that it was precisely the weakness of the financial system and the loopholes within the regulatory and supervisory frameworks that exacerbated its aftermath. Additionally, he further states that “the unlimited deposit insurance scheme, which protected all banks’ liabilities without any restriction, induced moral hazard and increased the cost of banking resolution.”⁵³ Poor banking skills and conflicts of interests, specifically related to lending, were also contributing factors according to Sidaoui. He highlights the conclusions found by R. La Porta *et al.*,⁵⁴ on related lending and the crisis. Sidaoui claims that related lending increased the severity of the crisis. Like Haber and Kantor, Sidaoui claims that the judicial system was inefficient. “Many loans were written off because of the issues directly related to the inefficient judicial and regulatory procedures that involved the recovery of loans from bankrupted companies. The legal framework proved to favor debtors over creditors.”⁵⁵

The government’s response to the banking crisis came through a series of actions, including the development of programs to restructure consumer and commercial payments, to provide new banking capital, and to reform laws to allow investment in the financial sector. “Preventive measures were also taken on the domestic financial markets to avoid contagion, by means of a rescue package in support of banks and borrowers alike, and prevent a widespread collapse of financial institutions.”⁵⁶ One such program consisted of an injection of loans in U.S. dollars made by *Banco de México* [the Mexican central bank] to banks so they could fulfill their obligations and renew their loans.⁵⁷

⁵¹ *Id.* at 14.

⁵² José J. Sidaoui, *The Mexican Financial System: Reforms and Evolution 1995-2005*, 28 BIS PAPERS 277 (Aug. 7, 2006), <http://www.bis.org/publ/bppdf/bispap28s.pdf> (last visited May 15, 2011).

⁵³ *Id.* at 278.

⁵⁴ See R. La Porta, F. López-de-Silanes & G. Zamarrita, *Related Lending*, 118 QUARTERLY JOURNAL OF ECONOMICS, 231-36 (2003).

⁵⁵ *Id.*

⁵⁶ Guillermo Ortíz Martínez, *What Lessons Does the Mexican Crisis Hold for Recovery in Asia?*, 35 IMF FINANCE AND DEVELOPMENT 2 (1998), <http://www.imf.org/external/pubs/ft/fandd/1998/06/ortiz.htm> (last visited May 20, 2011).

⁵⁷ William Gruben & John H. Welch, *Distortions and Resolutions in Mexico’s Financial System*, in CHANGING STRUCTURE OF MEXICO, POLITICAL, SOCIAL, AND ECONOMIC PERSPECTIVES, 72 (Laura Randall ed., Sharpe, 1996).

This was to be done through the *Fondo Bancario de Protección al Ahorro* [Banking Fund for the Protection of Savings, FOBAPROA], which was created by the Salinas administration as a contingency fund to face extraordinary financial problems in times of economic crisis created by bank insolvency due to noncompliance of bank debtors and a massive withdrawal of funds.⁵⁸ The FOBAPROA received capital from a World Bank loan that will be discussed below. The use, or misuse, of this bailout fund was the cause of much debate within Mexico when the banks' debts were passed on to the taxpayers in 1998.

Other programs initiated in 1995 included the *Apoyo Inmediato a Deudores de la Banca* [Immediate Support Agreement to Bank Debtors, ADA] and the *Unidades de Inversiones* [Investment Units, UDIs]. The first program, the ADA, offered immediate interest rate relief for up to 18 months and allowed long-term debt restructuring.⁵⁹ The second program "was designed to assist mortgage holders and small business by establishing a repayment schedule based on inflation-indexing terms, thus reducing the cash flow burden on borrowers."⁶⁰

Programs for raising capital were also initiated. One such program was the *Programa Emergente de Capitalización Temporal* or PROCAPTE [Emergent Program for Temporary Capitalization]. Under this program "troubled banks could raise capital by creating and selling subordinated debentures (bonds) to the nation's deposit insurance, FOBAPROA."⁶¹ Additionally, many other programs were initiated to support debtors during this time.⁶²

The above-mentioned programs were administered through the FOBAPROA, which was supposed to put the banking industry back on track. However, it is argued that "the opaque nature of the process left a large cloud of doubt, making it appear that assistance had been designed more to 'legalize' and cover up malfeasance than to actually put the banking system back on its feet."⁶³ The aid process "turned out to be more of a cover-up operation than a serious attempt to root out fraud. A large part of the non-performing loans which the government purchased were delinquent, often due to an intentional refusal by large industrial and financial groups to pay back loans

⁵⁸ See ELVIA ARCELIA QUINTANA ADRIANO, ASPECTOS LEGALES Y ECONÓMICOS DEL RESCATE BANCARIO EN MÉXICO 76 (UNAM, 2003). For a full discussion of the use, or misuse, of the FOBAPROA, see also SIGMOND, *supra* note 1, at 74.

⁵⁹ JOHN A. ADAMS, MEXICAN BANKING AND INVESTMENT IN TRANSITION 127 (Quorum Books, 1997).

⁶⁰ *Id.*

⁶¹ *Id.*

⁶² See Banxico, *Reformas al Sistema Financiero* [Financial System Reforms], http://www.banxico.org.mx/tipo/disposiciones/ReformaSisfin/ref_1995.html (last visited May 10, 2010).

⁶³ Irma E. Sandoval, *Financial Crisis and Bailout: Legal Challenges and International Lessons from Mexico, Korea, and the United States*, in COMPARATIVE ADMINISTRATIVE LAW (Susan Rose-Ackerman & Peter L. Lindseth, eds., Edward Elgar Publishing, 2010).

instead of a real inability to pay on the part of small- and medium-sized debtors.”⁶⁴ In the end, the cost of the bailout was passed on to the taxpayers by executive actions that converted the FOBAPROA’s liabilities into public debt. This was done despite constitutional restraints for acquiring debt and, therefore, many argue, illegal⁶⁵ and with a huge fiscal cost.⁶⁶

3. *International Loans and Conditions for Reforms*

The role of the international loans in the reform of the Mexican financial system played a key part. The International Bank for Reconstruction and Development (World Bank) made several loans to Mexico with the objective of strengthening the financial system.⁶⁷ The first loan to support the restructuring of Mexico’s financial sector was for the amount of US\$1,000 million⁶⁸ and the objectives established in the loan proposal were designed to:

- (a) Restore the solvency and soundness of Mexico’s banking system and improve confidence in the financial system;
- (b) Reform accounting standards and prudential regulations for banks, and strengthen supervision to prevent a future recurrence of systemic problems;
- (c) Improve management of the provision of liquidity on behalf of the *Banco de México* and development banks; and
- (d) Initiate reforms in the accounting practices and regulation of financial groups.⁶⁹

The proposed loan would support actions to:

- [...]
- (a) Determine the health of the banking system through an intensive inspection of commercial banks and a review of the situation of banks entering the temporary capitalization program (PROCAPTE);
- (b) Restructure banks that have experienced exceptional decapitalization;
- (c) Initiate reforms to accounting standards and prudential regulations for banks;

⁶⁴ *Id.* at 556.

⁶⁵ See QUINTANA, *supra* note 58, at 76 (according to Article 73 of the Mexican Constitution, if the Federal Government had been acquiring debt during the bailout process, then Congress should have approved it, which was not the case).

