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A Mandate for Mexico

BY LUCY CONGER

Wilson Center
One Woodrow Wilson Plaza
1300 Pennsylvania Avenue NW
Washington, DC 20004-3027

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Introduction

It was not so long ago that Mexico teetered on the brink of bankruptcy following a short-lived oil boom and a wild run of government spending. And, until quite recently, Mexico, despite sharing a 2,000-mile border with the United States, kept foreign goods out and gave domestic industries nearly exclusive access to a country-sized captive market.

During the decades leading up to the 1980s, the Mexican president exercised virtually unchecked power. His ruling Institutional Revolutionary Party (PRI) controlled congress and all governorships for five decades straight and economic policy could and did change at the whim of the executive. The economy grew at robust rates year in and year out, and political control mechanisms of the state party included corporatist labor unions, media concessions and poor access to information, universal primary education, and some redistributive measures for the lower classes.

This solid record of economic stability, political control, and steady progress for citizens within a protected economy was shattered by the 1982 debt crisis. Mexico defaulted on its oil-fueled foreign debt, unleashing a financial and economic collapse. The ruling party suffered internal divisions over demands to restrict the president's ability to choose his successor, and the greatest opposition challenge ever, headed by PRI deserter Cuauhtémoc Cárdenas, created an intensely contested national election in 1988. PRI candidate Carlos Salinas de Gortari was declared the winner, but his victory was tainted by accusations of fraud.

Mexico's First Response

Mexico suffered a deep recession from 1983 to 1988 and a period of low growth with high deficits from 1988 to 1994. During this stretch, a series of economic reforms were launched to set the economy on a better course.[1] These reforms, led first by President Miguel de la Madrid and then by President Carlos Salinas, would transform the management of public finances, tame inflation, stabilize leading economic variables, reduce the number of state-held companies, lift regulations on some sectors, and ultimately make Mexico a free trader with the rest of North America. Taken together, Mexico, the United States, and Canada make up one of the very largest trading blocs in the world, with a combined GDP of more than $19 trillion today. The free trade agreement broke

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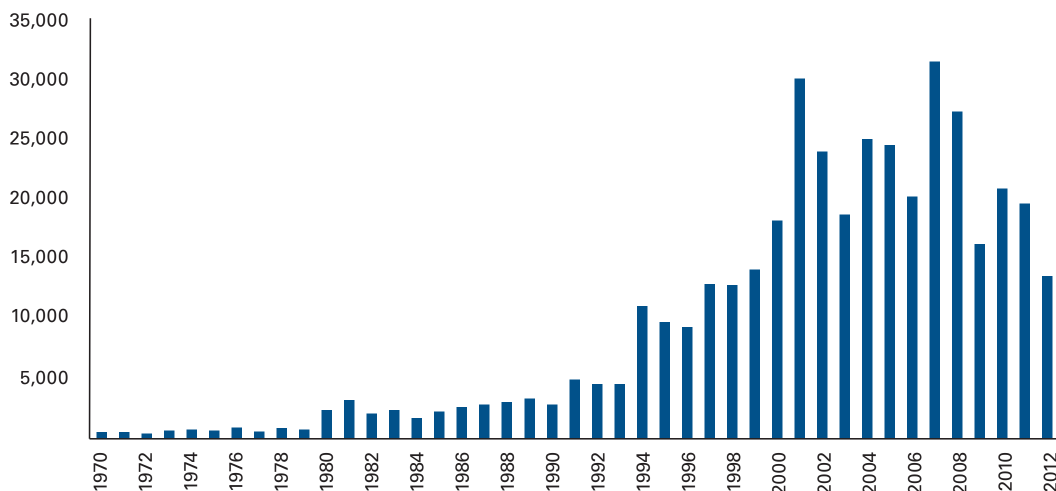
[1] The average annual growth rate of real GDP per worker averaged -3.05% from 1983-88 with an average current account balance of 1.17% of GDP. From 1998-84, annual growth of real GDP per worker was 0.75% and the current account balance was -4.93% of GDP. See Rodrigo García-Verdú, "Demographics, Human Capital and Economic Growth in Mexico: 1950-2005." World Bank, Poverty Reduction and Economic Management Unit, Latin American and the Caribbean region. June 2007, p. 8.

new ground by linking an underdeveloped country with developed economies on an equal footing, and foreign direct investment in Mexico rose sharply once NAFTA took effect in 1994.

