The debt bomb is set to explode in Mexico—again

by Dennis Small and Carlos Cota Meza

The following two articles are taken from a longer study of the Mexican physical economy which was published in the Feb. 1, 1997 issue of EIR*'s Spanish-language magazine,* Resumen Ejecutivo.

The band once again struck up a cheery tune on the deck of the sinking *Titanic* in early January 1997, as groups of bedraggled passengers in bankers' three-piece suits, with forced smiles plastered on their faces, strutted out onto the dance floor to go through their paces for the umpteenth time.

The government of Mexico had just managed to pre-pay a $5 billion installment on the $50 billion loan package it had lined up from the United States government and the International Monetary Fund (IMF) in the aftermath of the December 1994 explosion of the debt bomb in Mexico. The London *Financial Times* pontificated that this "marked something of a watershed for the embattled country," and applauded "Mexico's rapid economic turnaround." The British wire service, Reuters, pronounced that Mexico had finally "shed the stigma of the peso crisis." And Mexico's President Ernesto Zedillo happily concluded, "We have overcome the economic emergency." Mexico, the pundits all agreed, had once again "turned the corner."

It is now widely admitted, as only *EIR* had reported at the time, that the Mexican meltdown of 1994 nearly sank the entire world financial system. But the policies adopted since then, both in Mexico and internationally, have totally failed to address the underlying cause of the crisis: that global monetary aggregates, let alone the financial aggregates that have been speculatively pyramided on top of that monetary growth, have expanded hyperbolically and out of all proportion to the physical economic activity which ultimately must sustain them.

This global problem has only worsened since December 1994. And for Mexico, specifically, the steps taken have *not* solved the problem, nor even turned the corner, contrary to what the world has been told. As the following study of Mexico's physical economy proves, everything that has been done to deal with the crisis since that time, has been exactly the opposite of what is actually required, and has thus made things worse. Rather than building up Mexico's productive apparatus, it has been further decimated, at the IMF's insistence. And, instead of containing the speculative debt bubble, that cancer has simply been fed and given a new lease on life—and it is once again growing out of control.

The picture that emerges is of a nation that is rapidly becoming "Africanized." Since the relative high point of Mexico's economic development in 1981, IMF policies imposed on Mexico have wiped out 22% of its per-capita production of consumer goods and 29% of its producer goods, and have left half of its labor force unemployed. Manufacturing workers have become a dying breed, plunging from 10% to less than 5% of the total labor force, and science and engineering have become lost arts. The cancer of the *maquiladora* assembly plants is rapidly taking over the economy, setting up virtual Auschwitzes south of the U.S. border, as required by George Bush's North American Free Trade Agreement.

As a result, Mexico today, two years later, stands at the precipice of a debt bomb explosion—again. And just as it was two years ago, Mexico in 1997 is both a microcosm, and a harbinger, of what is to come in the world financial system as a whole.

Two years of destruction

Precisely two years ago, in January 1995, *EIR* published an in-depth study of Mexico's physical economy in order to explain the causes behind the December 1994 meltdown. In that study, we looked at the production of standard market baskets of consumer goods and producer goods, during 1970-94. For each of the items included in our two market baskets, we calculated physical production per capita or per household, measured in actual physical units such as tons, kilowatts, and so on, taken principally from official government statistics published by the National Institute of Statistics, Geography, and Information (INEGI). These series were then converted into indices (1981 = 100), and combined into an equally weighted composite index for each market basket.

The result was a useful, if crude, first approximation of what had happened with key elements of Mexico's physical economy over the last 25 years. There was a consistent pattern of modest growth from 1970 through 1981, and then a visible, across-the-board collapse beginning in 1982 with the

application of IMF policies.

The study which follows below, both updates and expands significantly upon our report of two years ago.

In the case of *consumer goods,* our new market basket is made up of 12 items (as opposed to 11 considered in 1995), and updates the data from 1994 to 1996. Although the overall market basket had already declined by 16% from 1981 to 1994, another 6% was lost in the last two years alone—an acceleration of the crisis as a result of the policies adopted in the wake of the 1994 debt blowout. Total grain production per capita, for example, had already dropped from 370 kilograms per capita in 1980, to 302 kg in 1994, but it then fell again to 283 kg per capita in 1996—a 7% plunge in just two years. Furthermore, imports of food items to help fill the gap have also fallen off, because Mexico has no money for imports but only for debt payments, and hunger is now threatening to pass over into starvation in significant parts of the country.

