President Zedillo Bequeaths Mexico a 'Balkanized' Economy

by Carlos Cota Meza

The North American Free Trade Agreement (NAFTA) was launched in 1995, just as the new Mexican government, which finishes its term this year, took power. From the beginning, President Ernesto Zedillo tied the Mexican economy to the fate of the U.S. economy. The 1999 Annual Report of the Bank of Mexico proclaims that the U.S. economy has "had unprecedented expansion for the past nine years," and the result, according to Mexico's central bank, is that "the Mexican economy has had 16 consecutive quarters of uninterrupted annual growth." This performance of the Mexican economy is said to be a product of "the expansion of the United States' economy, which encouraged exports from Mexico."

If the driver of the Mexican economy's supposed growth has been the United States, this strategy is in urgent need of review. On April 14, Wall Street was hit by a crash, in which $2.1 trillion evaporated overnight. Two months later, the ashes are still being sifted, but among the preliminary losses are those of a reported 18 million greenhorn investors. The U.S. economy, whose negative domestic savings rate helped to inflate the speculative bubble, is fracturing.

According to official estimates, families in the United States in 1998 had 53.9% of their financial assets invested in stocks. The fall in speculative income they have suffered in recent months, has necessarily been reflected in reduced consumption, such that many commentators are now predicting an economic "recession" in Mexico's neighbor to the north, which would in turn cause a "deceleration" of its imports, and of exports from Mexico as well as from other parts of the world. The Mexican government's response to the April 14 stock market crash has been to repeat over and over: "There will not be a recession in the United States." But, although no one wants to believe it, the effects of just such a recession are already being felt.

The 'Benefits' of Globalization

Supposedly having benefitted from U.S. expansion, in 1999 Mexico registered a trade deficit of $5.361 billion. Exports were $136.7 billion, and imports $142.064 billion. Against all logic, the Mexican government customarily considers a trade deficit as something positive.

Mexico has an "abundant" consolidated surplus with the member countries of NAFTA, the result of a surplus with the United States and a deficit with Canada. There is a surplus with the rest of the Americas, although this has declined by 50% in the past two years. The trade deficit with the rest of the world is of a truly inexplicable amount, surpassing the surplus with the United States by 20% (see **Table 1**).

This picture of Mexican foreign trade by regions, demonstrates how the U.S. economy is eating up a portion of the Mexican economy (one-third, according to official figures).

Total exports, measured as a portion of the GNP, reached 32.7% (29.8% in 1998), while 71% of total imports of intermediate goods ($109.359 billion), were used for export. The "degree of opening" of the Mexican economy (according to the Bank of Mexico's calculations), which is expressed as the sum total of exports and imports of goods and services as a percentage of GDP, is 65.5%. The Mexican economy's dependence on foreign markets is unprecedented in the entire history of the national economy.

The trade deficit with the rest of the world has to be seen from the standpoint of what it means for the economies in which those imports originated. What do the Europeans and Asians think of the fabulous amounts Mexico is buying from them in excess, and which use the Mexican economy as a

TABLE 1
Mexico: Balance of Trade, by Region
(millions $)

	1997	1998	1999
NAFTA Zone	**12,490**	**9,064**	**14,605**
a) United States	12,301	9,835	15,253
b) Canada	189	–771	–638
Rest of the World	**–11,866**	**–16,977**	**–19,976**
a) Rest of the Americas	4,022	2,975	2,010
b) Europe	–6,270	–8,248	–7,821
c) Asia	–9,106	–10,902	–13,092
d) Other	–512	–766	–1,073
Total	**624**	**–7,913**	**–5,361**

Source: Bank of Mexico.

trampoline into the U.S. economy, both as finished and semi-finished goods?

Recently, the Sony representative in Mexico, Shin Takaga, told President Zedillo what will undoubtedly become the key topic of debate in the months to come. Speaking in the name of the *maquiladoras* (cheap-labor, foreign-owned assembly plants), Takaga told Zedillo that government action is needed with regard to both public and legal security of companies in Mexico. The situation in Mexico, he said, "is beginning to give reasons enough for the company to decide to reduce its investment or transfer its installations to a secure country."