Foreign direct investment, 1970 – 2012 (US$ millions)



Source: UNCTAD, 2013 as rendered in: Vergara González, Reyna, y Yolanda Carbajal Suárez. “La inversión extranjera en México, 1994-2012. Un análisis sectorial y por entidad federativa.” Universidad Autónoma de Madrid, 2013, Slide 8. http://www.econolatin.com/jornadas-latinoamerica/mexico_noviembre_2013/ponencia.pdf

Thirty years on, Mexicans and markets alike take it for granted that government spending and inflation will be held within reasonable parameters, the peso will not suffer sharp devaluations, economic growth will be fueled by trade in manufactured goods, and shoppers can choose their food and home appliances produced by an enormous range of domestic and foreign companies. Free trade has made Mexico a powerful manufacturing platform, a top global automobile assembler, and has radically diversified the economy, sharply reducing dependence on oil exports.

The paradigm shift that unfettered Mexico’s protected and closed economy has been highly successful in creating a stable economic and policy environment and in making Mexico a market-friendly global super-trader. But formidable challenges remain. Economic growth has slowed and consistently falls short of the level needed to create enough jobs to absorb the expanding domestic labor force. Alarmingly, Finance Minister Luis Videgaray believes that productivity growth has been negative over the last 30 years.[2]

[2] Videgaray, Luis. Interviewed by Leonardo Curzio on “Enfoque” radio program, April 23, 2015.

Even while attracting more foreign investment, Mexico's competitiveness has been poor during the reform period that began in 1985. The World Economic Forum Global Competitiveness Index for 2014-15 ranks Mexico as number 61 out of 144 countries, putting it near the mid-point.[3] This is a relevant drop from Mexico's ranking in each of the two previous reports, from 53 in 2012-13 and 55 in 2013-14. Mexico, a middle income country with the tenth largest market in the world, lags behind other emerging countries in overall competitiveness, such as China (ranked 28), Chile (33), and Turkey (45). It trails regional rival Brazil (57) but does edge Peru (65), Colombia (66), and India (71).

Mexico's Competitiveness measured by the World Economic Forum

Year	Mexico ranking / no. of countries
2014 - 2015	61 / 144
2013 - 2014	55 / 148
2012 - 2013	53 / 144
2011 - 2012	58 / 142
2010 - 2011	66 / 139
2009 - 2010	60 / 133
2008 - 2009	60 / 134
2007 - 2008	52 / 131
2006 - 2007	58 / 125
2005 - 2006	59 / *
2004 - 2005	48 / 104
2003 - 2004	47 / *
2002 - 2003	45 / 80
2001 - 2002	51 / 75
2000 - 2001	42 / 58
1999 - 2000	31 / 58

**The original report from these years was not accessible on internet.*

Source: http://www.weforum.org/reports/

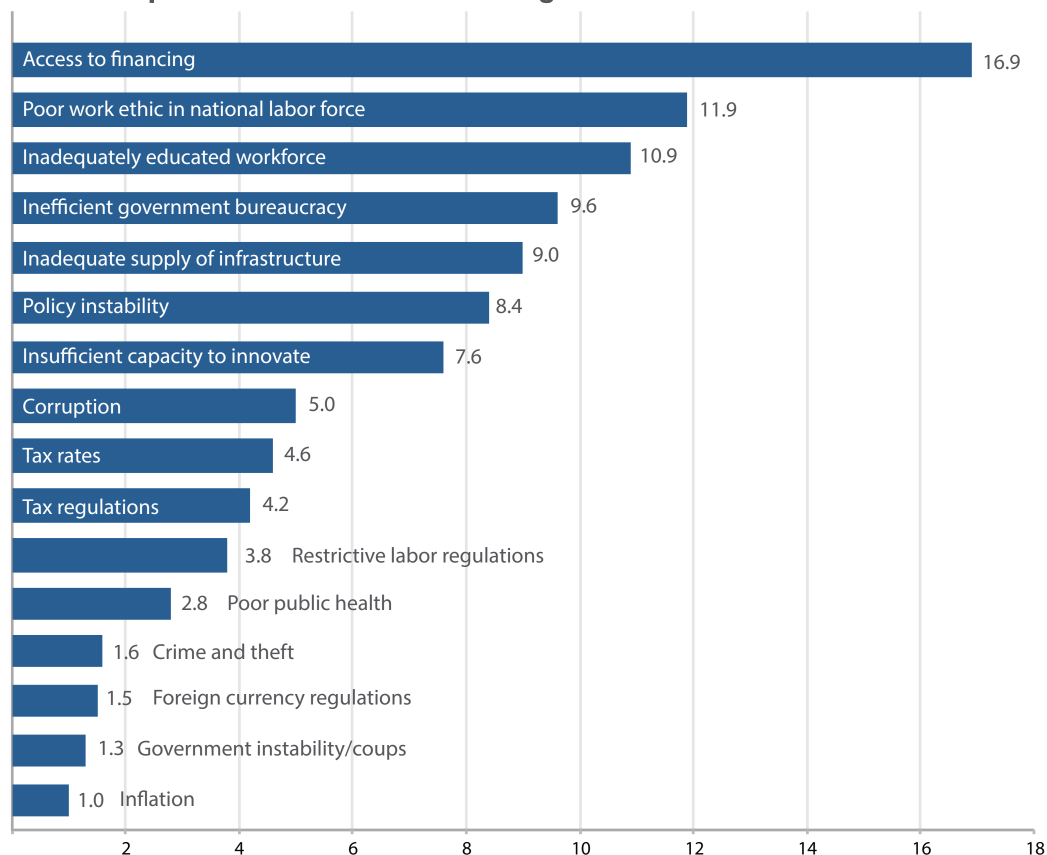
When competitiveness is broken down into the components documented by the Competitiveness Index, Mexico's institutions rated very poorly in 2014 —102 out of 144— and elements of "efficiency enhancers" place Mexico deep in the lower half of countries: labor market efficiency