As for *producer goods,* we have expanded our market basket from 8 items considered in our first study, to 16. Available data in this area are not as current as for consumer goods, so our earlier picture went up to only 1991, and the current one goes only to 1994—i.e., still before the big collapse of the last two years. Even so, the market basket of producer goods production also shows an additional drop of about 7%, from an index level of 76 in 1991, to 71 in 1994 (see **Figure 1**). It is certain that when the data come in for 1995 and 1996, they will show that production plummeted even more rapidly in these two years.

One typical example is that of iron production, which dropped from 548 kilograms per household in 1991, to 524 kg in 1994. Capital goods were hit even harder: The production of electrical machinery and equipment, for example, fell almost by half, from an index of 48 in 1991, to 26 in 1994.

EIR's 'standard market basket' defined

In addition to updating our earlier study of consumer and producer goods, the current report includes a number of new features that allow for a broader and more thorough analysis of the Mexican physical economy.

In the current study, *EIR* has for the first time compiled a market basket of 10 *infrastructure*-related products and activities, in order to profile this critical area of economic functioning. Although preliminary, our findings are consistent with the picture in consumer goods and producer goods: The infrastructure market basket index rose modestly from a level of 87 in 1970, to a peak of 100 in 1981, and then fell back to a level of 88 by 1994 (see Figure 1). Here, as well, the data for 1995 and 1996 are unavailable, but will certainly show an accelerating rate of collapse.

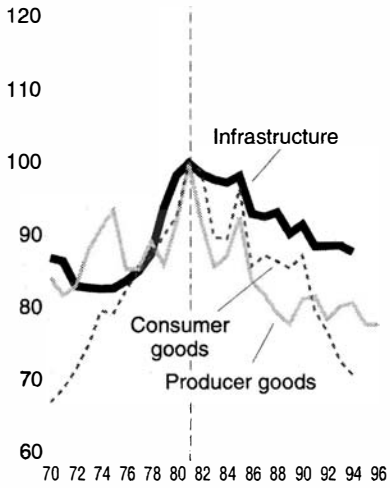
The second new feature is the development of a "standard market basket," or norm, for Mexico, for purposes of judging actual physical economic performance by comparing current levels to what they should be. In similar *EIR* studies of the U.S. economy, a 1967 standard market basket has been used, because that year marks the high water mark for the United States in most areas of physical economic activity, after which there has been steady collapse. As such, it reflects a level that must be returned to—as a jumping off point for subsequent development.

In the case of Mexico, however, it is not appropriate to use 1967 or 1970 per-capita and per-household levels of production as a standard, because there was real economic growth for another decade or so after that. The 1981 levels, although the high point over the last 25 years, are not an adequate standard either, because the absolute levels of output that year, per capita and per household, in general were woefully inadequate to the objective tasks of development: It would thus be misleading to judge Mexico's current performance by simple comparison to such levels.

Although it would certainly be good if Mexico, as an interim step, returned to where it was in 1981, a far better market basket standard can be developed by calculating what the level of per-capita production would have been, in each successive year, *had the average annual rates of modest growth over the 1970-81 period continued over the next 15 years, from 1981 to 1996.* It is that standard, calculated on a year-by-year basis, which we have selected as *EIR*'s "market basket standard" or norm. Each year's current real output can then be described as a percentage of what it should have been in that year—or would have been, had IMF policies not been imposed.