⁶⁶ Sandoval, *supra* note 63 (originally, the cost of the bailout was supposed to be between 5 and 8 percent of the GDP in 1995, but ended up reaching 20 percent).

⁶⁷ The World Bank, Financial Sector Restructuring Adjustment Loan, www.worldbank.org (last visited May 10, 2010).

⁶⁸ *Id.*; see also Inter-American Development Bank, Report No. PIC2076 (Inter-American Development Bank is processing a parallel Sector Adjustment Loan amount of US\$750 million under similar terms).

⁶⁹ *Id.*

- (d) Strengthen bank supervision;
- (e) Improve the regulatory framework to facilitate corporate work-outs and debt restructuring; [...].⁷⁰

Several World Bank documents associated with this loan include further conditions for the Mexican government⁷¹ that would have a long term impact.

In the context of the IMF, “the set of conditions that apply to loans is what is commonly referred to as «IMF conditionality»”⁷² and are basically policy prescriptions. “The policy prescriptions contained in IMF-supported programs essentially serve to provide the safeguards that the country will be able to rectify its macroeconomic and structural imbalances, and will be in a position to service and repay the loan.”⁷³ Much has been written on whether these conditions are impositions and whether they in fact work.⁷⁴ In the case of Mexico, a strong argument can be made that policy recommendations did work for the financial system, given the performance of the banks during the most recent crisis.

However, not all scholars view international organizations, their loans and policy recommendations as seeking to prevent financial failures. One such scholar, Robert J. Barro, raised controversy in his viewpoint piece titled “The IMF Doesn’t Put out Fires, it Starts Them.”⁷⁵ In his note he states that with the help of the United States, the IMF encourages bad economic policy by rewarding failure with showers of money.⁷⁶ In particular, in the “Mexican Mess” as he calls it, “the IMF-U.S. lending package was effectively a reward for corrupt and risky bank lending and poor macroeconomic policies.”⁷⁷ He further states that the bailout that followed kept foreign lenders whole and became a liability for Mexican taxpayers. Furthermore, “the real shame of the Mexican bailout is that it was judged by many observers to be a success, mainly because the U.S. Treasury got repaid.”⁷⁸

⁷⁰ *Id.*

⁷¹ *Id.*; see also Guarantee Agreement L3911, Financial Sector Restructuring Loan (June 23, 1995); Loan Agreement L3911 Financial Sector Restructuring Loan (June 23, 1995); Mexico Financial Sector Restructuring Adjustment (Sept. 5, 1997).

⁷² MOSHIN S. KHAN & SUNIL SHARM, IMF CONDITIONALITY AND COUNTRY OWNERSHIP PROGRAMS (IMF, Sept. 24, 2001).

⁷³ *Id.*

⁷⁴ See Williamson, *supra* note 15 (In Williamson’s paper on the Washington Consensus, he refers to “Washington” as including international financial institutions [*i.e.* the IMF and the World Bank] and their suggested policy reforms. Thus, the conditions placed also follow the same theme).

⁷⁵ Robert J. Barro, *The IMF Does not Put out Fires, it Starts Them*, BUSINESS WEEK, Dec. 7, 1998, at 18, available at http://www.economics.harvard.edu/faculty/barro/files/bw98_12_07.pdf (last visited June 29, 2011)

⁷⁶ *Id.*

⁷⁷ *Id.*

⁷⁸ *Id.*

Despite conflicting opinions, the peso crisis, the bank bailout and the conditions imposed by international loans prompted a series of regulatory changes that sought to consolidate the Mexican financial system and prevent future meltdowns.

4. Reforms in Mexican Financial Laws⁷⁹

The first set of reforms was published on February 15, 1995. As a whole, these were intended to strengthen the structure of financial institutions and their organization, as well as to improve their performance. The immediate intent was to stabilize the national economy and create policies that would lead to future growth.

In order to carry out the above objectives, capital for financial institutions was needed. The government, therefore, initiated a set of reforms that would strengthen and modify the share structure of financial institutions in order to allow access to national and international investment. The modifications discussed below sought to increase investment and the development of strategic alliances that would lead to increased levels of efficiency in the financial system.⁸⁰

For banking institutions, reforms to laws that regulate the financial system were crucial. First, six articles in the *Ley de Instituciones de Crédito* [Credit Institutions Law, LIC]⁸¹ dealing with shareholder structure were modified.⁸² All the modifications had a common denominator: to increase the ability of Mexican and foreign investors to hold shares, in greater percentages, in Mexican banks. An injection of capital was much needed and this was one way of reaching that goal.

The *Ley del Mercado de Valores* [Securities Market Law]⁸³ was also modified to allow more investment in securities markets. The reforms made in 1995 gave more access by abrogating certain government limitations on foreign investment in brokerage houses.⁸⁴ Due to this modification, foreign investment was opened for certain shares that had previously been closed.⁸⁵

⁷⁹ For an in depth study of banking regulations and reforms, see JESÚS DE LA FUENTE, 1 TRATADO DE DERECHO BANCARIO Y BURSÁTIL, SEGUROS, FIANZAS, ORGANIZACIONES Y ACTIVIDADES AUXILIARES DEL CRÉDITO, AHORRO Y CRÉDITO POPULAR, GRUPOS FINANCIEROS (Porrúa, 2002).

⁸⁰ See Banxico, *supra* note 62.

⁸¹ Ley de Instituciones de Crédito [Credit Institutions Law], Diario Oficial de la Federación [D.O.], July 19, Julio de 1990 (Mex.).

⁸² The articles modified were articles 11, 13, 14, 15, 17 and 45.

⁸³ Ley del Mercado de Valores [Securities Market Law], *as amended*, Diario Oficial de la Federación [D.O.], Feb. 15, 1995 (Mex.).

⁸⁴ See *id.* article 17.

⁸⁵ See *id.* article 28 bis 7.

The *Ley para Regular las Agrupaciones Financieras* [Law to Regulate Financial Groups]⁸⁶ was also modified in February 1995. As with the above laws, the means by which this was carried out was by increasing the percentage of certain shares that could be held by foreign investors.

Additionally, pursuant to the Law to Regulate Financial Groups, new rules were issued for the establishment of credit bureaus. This was an important step towards reducing risks in the future. Prior to these rules, banks were making loans without a full assessment of the risks, which often led to non-performing loans. Thus, the capability of carrying out credit background checks was vital.

Furthermore, institutional reforms were also made in 1995. In order to strengthen the supervision of the financial institutions the *Ley de la Comisión Nacional Bancaria y de Valores* [Law for the National Banking and Securities Commission, CNBV] was implemented.⁸⁷ Previously, there had been two separate commissions, one for overseeing the securities market and another for the banking industry. With this new law, both were consolidated into a single commission. The new commission was given additional authority to establish preventive corrective programs or agreements, which were of mandatory compliance for financial entities, and focused on eliminating financial imbalances that could affect liquidity, solvency or stability.⁸⁸ Further authority was given to the CNBV to issue prudential rules to preserve the liquidity, solvency and stability of the intermediators.⁸⁹ The new rules included rules for the diversity of risks, capitalization and the creation of preventive provisions. Finally, with the new consolidated structure, the capacity for supervision and oversight was strengthened. The hope was that with this new commission preventive actions could be taken with greater ease and speed in order to avoid complete meltdowns in times of financial crisis.