[3] World Economic Forum. Global Competitiveness Report, 2014-15. http://www3.weforum.org/docs/WEF_GlobalCompetitivenessReport_2014-15.pdf. See p. 270-71.

ranks 121 and goods market efficiency ranks 86.[4]

The five most problematic factors for doing business in Mexico are corruption, tax regulations, inefficient government, crime and theft, and access to finance in that order.[5]

The most problematic factors for doing business in Mexico



Source: WEF. The Global Competitiveness Report 2014 – 2015, p. 270.
http://www3.weforum.org/docs/WEF_GlobalCompetitivenessReport_2014-15.pdf

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4 Ibid.

5 Ibid.

A Second Wave

Today, a second wave of reforms is underway in Mexico, a package of constitutional changes that, taken together, would effect a sweeping transformation of the economy.

The reforms have their genesis in the extraordinary secret negotiations held between the three leading political parties in the months before Peña Nieto took office to reach agreement on priorities for Mexico's development. This undertaking between the heads of the Institutional Revolutionary Party (known by its Spanish acronym, PRI), National Action Party (PAN), and Party of the Democratic Revolution (PRD) grew out of the dismal record of legislative gridlock in which rival parties routinely blocked each other's initiatives from 1997-2012, effectively imposing a fifteen-year stop on further reform.

The negotiations resulted in the *Pacto por México*, a political agreement to advance policies centered around fundamental agreements on civil and human rights including social safety nets and improvements to public education; economic growth, employment and competitiveness; security and justice; transparency, accountability and combating corruption; and democratic governance including political reforms to allow independent candidates, citizen initiatives and an election tribunal with national coverage.[6]

The *Pacto* was unveiled the day after Peña Nieto's inauguration by the President and the three party leaders, and took Mexico by surprise. The predominant political forces jointly endorsed the premise that Mexico's economy must grow at more than 5 percent per year, or more than double the average growth rate of the past 30 years. The economic axis of the *Pacto* includes agreements on 36 specific policies to create a reform of the energy sector so that it becomes a motor of development; deepen competition in telecommunications and broadcast media; produce a tax reform; expand the availability of credit for business loans; and legislate to favor innovation and modernization of a host of industries.

Over the next 21 months, the political consensus enabled the approval of the most ambitious set of reforms to the Constitution passed in modern Mexico. The package of Peña Nieto reforms opened the energy sector to private investment, strengthened the telecoms and broadcasting regulator, granted autonomy to the anti-trust agency, produced measures to reduce bank fees and expand credit to businesses, and created a fiscal reform that has increased federal tax revenues. Peña Nieto "passed reforms that alter the tenets of the Mexican economy, are historic, and create a new foundation for potential changes," says Luis Rubio, chairman of CIDAC development policy center. These reforms, which passed congress between 2012 and 2014, exceeded the expectations

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[6] "Pacto por México." www.pactopormexico.org.

of most seasoned Mexico-watchers. Taken as a whole, the reforms are intended to sustainably raise Mexico's sluggish economic growth and improve the country's lagging competitiveness.

