MEXICO

The Remaking of an Economy

SECOND EDITION

Nora Lustig

Brookings Institution Press Washington, D.C.

Contents

Preface to the Second Edition Abbreviations and Acronyms	xv xvii
PART I The Remaking of an Economy	
Introduction ·	1
Mexico's Adjustment and Recovery: A Summary 2 A Note on Method 12	
1. The Genesis of the 1982 Crisis	14
The Golden Years of "Stabilizing Development" 14 Macroeconomic Imbalances and the 1976 Balance-of-Payments Crisis 17 The Oil Boom and the Onset of the 1982 Crisis 20 Concluding Remarks 26	
2. From Crisis to Recovery The First Attempt at Stabilization, 1983–85 29 The Failure of the First Stabilization Program 34 From the 1986 Oil Shock to the 1987 Run on the Peso The Implementation of the Economic Solidarity Pact The Pursuit of Economic Recovery 55 Concluding Remarks 59	28 39 50
Concluding Remarks 59	ix

. The Social Costs of Adjustment	61
Adjustment, Living Standards, and Income Distribution	61
Living Conditions before the Crisis 65	
Trends in Earned Real Incomes since 1982 66	
Unemployment and Employment Patterns 75	
Social Income: The Evolution of Public Spending	
on Social Sectors 78	
Resource Availability in Education and Health 83	
Food Subsidies: From General to Targeted 86	
Social Indicators: Nutrition and Health, Education,	
and Incidence of Crime 87	
Household Survival Strategies 89	
Who Bore the Costs and to What Extent? 92	
Concluding Remarks 94	
. Public Sector Reforms	. 96
Fiscal Policy Reform 98	
Divestiture of Public Enterprises 103	
Deregulation 107	
Concluding Remarks 112	
;. Looking Outward: Reforms in the Foreign Trade	
and Investment Regimes	114
and investment regimes	114
Trade Liberalization 117	
Impact of Trade Liberalization on Economic Performance	120
Industrial Programs 122	
The Changing Foreign Investment Regime 125	
Intellectual Property Rights 129	
Joining the General Agreement on Tariffs and Trade 130)
Seeking Closer Ties with the United States 132	
Concluding Remarks 137	
Epilogue 140	

Contents	xi
PART 2 The Re-Remaking of an Economy	
6. Slow Growth and the Peso Crisis	143
Slow Growth: Why Were Reforms Not Paying Off? 147 The Devaluation in December 1994 154	
7. Rescue, Recession, and Recovery	172
The Unexpected Financial Debacle 173 The Rescue Package Is Increased 177 The Mexican Recession and Economic Recovery 190	
8. The Unhappy End: Poverty and Inequality	201
The Evolution and the Profile of Poverty and Inequality 201 Poverty in the Primary Sector: Why Did It Rise? 205 Economic Openness and Inequality 208 Living Standards and the Peso Crisis 209	
9. Conclusion	213
Appendix: Agreement Signed by Mexico and Its Commercial	
Banks on Debt and Debt Service Reduction	221
Notes	225
Index	281
Tables	
 1-1. Average Annual Growth Rates and Sources of Changes in Total Gross Manufacturing Production in Mexico, Korea, and Taiwan, Selected Periods, 1950-75 1-2. Percentage Distribution of Gross Domestic Product, 	15
by Sector, Selected Years, 1950–85	16

xii Contents

1-3.	Percentage Distribution of the Economically Active	
_	Population, by Type of Activity, 1950, 1960, 1970	17
1-4.	Leading Economic Indicators, 1956–76	18
	Economic Performance, 1976–81	22
2-1.	Fiscal Adjustment and Real Exchange Rate, 1980-91	30
	Debt Burden, External Shocks, and Net Resource	•
	Transfers, 1980–90	32
2-3.	Targets and Actual Performance of the First Stabilization	•
•	Program, 1983-85	35
2-4.	Indicators of Economic Performance, 1981–91	40
2-5.	Net Public Indebtedness, Net IMF Disbursements,	•
	and Interest Payments, 1982–90	48
3-1.	Demographic Characteristics of Households, Intra- and	
	Interdecile, Third Quarter,1984	64
3-2.	Evolution of Real Wages and Per Capita Private	
	Consumption, 1981–90	68
3-3.	Employment and Unemployment, 1981–90	70
3-4.	Wage and Nonwage Income, 1981–90	72
3-5.	Distribution of Total Household Income by Source,	-
	Third Quarter, 1984	73
3-6 .	Evolution of the Agricultural Sector, 1981–90	76
3-7.	Government Spending on Social Sectors: Total,	
	Education, and Health, 1980–90	80
3-8 .	Educational Resources, Total and Primary School,	
	Academic Years 1980–81 through 1991–92	82
3-9.	Human and Physical Resources in the Health Sector,	
	1980–91	84
	Social Indicators in Health, 1980–89	88
3-11.	Social Indicators in Education, Academic Years 1970–71,	
	and 1980–81 through 1991–92	90
	Income Distribution in Mexico, Selected Years, 1963–89	92
4-1.	Federal Nonfinancial Public Sector Revenues and	
	Expenditures, 1979–89	100
	Summary of the 1987 and 1989 Tax Reforms	102
	Number of Public Enterprises, 1982–90	10
4-4.	Top Ten Privatizations during the First Two Years of	
	the Salinas Administration	106
	Import Licenses and Protection Rates, 1956–83	115
5-2.	Import Trade Liberalization Schedule in Mexico, Main	
	Events and Characteristics, 1983–89	118
	Measures of Trade Liberalization, 1980–90	120
5-4.	Direct Foreign Investment by Source Country, 1989	12

	Contents	xiii
5-5.	The 1973 Foreign Investment Law and Limits to Foreign	
	Investment	127
	Mexico's Major Trading Partners, 1989, 1990	136
	Macroeconomic Indicators, 1989–96	144
	External Sector, 1989–96	148
	Financial Rescue Package, 1995	182
	Supply and Demand, 1989–96	188
	Real Wages and Unemployment, 1989–96	192
	Poverty Measurements	202
	Income Distribution	203
	Extreme Poverty by Subcategories	204
	Wage and Nonwage Income	206
8-5.	Social Spending according to Growth and GDP, 1989–96	211
Figur	es	
6-1.	Industrial Production and Employment in Mexico, 1988–93	151
6-2.	Nominal Interest Rates in Mexico and the United States	157
6-3.	International Reserves	159
6-4.	Mexico: Monetary Base and Domestic Credit	161
7-1.	Peso Exchange Rate, December 1994 to November 1995	194
7-2.	Nominal Interest Rates, 1995	195
7-3.	Real Interest Rates, 1995	196
7-4.	Profile of Domestic Debt	197
7 -5.	Maturities of External Debt	198
7-6 .	Inflation, November 1994–November 1995	198
7-7.	Evolution of GDP, 1991–96	199
8-1.	Skilled versus Unskilled Wages	209