Further reforms to the financial laws were published in the *D.O.* in November 1995. These reforms were made to strengthen the protection of public interests and the modification of stock structure for certain financial intermediators, as well as to adopt measures that contribute to preventing and combatting money laundering.⁹⁰ For such purposes, several modifications were proposed and a motion passed to update the LIC and the law regulating the stock market. The primary objective was to grant more powers to the CNBV to effectively protect consumers of bank and credit services by allowing the CNBV to review the different contract models so as to verify that confusing

⁸⁶ *Ley de la Comisión Nacional Bancaria y de Valores* [Law for the National Banking and Securities Commission, CNBV], *Diario Oficial de la Federación* [D.O.], Feb. 28, 1995 (Mex.)

⁸⁷ *Id.*

⁸⁸ *See id.* article 4.

⁸⁹ *See id.* article 6.

⁹⁰ Banxico, *supra* note 62.

clauses that hindered the consumers from understanding the extent of the obligations agreed to were not contained in contracts.⁹¹

Modifications to the NAFTA were also made. In February 1995, foreign companies that could establish banks, subject to the approval of the Finance Ministry, would be allowed to acquire between 51 and 100 percent of the controlling interest in an individual bank, with some exceptions.⁹² The protective measures established in NAFTA were removed.

The Foreign Investment Law⁹³ was also modified. Article 7 of this law regulated and restricted foreign investment in financial activities. In 1993, up to 30 percent foreign investment was allowed in multiple bank credit institutions.⁹⁴ After the bank crisis, this article was reformed on several occasions, raising the percentage, until the restriction was completely repealed and up to 100 percent foreign investment was allowed.

Despite the fact that 1995 had a shocking beginning in Mexico, by the end of that year, the dust was beginning to settle. Massive amounts of money were being injected into the financial system, legal reforms were made to financial laws, bailout funds were being disbursed, and credit programs were in place. On November 14, 1995, Michel Camdessus, Managing Director of the IMF, commented on Mexico's economic policy of that year stating that:

The health of public finance has been restored, the necessary external adjustment has taken place, and the country has regained its access to the international capital markets. Although economic conditions remain difficult, growth is expected to resume, and the markets will stabilize as economic agents become convinced of the authorities' policy commitment.⁹⁵

Additionally, he defended the actions of the IMF in the large loan arrangement made for Mexico. He argued that “[a] decade of unstinting international efforts to open markets and liberalize emerging economies would have been at risk. Instead, Mexico was able to address its problems, to put itself back on the path of recovery, while at the same time limiting the negative impact of the crisis on other countries.”⁹⁶

On the other hand, some authors state that the process of deregulating the banking system, through financial reforms, deepened the banking crisis.⁹⁷ Alicia Girón and Noemí Levy find that the privatization process of the

⁹¹ *Id.*

⁹² ADAMS, *supra* note 59, at 127.

⁹³ *Ley de Inversión Extranjera*.

⁹⁴ *See id.* article 7 III (b).

⁹⁵ Michel Camdessus, *International Monetary Fund News*, Address at the Zurich Economic Society, *The IMF and the Challenges of Globalization – The Fund's Evolving Approach to its Constant Mission: The Case of Mexico* (Nov. 14, 1995), available at <http://www.imf.org/external/np/sec/mds/1995/mds9517.htm> (last visited May 15, 2011).

⁹⁶ *Id.*

⁹⁷ ALICIA GIRÓN & NOEMÍ LEVY, MÉXICO: LOS BANCOS QUE PERDIMOS (UNAM, 2005); *see*

early 1990s led to the *foreignization* of the banking system and the disappearance of credit channels by cancelling a regulated financial system without the construction of other channels of credit.⁹⁸ Their studies conclude that the foreignization process rapidly increased, without increasing efficiency and productivity in the banking industry, and without carrying out its primary function: the issuance of credit.⁹⁹ Therefore, according to these authors, the banking sector has since then failed to contribute to the economic growth of Mexico.

Nonetheless, others hold that “foreign participation has essentially rebuilt the sector, improving capitalization and the quality of bank assets and contributing to the accelerated decline in bad loans. Since 2004, foreign participation has helped to increase bank credit in the economy.”¹⁰⁰ Then again, one must look to the type of credit (private industry, credit for consumption, housing, to name a few) referred to by the authors on both sides because if we look at private industry credit, both agree it remains stagnant.¹⁰¹

IV. GLOBAL FINANCIAL CRISIS, 2007-2009

The most recent global financial crisis began in 2007 and became evident in 2008. This section will review the causes that led to this phenomenon and then ground the analysis in the Mexican context. The external causes and impacts in Mexico and the government and banks’ initial response will be mentioned. Given the proximity of the events, it is too soon to tell what the long term impacts will be.

1. *The 2008 Crisis*

In the most recent financial crisis, most analysts point their fingers towards the United States. The causes of the crisis are still being debated as some experts point to some factors, while others highlight different ones. One author claims the following:

also L. M. Galindo & C. Guerrero, *El impacto de la liberalización financiera sobre el ahorro privado en México, 1983-1998*, in *DE LA DESREGULACIÓN FINANCIERA A LA CRISIS CAMBIARIA: EXPERIENCIAS EN AMÉRICA LÁTINA Y EL SUDESTE ASIÁTICO* (G. Mántey & N. Levy eds., UNAM, 2000).

⁹⁸ *Id.* at 66.

⁹⁹ *See id.* at 79; SALINAS, *supra* note 14, at 172 (Carlos Salinas de Gortari, the president that initiated the privatization movement, later laments the foreignization of banks. He states that this loss of the system of payments to foreigners is a loss of Mexican sovereignty, similar to other historical moments such as the loss of half of the Mexican territory to the United States in 1847).

¹⁰⁰ Rubén Hernández-Murillo, *Experiments in Financial Liberalization: The Mexican Banking Sector*, 89 *FEDERAL RESERVE BANK OF ST. LOUIS REVIEW* 415-32 (2007).

¹⁰¹ Another set of important reforms took place which provided further prudential oversight and best practices for the banking sector. *See* De la Fuente, *supra* note 79.

The candidate causes of the economic and financial crisis of 2007-09 fall into four broad categories: (1) macroeconomic failures, which have three subcategories: monetary and fiscal policies, global imbalances, and housing booms; (2) failures of financial-sector supervision and regulatory policies and practices, which have innumerable subcategories; (3) excesses of poorly understood innovations in financial engineering, which have several subcategories: subprime mortgages, credit default swaps, and new forms of securitization to name a few; (4) excesses, or imprudence, on the part of large private financial institutions, in particular those with a global reach.¹⁰²

Once the crisis became evident, the spillover effects began. In an economy so closely tied to the U.S. market, Mexico quickly felt the crunch. Manufactured goods and petroleum exports decreased.¹⁰³ The remittances sent to Mexico from Mexican workers in the United States also dropped.¹⁰⁴ Volatility in the exchange rate of the peso was observed. The stock market also took a hit. Overall, economic growth expectations dissipated.

