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Oil, trade deficit, and devaluation in Mexico

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When the Mexican government starts feverishly announcing that everything is fine on the economic front, Mexicans rightly prepare for another round of economic crisis.

The dramatic collapse in the world price of oil, a leading Mexican export, has vaporized the government's already precarious financial plans. The investment bank Goldman Sachs set the government trembling, when it recently reported that Mexico will need $51.2 billion to service its foreign debt in 1998, quite a jump over the $36 billion which the Mexican government had trumpeted, just a month before at the World Economic Forum in Davos, Switzerland, as "all" that it would have to come up with. Then, along came the Prime Minister of Singapore, Gho Chok Tong, who lectured Mexico's President Ernesto Zedillo: "If Mexico wishes to keep itself in the global economy, it will have to forget about a devaluation of the peso as a solution, and it had better seek ways to increase the productivity of its labor force."

Whatever the Prime Minister had in mind, his blunt statement intersected an intense battle within Mexico over the future exchange rate of the peso.

In late February, Trade Secretary Herminio Blanco, at the national congress of the Mexican Importers and Exporters Association, again advocated a peso devaluation, arguing that Mexico's "exchange rate policy is to avoid further deterioration of our trade." Guillermo Ortiz, governor of the Bank of Mexico (the central bank), immediately contradicted Blanco, telling a meeting of the American Chamber of Commerce of Mexico (AmCham), that "the response to the Asian crisis is not based on further devaluation." James F. McCabe, president of Amcham and president of Bank of America-Mexico, didn't take sides, but did note that the AmCham represents 85% of U.S. investment in Mexico, including major multinational corporations that, in light of the "reduction of costs" in Asia as a result of the crisis there, might well favor investments in that part of the world.

President Zedillo told the Mexican Council of Businessmen that the national economy "has had a highly satisfactory performance" since the Asian crisis exploded, but that in the near future, those economies will be strengthened, and therefore Mexico's "competitive position" could become "relatively weaker." Zedillo called for "increasing the rate of economic growth," in order to avoid "the recurring financial dislocations which have plagued the end of every Presidential term for the past quarter-century." As one local wag noted, Zedillo is talking about closing out his Presidential term, with three years still left to his administration.

Nothing balances out

The government statements, as effusive as they are contradictory, are in response to a simple problem: nothing balances out any more in the Mexican economy.

The Treasury Secretariat issued a report noting that, in January 1998, Mexico had a trade deficit of $565 million, the seventh consecutive month of such deficits. Although the government can, with some justification, blame the fall in the international price of oil for the crisis this year, the fact is that the entire IMF model imposed on the Mexican economy since 1981, is once again threatening to disintegrate, as a result of the same structural problems it has displayed since 1981-82.

According to information supplied by the Treasury Secretariat (which, as usual, does not jibe with that of the Bank of Mexico), the 1995 devaluation of the peso by more than 40% led to the reduction of imports by 8.68%, while exports grew 23%, leading to a trade surplus for the year of $7.1 billion. In 1996, imports grew 19%, while exports increased 17%, again producing a surplus, but only of $6.5 billion. In 1997, imports rose 18.5% and exports 13%, and as a result the trade surplus dropped to $624 million—a 90% reduction in one year. And in 1998, the trade deficit for January alone has wiped out 90% of the surplus from all of 1997. Not a very promising trend.

Furthermore, the composition of the balance of trade in January 1998, compared with the same month of 1997, shows clearly the lunacy of the government's operant "export at all costs to pay the debt" strategy.

Exports from the *maquiladoras* (the in-bond, cheap-labor assembly plants that line the U.S.-Mexican border) grew 18.9%, but non-*maquiladora* exports rose only 6.8%. Meanwhle, the price of Mexico's non-oil exports plummeted 23.5%, although the volume increased slightly.

To maintain this rate of growth of *maquiladora* and non-*maquiladora* exports alike, imports of intermediate goods grew 16.7%, imports of inputs for exporting companies rose 14.7%, and imports of inputs for non-exporting manufacturing companies grew 21.1%. Throughout 1997, one can see the same trend as in January 1998, where imports are outpacing exports, to the point that it is becoming more expensive to import inputs needed to maintain the *maquiladora* exports. The reality is that Mexico's trade surplus has always come from oil exports, ongoing devaluations of the currency, and starvation wages paid to Mexican workers.

If oil prices don't rebound, and soon, Zedillo will be facing another devaluation of the peso by close to 50%, as occurred in December 1994, which is what the Singapore Prime Minister was opposed to. The only other option is to finance the trade deficit the way his predecessor, Carlos Salinas de Gortari, went about it: by attracting highly speculative foreign capital, which was offered a rate of return which Mexico was never able to meet.

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