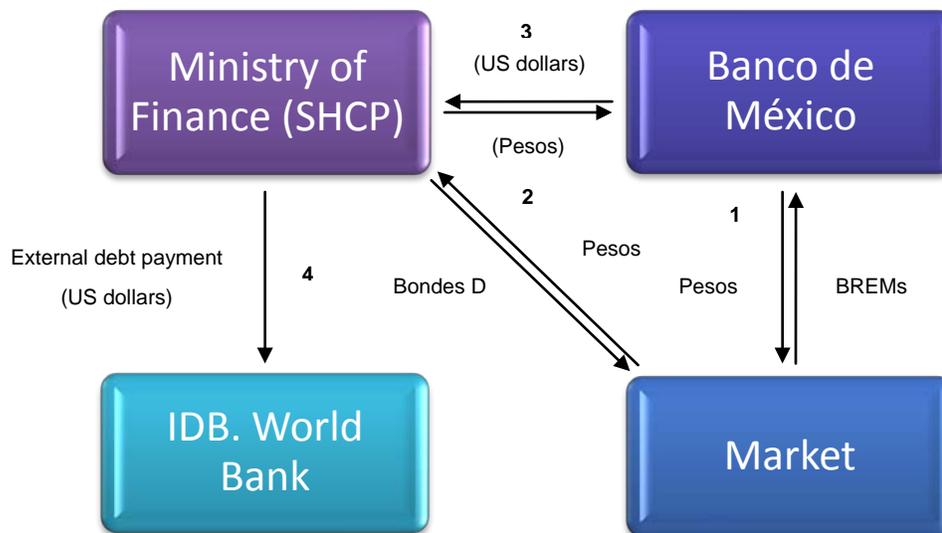




# BANCO DE MÉXICO

## US dollar sales to the Federal Government, BREMs auction repurchase and Bondes D exchange<sup>1</sup>

In August 2006, the Ministry of Finance (SHCP) announced its decision to prepay its debt with the World Bank and the Inter-American Development Bank (IDB). Such debt had been issued at less favorable terms than the cost of financing available to the government in that moment. The resources for such operation came from the federal government's issue of Bondes D for a total of 135 billion pesos. In a simultaneous operation, Banco de México withdrew an equal amount of BREMs. Bondes D have the same characteristics as BREMs and are used by Banco de México for monetary regulation purposes. Thus, although the total level of federal government debt remained constant, the cancellation of external debt reduced its vulnerability to exchange rate fluctuations. The decrease in the stock of international reserves in Banco de México implied a lower net cost for the central bank given the parallel decline in its peso denominated liabilities, which pay higher interest rates than those received by US dollar investments. This operation was well received by the market, enabling the initial amount to increase from 7 to 12.5 billion US dollars. The funds were used to repay liabilities with the World Bank and BID for 9 billion US dollars, as well as debt repurchase.



<sup>1</sup> Excerpt from the Financial System Report 2006

As a result of the operation described above, the stock of BREMs in circulation at the end of March 2007 was around 101 billion pesos, a figure equivalent to 1.1 percent of GDP. Starting in August 2006, Banco de México ceased to issue such securities in its liquidity management operations, substituting them for Bondes D (federal government bonds with similar features as BREMs).<sup>2</sup>

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<sup>2</sup> Bondes D are federal government liabilities. For this reason, Banco de México reimburses their financial cost to the government. Banco de México also uses Monetary Regulation Deposits to neutralize excess liquidity in the financial system. As of December 2006, the stock of Monetary Regulation Deposits was 279 billion pesos.