2. Comparison of 1995 Crisis to that of 2008

Analysts have now taken to the task of studying the recent crisis and questioning what was similar or different from previous crises. Already, we are beginning to see some common factors arise. “The crisis had four features in common with other crises: 1) asset price increases that turned out to be unsustainable; 2) credit booms that led to excessive debt burdens; 3) build-up of marginal loans and systemic risk; and 4) the failure of regulation and supervision to keep up with and get ahead of the crisis when it erupted.”¹⁰⁵ On this occasion, the crisis began in the United States, with housing prices increasing in excess of 30% in the five years preceding the crisis and peaking six quarters prior to the onset of the crisis.¹⁰⁶ Credit expansion in the United

¹⁰² EDWIN M. TRUMAN, LESSONS FROM THE GLOBAL ECONOMIC AND FINANCIAL CRISIS (Peterson Institute for International Economics, 2009).

¹⁰³ See Guillermo Ortiz, *La crisis de 1994-95 y la actual crisis*, CNN EXPANSIÓN, Feb. 3, 2009, available at <http://www.cnnexpansion.com/economia/2009/01/30/la-crisis-del-199495-y-la-actual-crisis>. Total Mexican exports to the United States went from 223,403.6 million dollars in 2007 to 184,878.5 million dollars in 2009. See e.g., Secretaría de Economía, http://www.economia-snci.gob.mx/sph_pages/estadisticas/cuad_resumen/expmx_c.htm (last visited May 5, 2010).

¹⁰⁴ On January 27, 2009, Banco de México published a statement indicating that family remittances had dropped 3.6% from 2007 to 2008, from 25, 145 million dollars, for a loss of 931 million dollars. See, e.g., Banco de México, *Las remesas familiares en 2008*, <http://www.banxico.org.mx/documents/%7BB7CBCFAF-AB7D-BE65-F78F-6827D524C418%7D.pdf> (last visited May 10, 2010).

¹⁰⁵ Stijn Claessens et al., *Lesson and Policy Implications from the Global Financial Crisis* (IMF Working Paper WP/10/44, 2010).

¹⁰⁶ *Id.*

States, particularly in the subprime mortgage segment, was also a contributing factor, as well as the fact that those housing loans were being made to high risk borrowers. The U.S. government's prudential oversight of financial innovation was insufficient. "As happened often before, the focus of authorities remained primarily on the liquidity and insolvency of individual institutions, rather on the resilience of the financial system as a whole."¹⁰⁷

As we can observe, some of the above-mentioned factors were present in Mexico's 1995 crisis. Common factors include: low international interest rates and investors' search for better rates; a wide availability of resources that promoted unmeasured growth of credit in a context of deficient banking practices; serious deficiencies in banking oversight and regulation; problems of opaqueness in the information; incentives that prompted financial institutions to take excessive risks; a financial crisis characterized by problems of systemic liquidity and solvency; direct intervention in several financial institutions by the authorities and a complicated political environment to implement the measures required to support the financial system.¹⁰⁸ Two salient common factors are the expansion of credit and the failure of regulation and supervision. Credit expansion, both in mortgages and credit cards was observed, as was an increase in non-performing loans. The "new" Mexican banks in 1994 were all too eager to offer credit and risk assessment was not the top priority. This has similarities with the subprime mortgage lending that took place in the United States. In both contexts, the banks were left unsupervised which led to catastrophic results and eventually huge bailouts at the taxpayers' expense.

In response to the subprime mortgage crisis, on October 3, 2008, U.S. President George W. Bush signed the Emergency Economic Stabilization Act (EESA), which contains the Trouble Asset Relief Program (TARP).¹⁰⁹ As stated in the EESA, the aims of the TARP are:

- (1) To immediately provide authority and facilities that the Secretary of the Treasury can use to restore liquidity and stability to the financial system of the United States; and
- (2) To ensure that such authority and such facilities are used in a manner that
 - (A) Protects home values, college funds, retirement accounts, and life savings;
 - (B) Preserves homeownership and promotes jobs and economic growth;
 - (C) Maximizes overall returns to the taxpayers of the United States; and
 - (D) Provides public accountability for the exercise of such authority.

¹⁰⁷ *Id.*

¹⁰⁸ Ortiz, *supra* note 103.

¹⁰⁹ Trouble Asset Relief Program (TARP) 110-343 (2008).

With the passage of this act, the Treasury Secretary was authorized to spend up to US \$700 billion and under Section 101, had the authority to “establish the Troubled Asset Relief Program (or “TARP”) to purchase, and to make and fund commitments to purchase, troubled assets from any financial institution, on such terms and conditions as are determined by the Secretary, and in accordance with this Act and the policies and procedures developed and published by the Secretary.” Stated simply, the government would buy toxic mortgage assets and other bad debts made by the financial institutions that took on the risk and then passed the burden of those bad choices to the taxpayers.

The TARP was highly criticized for diverse reasons. First, Henry Paulson, the Secretary of the Treasury who made the initial proposal and headed the Bush financial team at the time of the financial meltdown, had formerly been the CEO of the Goldman Sachs Group. Goldman Sachs was not only a contributor to the crisis, but later benefitted from the bailout.¹¹⁰ Thus, conflicts of interests concerns started even before the law was passed and claims were made that Paulson would help out his old friends.¹¹¹ Other scandals, dealing with excessive bonuses to top executives at financial institutions receiving TARP funds, soon came to light.¹¹² Consequently, the new Barack Obama Administration, similar to the Ernesto Zedillo Administration, inherited the crisis and then had to clean up the mess and put new regulations into place.

The most recent piece of legislation that responds to the financial crisis in the United States is the Dodd-Frank Wall Street Reform and Consumer Protection Act, which was signed into law on July 21, 2010.¹¹³ The aim of the legislation is to promote the financial stability in the United States by improving accountability and transparency of its financial system, to end the “too big to fail,” to protect the American taxpayer by ending bailout, to protect consumers from abusive financial services practices, and for other purposes.¹¹⁴ It is a comprehensive law that includes the creation of new agencies to in-

¹¹⁰ Goldman Sachs received \$10 billion from the Treasury and then wanted to return the money because of restrictions placed by TARP. See Christine Harper, *Goldman Sachs wants to Repay Treasury, CFO Says*, BLOOMBERG, Feb. 4, 2009, available at <http://www.bloomberg.com/apps/news?pid=newsarchive&sid=a7vRpWuhek3k>.

¹¹¹ See Ben White, *Details of Rescue Plan Unclear, but Some Already Benefit*, N. Y. TIMES, Sep. 19, 2008, available at <http://www.nytimes.com/2008/09/20/business/20winners.html>. See also Helene Cooper, *Obama orders Treasury Chief to Try to Block A.I.G. Bonuses*, N. Y. TIMES, Mar. 16, 2009, available at <http://www.nytimes.com/2009/03/17/us/politics/17obama.html>.

¹¹² See Liam Plevin, “AIG to Pay \$450 Million in Bonuses”, WALL ST J., Mar. 15, 2009, available at <http://online.wsj.com/article/SB123707854113331281.html?KEYWORDS=%22AIG+to+Pay+450+Million+in+Bonuses%22>.

¹¹³ THE DODD-FRANK WALL STREET REFORM AND CONSUMER PROTECTION ACT, PUB. L. 111-203 (2010).