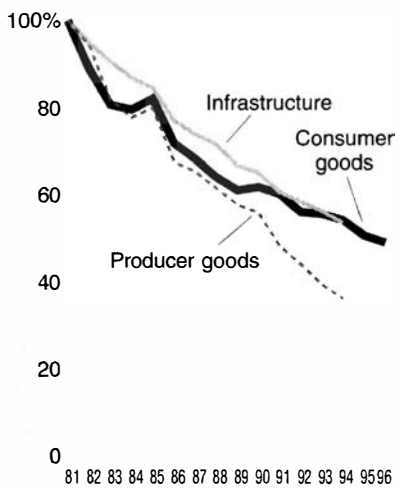
Measured against this standard, the production of the market basket of consumer goods in 1996 was 49% of what it should have been; producer goods in 1994 were at 38% of the standard for that year; and infrastructure in 1994 was at 49% of the standard (see **Figure 2**). This is the shocking reality of what has happened to Mexico's physical

FIGURE 1
Consumer goods, producer goods, and infrastructure
(index 1981=100)



Sources: Food and Agriculture Organization (FAO); United Nations Economic Commission for Latin America and the Caribbean (ECLAC); United Nations (UN); National Institute of Statistics, Geography and Information, Mexico (INEGI); Bank of Mexico (BdM); National Population Commission, Mexico (Conapo); Ministry of Trade and Labor, Mexico (SCT); Federal Electricity Commission, Mexico (CFE); Ministry of Energy, Mines and State Industry, Mexico (SEMIP); Ministry of Agriculture and Water Resources, Mexico (SARH); Ministry of Finance (SHCP); Ministry of Commerce and Industrial Development (Secofi); *EIR.*

FIGURE 2
Consumer goods, producer goods, and infrastructure
(% of standard market basket)



Sources: FAO, ECLAC, UN, INEGI, BdM, Conapo, SCT, CFE, SEMIP, SARH, SHCP, Secofi, *EIR.*

economic potential under IMF dictates: It has been more than halved.

Labor force and metric

The third new element in the present study, is a survey of the recent evolution of Mexico's labor force, which we present in the section immediately below. Here is where we see the worst damage done to the Mexican economy—and further proof that current policies are leading to another blowout.

Out of a total population of about 95 million in 1996, there are approximately 34 million who are considered part of the "economically active population," or labor force. Of these, 16.8 million are in reality unemployed—more than 2 million of them having joined the ranks of the unemployed in the last two years of "rapid economic turnaround," as the *Financial Times* happily put it. In other words, as opposed to the laughable official figures, Mexico's real unemployment rate today is 49%—and growing. Soon, more Mexicans will be unemployed than hold real jobs. This is the surest sign of a dying economy, of what might be called the "Africanization" of Mexico.

The number who hold *productive* jobs (see section below for definitions of this and other categories) has stagnated at just over 8 million, ever since 1983, which has meant a proportional decline from 37% to 24% of the labor force. And the number employed in the all-important manufacturing sector has declined, from a high of 2.3 million in 1981, to 1.6 million in 1996. Rather than being employed in new manufacturing jobs at higher skill levels, hundreds of thousands of Mexicans have been driven, at best, to slave labor jobs in the *maquiladora* assembly plants along the border with the United States—the legacy of Bush's NAFTA. Thus, employment in manufacturing in Mexico proper, taken as a percentage of the labor force, shows a decline from about 10% of the labor force throughout the 1970s, to an abysmal level of less than 5% by 1996.

These labor force proportions raise the central question of the proper metric, or yardstick, to be employed in measuring the performance of a physical economy. Measuring in terms of dollars or other monetary units is clearly meaningless, because it has little or no connection to the physical economic reproductive process. Any fixed physical unit, such as tons, is also useless: It may seem to work to measure performance within one product line over a specified time frame (which is the limited use we have given it in our market basket approximations), but it is clearly inapplicable as a unit of measurement across different products (that is, a ton of coal is not commensurable with a ton of wheat or, more to the point, a ton of machine tools). And, more important, such fixed physical units cannot take into account the changes in the actual value of given products that are brought about by the ongoing *technological* advance, which is the central feature of any successful economy. (For example, a ton of coal in the technological mode of 1920 is absolutely *not* the same thing as that same ton of coal in the technological mode of 1990.) This is the point at which all formal classroom mathematics breaks down, in being able to explain or measure the process which occurs in the physical economy.

In point of fact, as Lyndon LaRouche has explained his fundamental discovery in physical economy, economic growth is driven by constant technological progress, which produces discontinuous leaps as a society advances. Those technological breakthroughs are, in turn, *causally produced* by human creativity alone, which both generates new scientific concepts and spreads them throughout the economy. In this, the machine tool sector plays a critical role, as the strategic sector where such advances in ideas are transformed into machine tool designs.