Apart from the issue of public security, the *maquiladoras'* complaint is about regulations established by NAFTA for the permanent establishment of a company (everything up to now has been done under "temporary status"), payment of tariffs, preferential tax regime, tax exemptions for inter-*maquiladora* operations, etc. For Sony, the *maquiladoras* are losing competitiveness, "since multinational companies have the possibility of importing their finished products from their own group's companies in Asia."

What was not supposed to happen, did. The "profitability" of the Asia-Mexico-United States triangle is dwindling and, given their predatory nature, the *maquiladoras* are now threatening to go elsewhere, unless Mexico once again becomes "competitive."

A decline in *maquiladora* activity shows, once again, that the country is bankrupt, and that the attempts to maintain it as a "model" since 1982, have failed. As for the beautiful macroeconomic figures, they've also gone down the drain. We review them again here, so that those who declared themselves "deceived" in 1994, when the Mexican peso collapsed, don't do the same again in 2000.

For the fourth consecutive year in this six-year Presidential term (as occurred also in the previous government), the current account in the balance of payments had a deficit of $14.013 billion. The 1999 global deficit was the result of the trade deficit of $5.361 billion; the $1.619 billion deficit in non-factorial services (primarily payments for export and import insurance and shipping); and the $13.348 billion deficit in factorial services ($8.828 billion in interest payments, and $4.520 billion in profit remittances). The category of transfers showed a surplus of $6.315 billion (remittances from legal and illegal residents in the United States).

A current account deficit reflects the fact that internal investment, income, and consumption depend on a foreign capital inflow. Regardless of its origin as capital, the economy to which it goes must provide it with an "attractive" yield or earning. In order to export cheaply to the United States, Mexico incurs a trade deficit (more imports than exports), plus it pays shipping and insurance to foreign firms, and guarantees the transnationals a juicy repatriation of their profits. The remittances from emigrés, equal to 50% of Foreign Direct Investment (FDI), is the primary monetary flow sustaining the income and consumption of millions of Mexicans.

For the Zedillo government, this is a positive situation, since the current account deficit "is well financed" by long-term investment, like the $11.568 billion figure for FDI. However, an analysis of that figure shows that only $4.448 billion is new investment; $2.887 billion is a "reinvestment of profits," and $1.455 billion is "indebtedness" of Mexican branches of foreign companies. Add these two figures to the one for remittances, and you get the $8.847 billion in the "earnings" of multinationals—a figure equal to interest payments on the foreign debt!—and $2.778 billion is for machinery imports by the *maquiladoras*.

At the very least, it is odd that a trade deficit originating in Europe, Asia, and other countries is financed with FDI largely from the United States, with which Mexico has a trade surplus. In fact, the $15.253 billion surplus with the U.S. is used to pay the $19.976 billion deficit with the rest of the world—yet we still end up owing! The rest of the deficit shows up as an increase in the foreign indebtedness of "the non-banking private sector," which for 1999 was $6.786 billion.

As the Sony representative in Mexico has figured out, this fabulous structure of deficits and indebtedness has begun to fall apart, which is why he dared to make the noises he did to the Mexican President's face.

Globalization of the Banking System

President Zedillo's legacy is also the globalization of Mexico's commercial banks, which means the cutoff of credit to domestic productive enterprises. The Santander-Mexicano Group recently beat Britain's Hongkong and Shanghai Banking Corp. (HSBC) in the purchase of Banca Serfin, Mexico's third-largest bank. The Santander-Mexicano Group is an affiliate of the Banco Santander-Central Hispano, which in turn was a product of the merger of both banks in Spain. The Central-Hispano, which in Spain operates with British capital, in Mexico is a stockholder in Bancrecer.