¹¹⁴ See One Hundred Eleventh Congress of the United States of America, at the Second Session, H.R. 4173, Jan. 5, 2010, http://frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=111_cong_bills&docid=f:h4173enr.txt.pdf (last visited May 25, 2011).

crease oversight of financial institutions, promote transparency, and establish rigorous standards and supervision to protect the economy and consumers, among other new efforts to enhance the regulatory system. The complete coverage of this Act goes beyond the scope of this paper, but it is mentioned to draw a comparison with the modifications to the regulatory system post-crisis, as in the Mexican case.

In comparing government responses in the FOBAPROA and the TARP, one author claims, “the U.S. government behaved in a way dangerously similar to the Mexican government during the 1995 bailout.”¹¹⁵ Sandoval uses three basic rules, as established by Liliana Rojas-Suárez and Steven Waisbrod,¹¹⁶ to guide her analysis and make her assertions of the similarities between the two bailout processes. The first rule is that those who benefitted from taking the risks should be the ones to carry the weight of the bailout,¹¹⁷ or as Sandoval states, if someone must lose a part of their assets, “bank stockholders should be first in line.” The second is to avoid moral hazard during the bailout process, and the third deals with involvement of society and the political will to make the bailout a priority, assign public resources and avoid inflation. Sandoval calls this third rule “the need to build social legitimization for the bank bailouts through communication with and support from society.”¹¹⁸ She examines each rule and draws parallels between both bailout processes by noting who benefits in both (the banks and the bankers) and the discretionary powers of those administering the bailout monies in Mexico and the United States (FOBAPROA Technical Committee and the Secretary of the Treasury). Sandoval also notes the conflict of interests of those in charge of the TARP¹¹⁹ and highlights the fraud and looting of public resources in both scenarios, which speaks to moral hazard. And, as to the third rule, she states that Mexico’s bailout was riddled with fraud and self-dealing because there was little public scrutiny of the details of the process and that, although the U.S. bailout is more transparent, fundamental decisions can be taken with little oversight so that transparency only acts as an ex post check on Executive behavior.¹²⁰ Consequently, there is little communication and support from the

¹¹⁵ Sandoval, *supra* note 63, at 544.

¹¹⁶ Liliana Rojas-Suárez & Steven R. Weisbrod, *Manejo de las crisis bancarias: lo que debe y lo que no debe hacerse*, in *LAS CRISIS BANCARIAS EN AMÉRICA LATINA* (Ricardo Hausmann and Liliana Rojas-Suárez eds., Banco Interamericano de Desarrollo, Fondo de Cultura Económica, 1997) (in this text, the authors compare the banking crises in Argentina, Chile and Mexico using the three rules to analyze economic policy).

¹¹⁷ *Id.* at 137.

¹¹⁸ Sandoval, *supra* note 63.

¹¹⁹ For example, Sandoval notes that Henry Paulson was the CEO of Goldman Sachs Group, a beneficiary of the bailout, and then placed in charge of reforming the system that he helped bring into crisis. She parallels this to the Mexican case where government authorities hired some of the same bankers implicated in the crisis and put them in charge of the bailout process. *Id.*

¹²⁰ *Id.*

public. Furthermore, she states, “there are few mechanisms of accountability that have real legal bite.”¹²¹

On the other hand, the main differences should be noted. First, the most recent crisis originated in the United States, not in Mexico. Thus, the scope and impact of the U.S. crisis had global reach and depth. For Mexico, capital flight, a huge problem in 1995, was not the primary issue in 2008. The exchange rate of the peso, since 1994, was allowed to float and, therefore, is now much more flexible. Furthermore, on this occasion, Mexican banks had much more experience, information was more transparent, and international accounting rules were followed. Because of more supervision and regulation, the banks had a more solid footing for this crisis.

Another difference that should be emphasized deals with accountability and criminal prosecution, that is, the enforcement of the law. In Mexico, the fraudulent actions by bankers and those involved in the FOBAPROA scandal were not prosecuted.¹²² One blatant, and much publicized, example is the case of Carlos Cabal Peniche, who was the owner of Banca Cremi and accused of financial fraud, self-made loans, related lending and credits related to illegal activities linked with drug trafficking, money laundering and funding of the PRI electoral machine. After the prosecution had pressed on with the case for 16 years (in which time he fled from the country, was found in Australia and extradited to Mexico), Peniche was exonerated from all charges, except a minor tax evasion charge.¹²³

On the other hand, in the United States, Neil Barofsky, who is overseeing the \$700 billion TARP, says he has 20 criminal probes and call for changes to prevent fraud.¹²⁴ However, some critics say that these investigations will probably lead nowhere.¹²⁵ Nevertheless, in the United States, unlike in Mexico,

¹²¹ *Id.* at 556.

¹²² See *Queda sin castigo delito en Fobaproa*, REFORMA, Apr. 17, 2006 (in which it claims that 80% of the illegal actions committed in the Fobaproa went unpunished). See also *La extranjerización de la banca no la hizo más eficiente: CEPAL*, LA JORNADA, Sept. 25, 2006 (*La Jornada* cites a UN ECLAC study stating that in the majority of the countries in which a financial bailout of the banks has taken place, those responsible have been punished, this measure did not take place in Mexico. This same study is cited as stating that the foreignization of the banks in Mexico did not increase efficiency and productivity in the Mexican banking sector and that the FOBAPROA could have been avoided).

¹²³ Abel Barajas, *Cabal Peniche Derrota a PGR: Lo extraditaron, demandaron, juzgaron y resultó inocente; tampoco pagará 239 millones de pesos a Hacienda*, TABASCO HOY, Jan. 29, 2010, http://www.tabascohoy.com.mx/noticia.php?id_nota=187297 (last visited Feb. 10, 2011). Another example is Ángel Isidoro Rodríguez Sáez, aka “El Divino”, who was charged and extradited to Mexico from Spain only to be exonerated of all charges. See *Libre ‘El Divino’ de procesos judiciales*, NOTICIEROS TELEVISIA, Dec. 17, 2002, <http://www.esmas.com/noticierostelevisa/mexico/269576.html>.

¹²⁴ Jennifer Liberto, *Bailout Cop Busy on the Beat*, CNN.MONEY.COM, Apr. 21, 2009.

¹²⁵ See Joe Nocera, *The States Take on Foreclosures*, N.Y. TIMES, Oct. 29, 2010, available at <http://www.nytimes.com/2010/10/30/business/30nocera.html> (“a handful of federal investigations

states have taken on a more active role in investigating and prosecuting the mortgage foreclosure mess that led to the bank bailout. The state attorneys general had previously initiated actions against banks for predatory lending, but were stopped by federal regulators (the Office of the Comptroller of the Currency and the Office of Thrift Supervision) because of the pre-emption doctrine. National banks were governed by federal rules and pre-emption blocked state action under state consumer protection laws. Yet, the state attorneys general pushed forward. “In 2002, for instance, a coalition of attorneys general and the Federal Trade Commission settled a predatory lending suit against a subprime lender called First Alliance; it called for the company to pay up to \$60 million to reimburse homeowners it had victimized. That same year the A.G.’s reached a settlement with Household Finance for \$484 million.”¹²⁶ In 2006, Ameriquest agreed to pay \$325 million and reform its lending practices which eventually led them to shut down in 2008.¹²⁷

Furthermore, post-financial crisis, “no federal regulator would have the nerve [...] to try to block the states from investigating the mortgage foreclosure scandal” and foreclosure is a state matter, not a federal one.¹²⁸ Thus, the state attorneys general have geared up and are ready to prosecute. Additionally, under the Dodd-Frank Law,¹²⁹ states can enforce their own state consumer laws against nationally chartered banks. Plus, the Consumer Financial Protection Bureau has been established which should facilitate the process.¹³⁰ Nonetheless, it is too early to tell, but prosecutions will surely come and those responsible for the mortgage foreclosure scandal will be held accountable.