Inflection Point

Mexico is at a critical juncture. The record shows that the first wave of reforms that began 30 years ago failed to deliver the desired boost to economic growth and competitiveness. The reforms now underway promise even bigger changes for the economy, particularly by opening up the long closed petroleum industry. Looking ahead, can the new wave of reforms move Mexico into a higher gear, stimulate increases in productivity and economic growth, lubricate the economy with more credit, establish and enforce genuine competition in strategic sectors, and train the work force in modern skills? Or, three decades hence will we look back and say the Peña Nieto reforms were inadequately implemented and Mexico remains a low-growth, low-productivity economy?

This is a timely moment for reviewing Mexico's success with deep economic reforms and asking what is required from here on in to make the new wave of reforms successful so that Mexico and Mexicans can enjoy the benefits of higher growth and productivity.

This study offers a qualitative analysis of the deep economic reforms undertaken in Mexico during the past 30 years, the progress made and informed opinions on what is needed today to boost economic growth, enhance competitiveness and, hopefully, increase employment. The study summarizes the views about the successes and failures of the first wave of reforms as seen by a select group of former cabinet members and other prominent policy makers, consultants to government, opinion shapers in policy centers, and thought leaders in academia. These policy makers and shapers were asked to offer the three to five top priorities for action on the road ahead so the new reforms may become effective agents of growth and development. Their policy recommendations make up the conclusion of this report.

For this study, I conducted extensive interviews with an elite group of leaders in government, business, banking, academia, and public opinion. Nearly all of those surveyed have been prominent economic agents active since the economic opening began in the mid-1980s with deregulation, Mexico's entry into GATT, and privatizations of state enterprises. Two younger academics (including the only woman among the interviewees), both active in independent policy research groups that track current reforms, were also interviewed. All those interviewed are Mexican nationals. The sum of experience of these people includes decades of cabinet-level government service and central bank governance, high-level consulting to government reform processes, leadership in banking, and teaching at the nation's top universities. The experts consulted in this study include five members of the Trilateral Commission and advisors to more than 60 corporate boards in Mexico and abroad. The persons interviewed and a brief description of their professional careers appears in the chart, below. Summary biographies of those interviewed are included following the conclusion of the report.

Persons Interviewed

Government Service	
Government Minister	9: Agustín Carstens, Francisco Gil Díaz, Angel Gurría (2), David Ibarra, Guillermo Ortiz (2), Jaime Serra (2)
Undersecretary	8: Luis de la Calle, Francisco Gil Díaz, Santiago Levy, Pedro Noyola (2), Roberto Newell, Andrés Rozental, Jaime Serra
Central bank Governor/deputy governor	2; 1: Agustín Carstens, Guillermo Ortiz; Francisco Gil Díaz
Trade negotiators	3: Luis de la Calle, Pedro Noyola, Jaime Serra Puche
Directors of Mexican development banks/National Banking Commission	2; 1: Angel Gurría, David Ibarra; Eduardo Fernández García
Top executives of international financial institutions: OECD, IMF, IADB	3: Angel Gurría; Agustín Carstens; Santiago Levy
Director, Mexican Social Security Institute	1: Santiago Levy
President, first anti-trust commission, CFC	1: Santiago Levy
Ambassadors	2: Carlos Elizondo, Andrés Rozental
Private Sector	
Director General, Telefónica	1: Francisco Gil Díaz
President, Board of Advisors to President, Banorte	1: Guillermo Ortiz
Consultant to government	1: Roberto Newell
Presidents of consulting firms; independent consultant	4; 1: Luis de la Calle, Pedro Noyola, Rogelio Ramírez de la O, Jaime Serra; Eduardo Fernández García
Investment officer, investment management firm	1: Tim Heyman
Civil Society	
Executives, independent policy research centers	6: Manuel Molano, Roberto Newell, Juan Pardinas, Viridiana Ríos,+ Luis Rubio, Luis Serra Barragán

Academia/Policy Shapers**	
Professors, researchers, policy advisors	12: Carlos Elizondo Mayer-Serra, Gerardo Esquivel, Federico Estévez, Arnulfo R. Gómez, Carlos Heredia, David Ibarra, Isaac Katz, Manuel Molano, Juan Carlos Moreno Brid, Luis Rubio, Luis Serra Barragán
Members Trilateral Commission	6: Luis de la Calle, Carlos Heredia, Santiago Levy, Andrés Rozental, Luis Rubio, Jaime Serra
*This chart lists the most senior positions occupied by the persons interviewed. Brief biographies of each individual are included in the Biographical Highlights annex. **Many of the public servants and private sector executives have also served as professors. Many of the academics have acted as consultants or advisors to government programs. +Ríos is the only woman in the group, a reflection of the prevalence of men in cabinet and executive posts during the time period studied.	

