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estudios y perspectivas

42

Mexico: Economic growth exports and industrial performance after NAFTA

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Mexico, D. F., December 2005

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The opinions expressed here are those of the authors and do not necessarily reflect those of the United Nations Organization. The authors acknowledge the useful conversations held with Enrique Dussel and Ramón Padilla on Mexico's industrial policies, as well as comments by Claudia Schatan and René Hernández. We also thank Emily Young for her valuable assistance in the edition of this paper, as well as Indira Romero for her efficient research assistance. A slightly different version of this working paper was recently published in *Development and Change*.

United Nations Publication

ISSN printed version: 1680-8800

ISSN online version: 1684-0364

ISBN: 92-1-121577-8

LC/L.2479-P

LC/MEX/L.700

Sales N° : E.06.II.G.6

Printed in United Nations, Mexico, D. F.

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Abstract

This article concerns Mexico's industrial policy and economic performance, focusing on an analysis of the structural changes associated with NAFTA that have occurred in the country's manufacturing sector. The purpose of the article is to improve our understanding of why the post-NAFTA evolution of the Mexican economy has been characterized by lights and shadows, with low inflation, low budget deficit and a surge in non-oil exports, and on the other hand a slower than expected expansion of economic activity and employment. The article also presents some implications of economic policy that are essential for formulating a new development agenda in Mexico by which the country can finally succeed in its endeavour to attain high and sustained economic growth.

Introduction

In 1994, Mexico, the United States and Canada launched the North American Free Trade Agreement (NAFTA) which, if not exactly a free trade initiative, was a path-breaking compromise to drastically reduce barriers to intra-regional trade.1 But for the Mexican government at that time, NAFTA represented much more than a trade-boosting venue. It was the culmination of a radical change in the development strategy that Mexico had implemented since the mid-1980s. This change involved abandoning import substitution and state-led industrialization, and adopting instead a strategy drafted along the lines of the so-called Washington Consensus, centred therefore on trade liberalization and a reduction of state intervention in the economy.

Within this new strategy, NAFTA was seen as a vehicle for achieving two goals. The first was to set the Mexican economy on a non-inflationary, export-led growth path, driven by sales of manufactured goods mainly to the United States. The underlying assumption was that NAFTA, together with the drastic macroeconomic reforms and rapid, unilateral trade liberalization initiated in the second half of the 1980s, would encourage local and foreign investment in the production of tradable goods, thus exploiting Mexico's potential as an export platform to the United States. The fast expansion of Mexico's

[1] Article 102 of the Agreement formally identifies NAFTA's main objectives: '[to] Eliminate barriers to trade in, and facilitate the cross-border movement of, goods and services between the territories of the Parties; promote conditions of fair competition in the free trade area; increase substantially investment opportunities in the territories of the Parties; provide adequate and effective protection and enforcement of intellectual property rights in each Party's territory' (NAFTA, 1994).

manufacturing sector —which would allegedly occur, stimulated by exports of labour— intensive products— would then pull the rest of the domestic economy onto a trajectory of high and persistent growth. It was furthermore argued that downsizing the public sector and eliminating subsidies would cancel the fiscal deficit and cut inflation. The second —and politically decisive— objective was to guarantee the lock-in of Mexico's macroeconomic reform process. Indeed, the Salinas administration (1988–1994) claimed that NAFTA imposed international legal and extra-legal constraints that would deter any attempt by subsequent governments in Mexico to return to trade protectionism.

For Mexico, NAFTA and the macroeconomic reforms in which it is embedded have been neither the panacea claimed by its supporters nor the disaster predicted by some of its opponents.[2] The great expectations to which it gave rise have been only partially fulfilled. On the one hand, Mexico's performance over the last ten years has been marked by a small budget deficit, low inflation, and a surge in non-oil exports and foreign direct investment (FDI). On the other hand, economic growth has been disappointing. Indeed, fixed domestic capital formation has been rather stagnant, while real gross domestic product (GDP) has grown at a rate way below its historical average and clearly insufficient to generate the number of jobs required by the country's expanding labour force. Moreover, the balance of payments constraint on the Mexican economy's long-term rate of growth has become more binding.

Using data from official sources, including INEGI, Banco de Mexico and ECLAC, the rest of the article is organized as follows: Chapter I gives a background to industrial policy in Mexico between 1940 and 1984 within the overall context of the macroeconomic reforms that have been implemented in the last four decades. Chapter II describes Mexico's road to NAFTA, concentrating on two key aspects: unilateral trade liberalization and foreign investment deregulation. Chapter III discusses whether NAFTA has put Mexico on an export-led growth path. Chapter IV gives an analysis of some stylized facts concerning foreign trade, economic growth performance and their implications in the context of NAFTA and manufacturing. The article closes with some conclusions and policy recommendations in Chapter V.