Thus, it is man's creativity, as reflected in the development of the productive powers of the labor force, through rising skill levels, which is the only proper (non-mathematical) metric for an economy—and for the entire physical universe, for that matter. As Cardinal Nicolaus of Cusa explained in his 1450 dialogue, *The Layman: On Mind,* "mind is the measure of the universe."

The relative success or failure of a society to foster such creativity, LaRouche has explained, is then expressed as the potential relative population density which that society is capable of sustaining.

FIGURE 3
A typical collapse function

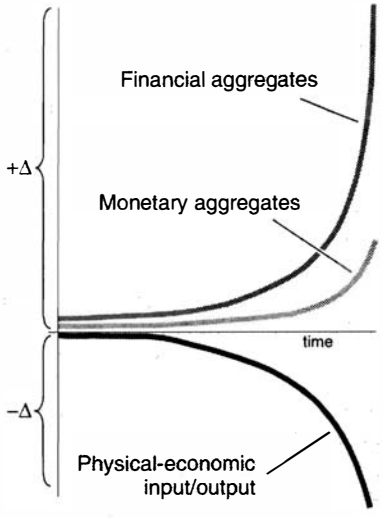
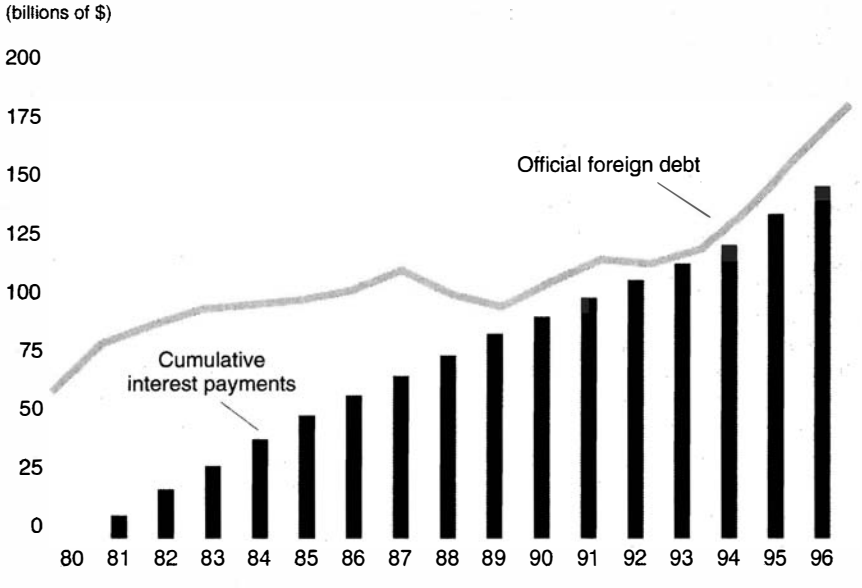
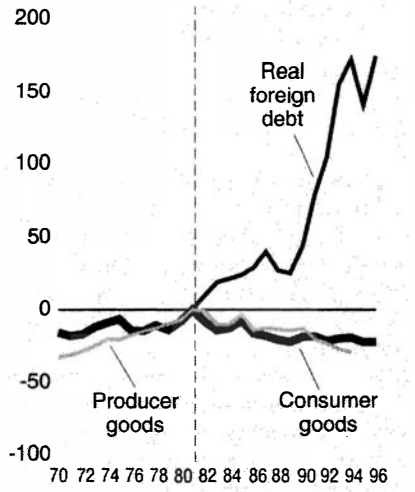


FIGURE 4
Foreign debt and interest payments



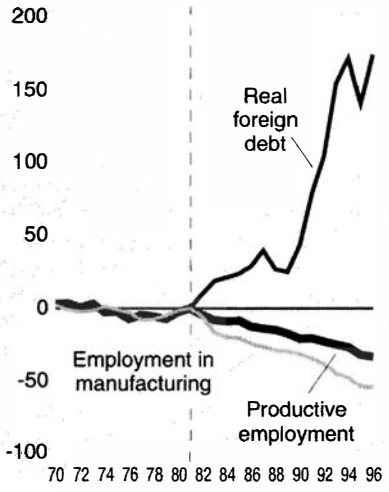
Sources: World Bank, SHCP.