The sources were asked to summarize the intent and promise of the first wave of reforms in the 1980s and 1990s, and then to assess the accomplishments, failures, and why the reforms failed to deliver on expectations. Their replies offer insight into the attitudes and practices that permeate the Mexican economy and shape the outcomes of policy.

Interviewees were then asked to offer their three to five priority recommendations for policies they believe are needed to make the current reforms successful and to boost Mexico's economic performance. Their recommendations for the tasks that lie ahead are summarized in the conclusion of this report.

The author wishes to express her deep gratitude to each of the people who made themselves available for interviews. Without their generously sharing their time and considered thoughts and their candor and graciousness, this project would have been impossible. Their extensive experience, informed opinions, and clear-eyed ideas for the future are the essence of this study.

Special thanks go to Duncan Wood, Director of the Mexico Institute at The Woodrow Wilson International Center for Scholars, who provided guidance and support that made this study possible. I also thank Paxton Helms for his valuable contributions as editor.

I am very grateful for the kind support of friends Steve Knaebel, Javier Márquez, Penelope Poole, and Teresina Múñoz Nájar.

All errors are those of the author.

Part 1: First Wave Reforms: Mexico Opens to Markets

In 1985, Mexico began a prolonged process of structural change to attack and tame the causes of instability in the Mexican economy, lift protections, and end restrictions on trade. Sharp cutbacks in government programs and agreements with business and labor to hold down prices gradually lowered inflation and brought federal deficits within manageable limits. Then, after a series of devaluations followed by sharp economic downturns, new policies were introduced to allow a free-floating currency and an autonomous central bank. At the same time, step by step, measures were adopted that opened Mexico's protected economy, attracted vastly more foreign investment, triggered an enormous expansion of manufacturing and export industries, and integrated Mexico into the North American economy.

These changes forged a new and more resilient economy, one that is almost unrecognizable from the politically controlled, closed economy that was dominated by state firms until the mid-1980s.

Morenovel / Shutterstock.com

A popular joke in Mexico in the 1970s was to call Volkswagen Beetles belly buttons. Why? Because everybody had one. Today, the Mexican car market is vastly different: 42 brands including Honda, Mitsubishi and Mercedes-Benz and 300 models are offered. The country is also the world's eighth

largest auto-manufacturer: international car-makers have 21 plants in northern and central Mexico, and they produce three million cars every year.[7]

Grocery shopping, too, has been revolutionized. A few decades only three national supermarket chains dominated the field and the goods on offer were almost exclusively local products. Today, Mexican consumers can buy not only chile sauces and tortillas, but also American donuts, imported cheeses, and some 10,000 other products at any one of 2,226 Wal-Mart retail centers that are now as ubiquitous as, well, the Beetle used to be. Walmart has become Mexico's largest grocer and retailer, and the market capitalization of its Mexican subsidiary Walmex is greater than that of French grocer giant Carrefour and Britain's Tesco, according to Thomson Reuters.[8]

During the past 30 years of structural reforms, Mexico's economy has expanded from $184 billion to $1.3 trillion; foreign direct investment rose from an average level of $1 billion a year to over $12 billion; annual bilateral trade with the United States grew to more than $500 billion; and cross-border investments along the Rio Grande rose to more than $100 billion. From 1983 to 2013, GDP growth has been on average 2.1 percent per year and growth of income per capita slowed to an annual rate of 0.6 percent, lower than that of other emerging markets.[9] But, productivity from 1980 to date has shown a negative average annual growth rate.[10]

> "During the past 30 years of structural reforms, Mexico's economy has expanded from $184 billion to $1.3 trillion."

The trade opening is a two-way street: Mexico's growing exports are frequently outstripped by its imports. In recent years, the trade balance has been negative. In 2012 and 2013, imports exceeded exports by $1.625 billion and $134 million, and in 2014, exports totaled $397.54 billion but the balance of trade was $-2.32 billion, according to International Trade Centre figures.