Additionally, at the federal level, the Office of the Special Inspector General for Trouble Asset Relief Program, SIGTARP, was established by Section 121 of the Emergency Economic Stabilization Act of 2008 (“EESA”).¹³¹ This office is entrusted with the mission to advance economic stability by promoting the efficiency and effectiveness of TARP management, through transparency, through coordinated oversight, and through robust enforcement against those, whether inside or outside of Government, who waste, steal or abuse TARP funds.¹³² In its latest quarterly report to Congress of January 26, 2011, it claims to have charged 45 individuals either civilly or criminally with fraud, 13 of whom have been criminally convicted. Thus, according to SIGTARP,

have also been announces, but we all know that they’re not going to amount to a hill of beans”).

¹²⁶ *Id.*

¹²⁷ *Id.*

¹²⁸ *Id.*

¹²⁹ The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (Dodd-Frank Law) established the Consumer Financial Protection Bureau (CFPB).

¹³⁰ The CFPB will go into effect on July 11, 2011. *See* The Consumer Financial Bureau, <http://www.consumerfinance.gov/the-bureau/> (last visited Feb. 14, 2011).

¹³¹ SIGTARP, http://www.sig tarp.gov/about_stat.shtml (last visited Feb. 10, 2011).

¹³² *Id.*

this agency has helped prevent \$555.2 million in taxpayer funds from being lost to fraud and it currently has 142 ongoing investigations.¹³³ One recent and much publicized conviction is that of Charles J. Antonucci, who has pleaded guilty to numerous criminal charges, including securities fraud, bribery and embezzlement. Antonucci has agreed to pay \$11.35 million and faces up to 135 years in prison.¹³⁴ This may be the first of many cases¹³⁵ in the upcoming months and marks a stark distinction between accountability in the Mexican bailout context and that of the United States.

Another interesting difference is that banks in the United States are actually paying back TARP monies. On June 9, 2009, it was published by the media that several large U.S. banks with names such as Bank of America (\$45 billion), JP Morgan Chase (\$25 billion), Goldman Sachs (\$10 billion), and Morgan Stanley (\$10 billion) were paying the government back and in some cases, like Bank of America, two years ahead of the projected payback date.¹³⁶ Citigroup joined the group of banks paying back TARP funds in December that same year. "The banks are eager to escape TARP and the restrictions that come with it, particularly the limits on how much they can pay their 25 most highly compensated workers."¹³⁷ Overall, the \$700 billion initially projected was not used by the Treasury and some analysts say that the actual cost to the taxpayer for this program may be nothing, once all borrowers pay.¹³⁸ More recent comments state that the TARP will end up costing U.S. taxpayers approximately 85% less than originally expected; that is, the bill will come to about \$50 billion, far less than the \$350 billion that the Congressional Budget Office initially estimated.¹³⁹ Unfortunately, in the Mexican case, this did not occur.

¹³³ *Id.* Those ongoing investigations include banks like Bank of America, OMNI National Bank, Mount Vernon Money Center, and others.

¹³⁴ Andrew Martin, *Ex-Head of Park Avenue Bank Pleads Guilty to Fraud*, N. Y. TIMES, Oct. 8, 2010, available at <http://www.nytimes.com/2010/10/09/business/09bank.html>.

¹³⁵ Another recent highly publicized case is that of Lee Bentley Farkas who was arrested by SIGTARP agents and charged with bank fraud, wire fraud, and securities fraud and allegedly committed a massive multi-billion accounting fraud that included an attempt to fraudulently acquire more than 500 million in TARP funds for Colonial Bank. TARP funds were not actually disbursed. This is an on-going case. See Eric Dash, *Executive Charged in TARP Scheme*, N. Y. TIMES, June 16, 2010, available at <http://www.nytimes.com/2010/06/17/business/17fraud.html>.

¹³⁶ David Grant, *Why Are Big Banks Like Citigroup Rushing to Pay Back TARP Funds?*, THE CHRISTIAN SCIENCE MONITOR, Dec. 14, 2009, available at <http://www.csmonitor.com/Business/new-economy/2009/1214/Why-are-big-banks-like-Citigroup-rushing-to-pay-back-TARP-funds>.

¹³⁷ Eric Dash, *10 Large Banks Allowed to Exit U.S. Aid Program*, N. Y. TIMES, June 9, 2009, available at <http://www.nytimes.com/2009/06/10/business/economy/10tarp.html>.

¹³⁸ *Id.*

¹³⁹ Danny King, *Treasury: Bailout Will Cost Taxpayers 85% Less Than Expected*, DAILY FINANCE, Oct. 5, 2010, available at <http://www.dailyfinance.com/story/treasury-bailout-will-cost-taxpayers-85-less-than-expected/19662064/>.

3. *Impact of Global Crisis on Mexican Banking*

International observers evaluating the impact of the global financial crisis in Mexico have made some very positive comments. For example, the IMF has stated that policy reforms over the past decade have helped Mexico weather the global economic crisis.¹⁴⁰ The Article IV consultation on March 16, 2010, resulted in the following comment:

The banking system is sound. The banking and financial sectors in Mexico came through the crisis in good shape, the IMF said. Non-performing loans seem to have peaked at only 3 percent of total loans by end-2009. Banks are well capitalized and should be able to absorb a possible additional deterioration in credit quality in the event that the economic recovery was to prove more sluggish than expected.¹⁴¹

Despite the optimism, the report goes further to state that Mexico could be affected by changes to global financial regulation because most major Mexican banks are owned by global banks and that these could face higher capital charges from regulators as a result of potential future reforms.¹⁴² Mexican banks are now 85 percent foreign owned.¹⁴³

Mexican bankers share a similar opinion as to the soundness of the banking system. In the recent meeting of the *Asociación de Bancos de México* [Mexican Bankers Association] held in April of 2010 the president of the Association, Ignacio Deschamps, stated that Mexico's banking system withstood the turmoil of the current situation because of its experience of 1995 and 1996.¹⁴⁴ He asserts that the country and the financial system were put to the test and that the system resisted. "The lessons learned during the 1995-1996 crisis that resulted in strict regulation allowed the Mexican banking system to withstand the shocks of the recent global financial crisis."¹⁴⁵

Similarly, the position of the Mexican government is that the banking system is solid and that the capital flight experience of 1995 will not repeat itself. Undersecretary of the Ministry of Finance Alejandro Werner recently commented that the Mexican economy is safeguarded to withstand a possible outflow of capital due to the interest rates being raised in the United States for

¹⁴⁰ See IMF survey, <http://www.imf.org/external/pubs/ft/survey/so/2010/new031610a.htm> (last visited May 10, 2010).