There is something sordid in all this, since Britain's HSBC had a 19.9% stake in Serfin, because of agreements made with the Mexican government agency Fobaproa in 1997. Its participation to the tune of $139 million will be absorbed by Fobaproa's successor, IPAB. With the purchase of Serfin, foreign capital now controls 50% of Mexico's banking system—and the stench of corruption is in the air. The bailout of Serfin cost the government $12 billion, while the purchasers bought it for $1.460 billion, at an exchange rate of 10 pesos to the dollar.

At the same time, Spain's Banco Bilbao Vizcaya Argentaria (BBVA, a product of Argentaria and BBV in Spain), in association with the Bank of Montreal, is seeking to buy Bancomer, Mexico's second largest bank. The Bank of Montreal, which merged with the Royal Bank of Scotland, already owns 20% of Bancomer. In a hostile bid, Mexico's largest bank, Banamex, suddenly made a counteroffer for Bancomer, in association with Chase Manhattan Bank, JP Morgan, and the Aegon insurance firm.

If BBVA wins, foreign participation in the Mexican banking system will reach 73%; if Bancomex wins, the percentage won't vary much, given the size of its foreign partners.

The bewildered Mexican asks, what are they buying, if Mexican banks are bankrupt? Officially, the bailout of the banking system has cost $100 billion, or 20% of GDP. But that's not all. In 1999, there was a drastic reduction in fixed term bank deposits, suggesting that former depositors preferred other types of investment instruments. At the same time, in 1999, commercial bank financing for the private sector, in real terms, was only 56.9% of the figure for 1994.

The study "Mexico: Five Years after the Crisis," prepared by Joseph Stiglitz, former chief economist at the World Bank, establishes that the "Mexican financial market presents a form of segmentation, in which some companies dominate the internal financial credit market, while others rely more on the U.S. market." Foreign financing, according to this report, is concentrated "on promoting activities linked to the export sector." Moreover, it explains that the possibility of credit for the Mexican productive sector has nothing to do with availability or with the internal interest rate system. According to the daily *El Financiero,* Stiglitz's study concludes with the recommendation that "a currency devaluation is advisable."

Financing an Economy, without Banks

For the Bank of Mexico, the contraction of financing for the domestic economy has generated "an important change in the characteristics of the intermediation process . . . it has increased the importance of alternative sources of financing, for example, foreign banks and suppliers, thus reducing the role of national banks."

At the close of 1999, the Bank of Mexico's "Survey of Conjunctural Evaluation of the Credit Market" reported that "less than 40% of the companies polled used bank credit. Small or non-exporting companies apply the least frequently for this type of financing." For the first trimester of 2000, the Bank's survey found that 58.5% of small companies and 47.5% of medium-sized companies, "use suppliers as their main source of financing." What the survey doesn't measure is the "debt arrears to suppliers," which fluctuates between 60 and 90 days. In plain English, financing from suppliers is simply a sale on consignment: "I'll give you the merchandise, and you pay me for what you sell." Small and medium-sized industry accounts for approximately 30-35% of Mexico's GDP.

According to preliminary data from the XII Population and Housing Census 2000, by Inegi, the sector with the greatest growth in activities is "cottage industry," which is no longer only linked to "informal trade," but also with the survival efforts of small and medium-sized companies.

Thus, we have one-third of the Mexican economy totally dependent on the United States, and on an onerous trade and indebtedness operation on a global scale; while on the domestic side, another third of the economy survives by barter and by a "source of financing" which also depends on the United States.

Foreign banks are acquiring the Mexican banking and financial services sector (which is equal to 20% of the GNP), not because it is good business, but because they are going to impose atrocious conditions on the next government of Mexico.

No matter who stays with Bancomer, the new foreign banking syndicate will be in a position to impose banking, monetary, and credit measures on the Finance Ministry, the Bank of Mexico and, above all, on the Presidency of Mexico itself. Joining their international assets, the new syndicate will have more capital than the country has international reserves, and possibly even more capital than the money circulating in the national economy. With such power, they will be able to carry out their first conditionality, which is to impose a currency board and/or the "dollarization" of Mexico.

This is President Zedillo's legacy.