Inequality of income has remained pronounced, and rising inequality is estimated to have knocked more than 10 percentage points off growth in Mexico between 1985 and 2005, according to the Organisation for Economic Cooperation and Development (OECD). The standard measure of income inequality, the Gini coefficient, does not improve after taxes nor after distribution of conditional cash transfers to the poor.[11]

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7 U.S. Commercial Service, U.S. Commerce Department, U.S. Embassy, "Selling into Mexico's Automotive Supply Chain." September 10, 2014. http://www.export.gov/mexico/static/AutomotiveMeetings_webinar1_Latest_eg_mx_079354.pdf. Consulted Dec. 13, 2014.

8 Fishman, Charles. The Wal-Mart Effect. p. 235, p. 6. I owe the point about market capitalization to Luis de la Calle, author interview, Dec. 1, 2014.

9 Author interviews with Rogelio Ramírez de la O, Nov. 10, 2014, and Angel Gurría, Jan. 5, 2015.

10 Videgaray, Luis. Press conference at the launch of draft legislation to promote sustained growth of productivity and competitiveness. Oct. 2, 2014.

11 Author interview with Santiago Levy, Nov. 11, 2014.

The Secretary General of the OECD, himself a former finance minister, reflects on the results of the structural reform period: "During the past three decades, the Mexican economy has experienced a prolonged growth slowdown leaving it behind other OECD countries," and confidence in public institutions has been weakened, says Angel Gurría.[12]

Overview of the Structural Reforms

The reforms that redefined the course of the Mexican economy were the outcome of consistent policy across the administrations of Presidents Miguel de la Madrid (1982-88), Carlos Salinas (1988-94), and Ernesto Zedillo (1994-2000). Continuity of policy was itself an innovation in Mexico, and this allowed the three administrations to put the many policies required to reshape the economy in place. The most important moves made to reform public finances and open the economy are summarized here.

The structural reforms were set in motion following the oil bust of the early 1980s and Mexico's default on government debt in August 1982. In 1983, President de la Madrid moved immediately to launch a shock treatment: deep fiscal cuts and a sharp devaluation to stimulate exports that, it was hoped, would reduce the government deficit. However, austerity and the devaluation failed to bring down inflation as projected and government borrowing requirements remained high, over 8 percent of GDP in 1983 and 1984.

Low confidence fueled a run on the peso and by mid-1985 Mexico was embroiled in another balance of payments crisis.[13] De la Madrid then imposed a tougher austerity program, a devaluation, and new policy instruments to confront the crisis. "The stabilization measures were accompanied by an acceleration in trade liberalization signaling the beginning of the structural reform process," writes Nora Lustig.[14] In July 1985, Mexico made the unilateral decision to reduce requirements for import licensing and to increase to 64 percent of imports those goods exempted from licensing.[15] In 1986,

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[12] Author interview with Angel Gurría. Dec. 5, 2014.

[13] This overview of the major reforms between 1982 and 1992 relies heavily on the authoritative, detailed recounting and analysis of economic changes in this period by Nora Lustig in her book, Mexico: The Remaking of an Economy. (Washington, D.C.: The Brookings Institution, 1992), pp. 29-37.

[14] Ibid., p. 39.

[15] Ibid., pp. 39, 118-19.

Mexico joined the General Agreement on Trade and Tariffs (GATT), marking an unequivocal shift to an export-led growth strategy.

The following year, inflation rose to a new high of 159 percent. In December 1987, government, labor, farmers, and business signed the Economic Solidarity Pact that included agreements to maintain public sector prices, continue controlling the exchange rate, charge a maximum tariff of 20 percent on trade inputs, and hold down wages. In 1988, inflation had been brought down to 51 percent for the year. A privatization drive, which had begun modestly in 1983, continued throughout the term and, before leaving office in 1988, de la Madrid had sold off or liquidated more than 700 para-state companies but had steered clear of putting the largest and most strategic public firms on the auction block.

"Salinas came to personify the concept of reform and he put in place a team that has remained influential to this day."

Throughout the "lost decade" of the 1980s, finance ministry officials cut spending and renegotiated the debt with international commercial banks and multilateral institutions to extend the repayment periods and make annual payments more manageable. To reduce peso volatility, Mexico pegged the currency to the U.S. dollar beginning in 1985.

In December 1988, Carlos Salinas took office following highly questionable elections in which his opponent, Cuauhtémoc Cárdenas, posed the most serious challenge ever to a candidate from the ruling PRI. The next month, Salinas moved to legitimize his hold on power by jailing the chief of the oil workers' union and launching the Pact for Economic Stability and Growth, a set of measures that strengthened the 1987 de la Madrid Pact.