FIGURE 5
Typical collapse function (Mexico)
(index 1981=0)



Sources: FAO, ECLAC, UN, World Bank, INEGI, BdM, Conapo, SEMIP, SARH, SHCP, Secofi, *EIR*.

FIGURE 6
Typical collapse function (Mexico)
(index 1981=0)



Sources: FAO, ECLAC, UN, World Bank, INEGI, BdM, Conapo, SCT, CFE, SEMIP, SARH, SHCP, Secofi, *EIR*.

It is with those considerations in mind that we have emphasized, wherever the data were available for Mexico, not the absolute numbers of employment, but the shifting internal *proportions* of the labor force (that is, the share of the total which is deployed to each economic task), as a superior metric for capturing actual economic trends.

Mexico's typical collapse function

In the concluding section of this study, we contrast the collapse of Mexico's physical economy, with the continuing wild growth of its foreign debt obligations. It is the impossibility of continuing to sustain this debt bubble as the real economy collapses, which guarantees the imminent next explosion of the debt bomb in Mexico. This is, of course, only a microcosm of the global financial situation.

LaRouche has repeatedly described this global process, with the help of his famous "Typical Collapse Function" graphic (see **Figure 3**). Here we see how hyperbolically collapsing physical-economic input/output becomes incapable of sustaining the hyperbolically increasing curves representing monetary aggregates and financial aggregates, that are leveraged on top of it.

Mexico's basic economic and financial parameters are almost a carbon copy of this LaRouche graph.

As the physical economy was collapsing by 7 to 10% over the last two years, Mexico's real foreign debt continued to skyrocket. In fact, the officially admitted component of this real foreign debt zoomed from $136 billion at the end of 1994, to $180 billion at the end of 1996—a 32% increase in two years. If we look back to 1980 (see **Figure 4**), we see that the official foreign debt was "only" $57 billion in that year; $150 billion in cumulative interest was paid over the next 15 years (almost three times what was originally owed), and yet the total foreign debt *rose* to $180 billion at the end of 1996. This is what we call "bankers' arithmetic": 57–150 = 180! Other categories of de facto foreign obligations have also begun to rise again, after their forced contraction in the year after the 1994 debt blow-out (see **Table 1**). Thus, Mexico is back on the exact same track which led to the last meltdown—all the while proudly proclaiming that it has "turned the corner."

If we look at the growth of Mexico's real foreign debt, against the market baskets of consumer goods and producer goods (see **Figure 5**), the parallels with LaRouche's typical collapse function are startling. Using 1981 as a base of 0, the real foreign debt has climbed quickly to an index of 175, while consumer goods output has dropped to −22, and producer goods output to −29. In **Figure 6,** a similar comparison is made with total productive employment and real employment in manufacturing (both taken as a percentage of the total labor force). Here we see productive employment dropping by a third to −33, while the manufacturing component plunged by half, to −54.

These, unquestionably, are "typical collapse functions," which can be expected to play themselves out, until Mexico and the world return to their senses. What that means is that the entire IMF system has to be put through bankruptcy reorganization, and the development of physical economy must become guided, once again, by what Cusa rightly called the metric of the universe: man's creative mind.

TABLE 1
Real foreign debt
(billions of $)

1) Public foreign debt	84	89	118	112
2) Private foreign debt	35	47	41	68
—owed by banks	20	25	21	?
—owed by companies	15	22	20	?
Official foreign debt (1+2)	**119**	**136**	**159**	**180**
3) 'Internationalized' internal debt*	26	32	5	3
—foreign-held Cetes, etc.	25	4	3	3
—Tesobonos	1	28	1	0
4) Foreign holdings in the stock market	55	44*	25	31
De facto foreign debt (3+4)	**81**	**76**	**29**	**34**
Total (1+2+3+4)	**200**	**212**	**188**	**214**

*as of Dec. 15, 1995

Sources: World Bank, ECLAC, BdM, SHCP, Secofi.