¹⁴¹ *Id.*

¹⁴² *Id.*

¹⁴³ OCTAVIO AVENDAÑO CARBELLIDO, *EL SISTEMA FINANCIERO INTERNACIONAL. INSTITUCIONES Y CRISIS FINANCIERAS* 232 (Porrúa, 2010).

¹⁴⁴ See *EL FINANCIERO*, Apr. 19, 2010. <http://www.elfinanciero.com.mx/ElFinanciero/Portal/cfpages/contentmgr.cfm?docId=257114&docTipo=1&orderby=docId&sortby=ASC> (last visited Apr. 23, 2010).

¹⁴⁵ *Id.* (Translation by author of this work).

the economic recovery of that country.¹⁴⁶ Because of the incentives granted by the U.S. government to face the crisis, interest rates are low and unattractive, making Mexico a better place to invest because it shows more profitability.¹⁴⁷ “Our economy is well prepared to face these eventual movements (outflow of capital), but we should continue to reinforce the elements that allowed us to be ready, such as the accumulation of international reserves, the free float regime (of the exchange rate), that have worked very well and a strong banking sector that is well capitalized.”¹⁴⁸ He goes on to mention that international reserves in Mexico reached a historic maximum of 97,433 million dollars on April 16th, since the previous record of 96,220 million dollars the week before, pursuant to data from the *Banco de México*. The outlook for growth is positive, given a fall of 6.5 percent in 2009, the worst in six decades.¹⁴⁹ He further stated that the government focus is on rebuilding trust in the stabilization funds and in international reserves so that Mexico can be perceived as a solid economy.¹⁵⁰

The one area that was hard hit by the crisis was consumer credit. Ignacio Deschamps reported that the global crisis led to restructuring the debt of 1.9 million bank clients, by extending terms and reducing interest rates.¹⁵¹ The amount involved in restructuring was 2,600 million pesos, primarily for credit card consumers, personal loans and durable goods.¹⁵² He also reported that the decrease of financing hit bottom in August 2009 and since then there has been a trend towards recovery. The month average growth of all portfolios from August 2009 to February 2010 has been 0.5 percent.¹⁵³ The number of default loans has also gone down from 4 percent in June 2009 to 3.3 percent in February 2010. Deschamps stated that the prudential measures adopted by banks in recent years have, unlike before, allowed the banks to face the recession and financial instability with strength.¹⁵⁴

Other factors that are different for Mexican banks in this financial crisis are capitalization and market penetration. Deschamps reports that the capitalization level in December 2009 was 17.3 percent. He also states that the number of bank clients has increased by more than 15 million since 2003 and has almost doubled in credit and debit cards in the last 5 years.¹⁵⁵ Both

¹⁴⁶ See Astrid Espinoza, *México resistirá salida de capitales*, CNN EXPANSIÓN, Apr. 23, 2010, <http://www.cnnexpansion.com/economia/2010/04/23/mexico-tasas-estados-unidos-cnnexpansion>.

¹⁴⁷ *Id.*

¹⁴⁸ *Id.* (Translation by author of this work).

¹⁴⁹ *Id.*

¹⁵⁰ *Id.*

¹⁵¹ Israel Rodríguez and Víctor Cardozo, *Reestructuran deuda de 1.9 millones de usuarios*, LA JORNADA, Apr. 22, 2010, available at <http://www.jornada.unam.mx/2010/04/22/>.

¹⁵² *Id.*

¹⁵³ *Id.*

¹⁵⁴ *Id.*

¹⁵⁵ *Id.*

factors demonstrate a more mature banking sector than that which existed in the previous decade.

Although most voices at the Bank Convention were optimistic, one critic did point out areas that needed improvement. Guillermo Babatz, the president of the CNBV, stated that the financial system still requires adjustments because it does not correspond to an economy the size and sophistication of the Mexican one.¹⁵⁶ He highlighted that the credit granted to companies was still low in comparison with the size of commercial activities.¹⁵⁷ Additionally, he criticized that over the last five years there have been more errors than appropriate actions in consumer credits.¹⁵⁸

V. LEARNING FROM FINANCIAL CRISES

As discussed in part III, the most recent crisis has similarities and differences with previous ones. This part will discuss the measures taken by the Mexican government in reaction to financial crisis and explore whether there are lessons that can be derived from these experiences.

1. *Mexico's Reactions to the Recent Crisis*

According to the U.N. Economic Commission for Latin America and the Caribbean, Mexico's economic policy reaction to the global financial crisis contained certain measures.¹⁵⁹ Pursuant to the initial summary report, the Mexican government did the following: in terms of monetary and financial policy, it provided liquidity in the national currency; in tax policy, it increased spending in infrastructure; in trade policy, it reduced tariffs; it provided support to small and medium-sized companies; and it created employment programs.¹⁶⁰

Furthermore, to combat the crisis the *Banco de México* released into the market a maximum of 400 million dollars a day, while maintaining a healthy reserve of dollars in an effort to reduce volatility in the exchange rate.¹⁶¹ Ad-

¹⁵⁶ Jeanette Leyva et al., *Desfasado, el sistema financiero*, EL FINANCIERO, Apr. 23, 2010, <http://www.efectoespejo.com/archives/11170> (last visited July 1, 2011).

¹⁵⁷ *Id.*

¹⁵⁸ *Id.*

¹⁵⁹ See Comisión Económica para América Latina y el Caribe, *Competitividad. La reacción de los gobiernos de América Latina y el Caribe frente a la crisis internacional: una presentación sintética de las medidas de política anunciadas hasta el 10 de diciembre de 2008*, <http://competitividad.org.do/wp-content/uploads/2009/02/la-reaccion-de-los-gobiernos-de-america-latina-y-el-caribe-frente-a-la-cri-sis-financiera.pdf> (last visited May 3, 2010).

¹⁶⁰ *Id.*

¹⁶¹ Ortiz, *supra* note 103.

ditionally, a special liquidity window was made available to commercial banks to allow them to receive automatic financing, agreements were made at an international level to allow Mexico to have access to dollars from the Federal Reserve, if needed, and programs were put in place to foment growth and employment, to name a few of these measures.¹⁶²

2. *Lessons Learned*

One can learn both from Mexico's past and recent financial crisis experience. In the 1990s, banks were left completely in the hands of the private sector and it soon became obvious that there would be no self-restraint. In the face of competition and in their attempt to gain market share, banks did not properly measure the risks. The government stood on the sidelines. The banks went from being a nationalized sector to being privatized in a short period of time. The government's position went from complete control to not supervising and regulating. The newly privatized banking sector was transformed from a protected sector, allowing little foreign investment, to almost completely foreign owned. The swings have been sudden and in response to crises. Nevertheless, although banks seemed to have matured and reacted more favorably recently, the issue of the impact of foreignization on the consumer leaves room for further research.

The global nature of the financial crisis has made clear that financially integrated markets, while offering benefits in the long run, pose significant short-term risks, with large real economic consequences, and that reforms are needed to the international financial architecture to safeguard the stability of an increasingly integrated global financial system. Such reforms need to be guided by the right principles rather than being formulated as rushed responses to the public pressure.¹⁶³

Apparently, Mexico learned its lesson in 1995. Its banking sector, albeit more regulated perhaps to the disdain of bankers, did weather the storm of the most recent financial crisis. Risks were reduced.