Economic liberalization quickened and deepened starting in 1989 when deregulation of trucking, petrochemicals, fishing, and mining and the privatization process opened up wide sectors of the economy to private investment. The sales of public firms raised funds for the strapped public budget.[16] In those same years, the two national airlines, the Cananea copper mining company and the controlling share of the national telephone company, Telmex, were sold to private Mexican and foreign owners for a combined total of approximately $2.6 billion.

President Salinas "had a clear concept of what he wanted, all Mexicans knew where he was going," says Luis Rubio of CIDAC policy research center.[17] Salinas came to personify the concept of reform and he put in place a team that has remained influential to this day.

[16] Ibid., p. 109-10.

[17] Author interview, Luis Rubio, Aug. 27, 2014.

Between June 1991 and July 1992, the entire banking system was privatized in a process that placed a premium on selling at high prices and raised business expectations. The 18 state-owned commercial banks brought in prices between 2.62 and 5.3 times book value, reaping a total of more than $12 billion.[18] Privatizations continued throughout the Salinas term, and by mid-1993 nearly 1,000 firms had been divested and the government held only 213 companies, though they included state-owned oil monopoly, Pemex.[19] In 1993, a foreign investment law was passed that provided unprecedented guarantees on foreign capital and opened formerly closed sectors to international investors.

The most dramatic of the structural reforms, the trade opening, evolved in four stages, spanning the presidencies of de la Madrid and Salinas. In 1986, Mexico joined the GATT, fully 40 years after the launch of the multilateral agreement to facilitate international commerce. In 1987, Mexico unilaterally set a ceiling of 30 percent on tariffs in any sector as part of the economic stabilization pact. In early 1990, following the fall of the Berlin Wall, Salinas decided to favor regional trade integration over a multi-lateral approach for a trade opening with the European Union and announced Mexico would pursue a North American Free Trade Agreement (NAFTA). Following negotiations with the United States and Canada on free trade and on environmental and labor rules, NAFTA took effect on January 1, 1994. "That was the big jump, that was a huge commitment," recalls Jaime Serra, former trade minister and leading negotiator on the Mexican team.[20] From 1995 on, Mexico has negotiated a series of bilateral and multilateral free trade agreements that cover 44 countries, including the members of the European Union.

"NAFTA took effect on January 1, 1994. "That was the big jump, that was a huge commitment."

The last major Salinas reform was put into place when the central bank was granted autonomy in April 1994. This historic measure was intended to enhance stability and bring an end to devaluations. "It got off to a rocky start," says Guillermo Ortiz, then the central bank governor, rocking slightly in a leather sofa in his office at Banorte's headquarters as he recalls those tense days.[21] They were turbulent times. In the first three months of 1994, a guerrilla uprising broke out in southern Chiapas state and the government party's presidential candidate, Luis Donaldo Colosio, was assassinated, shaking confidence to the core and fueling capital flight. A fixed exchange rate regime that pegged the peso to the dollar and let it float within a narrow band, a growing current account deficit that reached 7 percent of GDP, and the issuance of short-term

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[18] Ortiz Martínez, Guillermo. La reforma financiera y la desincorporación bancaria. (Mexico, D.F.: Fondo de Cultura Económica, 1994), pp. 267-336.

[19] Rogozinski, Jacques. La privatización de empresas estatales. (México, D.F.: Fondo de Cultura Económica, 1993), p. 47.

[20] Author interview, Jaime Serra, Nov. 13, 2014.

[21] Author interview, Guillermo Ortiz, Nov. 21, 2014.

treasury bills with guaranteed repayment in Dollars were the explosive mix of policies left as a legacy to Salinas' successor.

President Ernesto Zedillo took office in December 1994 with the peso under enormous pressure. The administration's initial move of resetting the exchange rate band did not hold. Barely three weeks in office, the government announced a free float and the peso immediately lost 40 percent of its value and finance minister Jaime Serra lost his job. "We had to float the exchange rate because we were left with no reserves. No emerging country had a floating rate. I was finance minister, frankly I didn't know if the floating regime would work," says Ortiz.[22]

Banks were exposed to large loan portfolios in dollars, hundreds of their business loans lapsed and, and as annual interest rates shot up to more than 80 percent, thousands of homeowners defaulted on mortgages. The financial crisis spread into the entire economy. Zedillo obtained a $50 billion loan package arranged by the U.S. government. He created a rescue plan that included recapitalizations and interventions of the banks and ultimately consumed 18 percent of GDP.[23]

In 1995, Zedillo carried out judicial and political reforms that proved significant in paving the way for Mexico's advance toward stronger checks and balances and political pluralism. The judicial reform strengthened the independence of the Supreme Court and in 1996 an autonomous federal election commission was created to supervise elections. In the 1997 mid-term races, the PRI lost control of the lower house of congress, the Chamber of Deputies.