Therefore, one lesson that the international community can learn from the Mexican experience is the importance of having a sound banking system in order to increase resilience of the economy to future shocks [...] Overall, a sound financial system reduced significantly the vulnerability of the Mexican economy to the external shocks that were occurring since 2008.¹⁶⁴

¹⁶² *Id.*

¹⁶³ Claessens *et al.*, *supra* note 105.

¹⁶⁴ Víctor Pavón-Villamayor, *Case study 3 – Mexico*, in REGULATORY REFORM FOR RECOVERY, LESSONS FROM IMPLEMENTATION DURING CRISIS (OECD, 2010).

Although there is no quick check list of lessons learned, some aspects are worth reviewing. In times of crises vulnerabilities and shortcomings become more evident. For this reason,

[...] international reform efforts in prudential supervision are currently focused on making the financial system more resilient to shocks. The reform proposals include measures to improve the quality and risk coverage of Basel II capital requirements, improving global liquidity standards to make financial institutions less vulnerable to fluctuations in short-term wholesale funding [...] The new architecture for supervision and regulation has been labeled “macro-prudential” in nature —that is, the focus is on maintaining the soundness and resilience of the financial system as a whole and its interconnecting parts rather than just the solvency of individual financial institutions.¹⁶⁵

In 1995, Mexico rightly created the CNBV to supervise the financial system. The question is whether this can be done at an international level.

One thing that has recently been done at an international level, as a result of the crisis, has been the creation of new global rules that aim at balancing safety and growth.¹⁶⁶ In order to prevent a future financial collapse, financial authorities from 27 countries met in Basel, Switzerland, to draft new rules for the banking industry. According to Nout Wellink, chairman of the Basel Committee on Banking Supervision, “The system does not have the capacity for another round of bailouts, nor does the public have the tolerance for it.”¹⁶⁷ As a result of this meeting, new rules, informally known as Basel III, have been drafted to raise the capital requirements banks must fulfill. “Under the current rules, banks must hold bank at least 4 percent of their balance sheet to cover their risks. This mandatory reserve —known as tier 1 capital— would rise to 4.5 percent by 2013 under the new rules and reach 6 percent in 2019”.¹⁶⁸ Although some argue that this will safeguard against future risks, others, such as the Institute of International Finance, argue that the higher capital ratios could slow economic growth.¹⁶⁹ Because new regulations usually respond to the previous crisis, it is yet to be seen whether these new rules will help prevent the next crisis. What is certain is that, as the Mexican case has demonstrated, because of the strategic nature of financial services, govern-

¹⁶⁵ Brevan Cook & Felix Delbruck, *The Crisis and the Reserve Bank's Stabilization*, http://www.rbnz.govt.nz/research/bulletin/2007_2011/Mar10_73_1Cook_Delbruck.pdf.

¹⁶⁶ See Greg Keller, *Global Banking Rules Aim to Balance Safety, Growth*, WASH. POST, Sept. 12, 2010, available at <http://www.washingtonpost.com/wp-dyn/content/article/2010/09/12/AR2010091202138.html>.

¹⁶⁷ Andrew Ross Sorkin, *New Banking Rules Expected to Ease Shocks*, N. Y. TIMES, Sept. 10, 2010, available at <http://dealbook.nytimes.com/2010/09/10/new-banking-rules-expected-to-ease-shocks/>.

¹⁶⁸ See Greg Keller, *supra* note 166.

¹⁶⁹ See Andrew Ross Sorkin, *supra* note 167.

ment regulators need to keep a closer watch on this sector and not leave its regulation to the invisible hand of the market.

Finally, not only does the financial sector need to be kept in a healthy regulatory environment, but when bank failures arise, the manner in which the bailout is conducted also matters. Thus, in this case, a lesson to be learned from the Mexican experience is what not to do. In case of crisis, if one remembers the three basic rules set out by Rojas Suárez and Waisbrod, then future bailouts can be conducted in a manner that does not repeat the Mexican mistakes. Perhaps this is where the U.S. bailout plan differed. As Sandoval correctly claims, the TARP began with some of the same problems that the FOBAPROA had, primarily due to the lack of public information, the misuse of discretionary powers and had similar initial results (conflicts of interest, fraud and looting). However, in the United States, because of the public outrage and a new administration, the TARP bailout process changed its course. The new Obama administration went into the banks' guts (payroll) and said actions would be taken to cut top executives' pay between 50 and 90 percent.¹⁷⁰ "In a report released in July 2010, Kenneth R. Feinburg, President Obama's special master for executive compensation, said that nearly 80 percent of the \$2 billion 2008 bonus pay was unmerited."¹⁷¹ Because of greater scrutiny and supervision, as well as the U.S. public's voicing its contempt of the banks and bankers, results, thus far, appear to be different. Criminal prosecutions of those defrauding taxpayers' money (TARP) are applauded and the message that there will be consequences for such actions resonates in U.S. financial circles.

VI. CONCLUSIONS

As noted in this work, Mexico has had its share of crisis and of bank failure. The liberalization movement of the late 1980s and early 1990s, as part of the policy reforms advocated by the Washington Consensus, transformed the banking sector from a nationalized bank, to a privatized and protected sector. Those that bought the banks were inexperienced, perhaps overzealous, in their attempt to recover their investment, and not very careful in assessing risks. Whether because of an external shock or bad banking practices, the banks quickly failed and had to be bailed out of their own mistakes. The Mexican government learned, at the taxpayers' expense, that closer supervi-

¹⁷⁰ See Stephen Labaton, *U.S. to Order Pay Cuts at Firms That Got Most Aid*, N. Y. TIMES, Oct. 21, 2009, available at www.nytimes.com/2009/10/22/business/22pay.html.

¹⁷¹ Louise Story, *Executive Pay*, N. Y. TIMES, Feb. 7, 2011, available at http://topics.nytimes.com/top/reference/timestopics/subjects/e/executive_pay/index.html?inline=nyt-classifier. However, in June 2010, six months into a compensation review of the country's 28 largest financial companies, the Federal Reserve found that many of the bonus and incentive programs that economists say contributed to the financial crisis remain in place. *Id.*

sion of this sector was needed. Additionally, a major incentive was there, international loans, to overhaul the regulation and supervision of the financial sector. Its new NAFTA partners and the international community were paying close attention to the changes made. Therefore, the reforms implemented post-crisis to provide for more oversight, preventive measures and establishing prudential rules were appropriate, and perhaps contributed to a more resilient banking sector in Mexico. In hindsight, other countries should have paid closer attention to the Mexican banking crisis and the measures implemented in consequence. The government response and bank bailout in Mexico presented an opportunity for other countries to learn what to do and what not to do. Given that studies demonstrate that certain common causes lead to bank failure, experience also shows that the responses of those involved may also be similar. Particularly, transparency is key and the bailout plan should maintain the public informed of how taxes will be spent, how much, and by whom. Furthermore, the misuse of such plans should be penalized. Enforcement is crucial. Consequently, governments must be cautious not to repeat the mistakes of the past and learn from the experiences, and mistakes, of other countries. Nevertheless, in 1995, nobody would have predicted that 12 years later the United States would face a very similar experience, with a much greater global impact, in which learning from the Mexican case would have been commendable.