The major economic reform of the Zedillo term was the 1997 pension reform creating obligatory individual pension accounts managed by professionals that would give workers an alternative

[22] Ibid.

[23] Author interview, Agustín Carstens, Dec. 19, 2014. Newell notes, p. 52 , that La Jornada newspaper cited in 2005 a World Bank presentation that estimated the cost at 25% of GDP, but adds the World Bank document is not available on the bank's site.

to public social security pensions.[24] By 2015, capital in the funds totaled more than $160 billion and has contributed to expanding the domestic capital market where the savings are invested in longer-term instruments. Zedillo's attempt in 1999 to pass a constitutional reform to allow private firms to generate and distribute electricity failed to win the required two-thirds majority in the divided congress. At the end of the Zedillo term, in 2000, the sale of the rescued banks began. That process was concluded in the early 2000s, during the first years of the presidency of Zedillo's successor, Vicente Fox. When the sales were completed, Mexico had a reconfigured banking system which is today 70 percent foreign owned and led by large, international financial groups.

"We created a competitive region and it could be more so."

[24] Newell, op. cit, pp. 54-57.

Part 2: The First Wave Reforms: Accomplishments

There is universal agreement among the experts interviewed that the two most significant and far-reaching achievements of the reform period are stabilization of the economy and opening Mexico to trade. The reform to create an independent tribunal to supervise elections is also cited by some analysts as a significant achievement that fostered plurality in the body politic, a necessary complement to the economic liberalization. The most significant aspects of these achievements are described below.

Economic Stability

Today, Mexicans for the most part assume that inflation, public debt, and the peso will move within reasonable parameters rather than fluctuate wildly, sparing the economy periodic crashes; and, they take for granted that a very large number of consumer goods will be available to them thanks to the open economy. Gone are the days when a devaluation could knock 50 percent off the value of the peso, inflation could zoom to more than 100 percent per year, and Mexico could spend its international reserves down to zero. Memories of those days certainly remain but they are growing dimmer.

The economic fundamentals became anchored and stable through a series of policies including cutbacks in government spending, paying down debt, and the shift to a floating regime for the peso managed by an autonomous central bank. As a result, during the past 15 years, the federal deficit has normally not surpassed 1.5 percent of GDP, public debt consistently totals about 37 percent of GDP, and annual inflation has rarely topped 4.5 percent. Even in the wake of the 2008 international financial crisis, the peso did not suffer a great loss of value. Since 1994, public finances have been manageable and no new economic shocks have occurred though Mexico has suffered what Carlos Elizondo calls "mediocre" growth.[25]

The sequencing of the reforms focused first on stabilizing the economic variables, and this was correct, says Santiago Levy, a former deputy finance minister. "Nothing good can happen in an unstable economy with high inflation and deficits," he says.

After developing a track record in sound economic management, Mexico was able to return to

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[25] Author interview, Dec. 1, 2014. See Elizondo Mayer-Serra, Carlos. Por Eso Estamos como Estamos: La economía política de un crecimiento mediocre. (Mexico, D.F.: Debolsillo, 2013).

international financial markets. "We lose track of the fact that for 10 or 15 years Mexico was two or three times a credit pariah. That set us back," says Angel Gurría, the leading debt negotiator throughout the reform period.[26] "I was the one who borrowed—I didn't decide how much—it wasn't sustainable," he recalls. The economic and investment horizons became longer term. "The average maturity of (Mexican debt) paper is now eight years, against 24 hours in 1994," says Francisco Gil Díaz, vice-governor of the central bank during the turbulent years of 1994-97.[27] Mexico's peso has since moved from being shunned for its riskiness to become the eighth most-traded currency in the world today. Mexico came to occupy a new position in international economic institutions with its admission as the first Latin American country to join the rich countries' club, the OECD, in May 1994.

Openness to Trade

During this phase, Mexico opened the economy to trade, investment, and capital flows and, in part as a result of NAFTA, became a manufacturing powerhouse. "We created a competitive region and it could be more so," according to Jaime Serra, Mexico's lead NAFTA negotiator.

> "The trade opening "put Mexico in line with western regimes."

NAFTA was a formal international commitment to respect and follow a set of rules governing trade and investment. In separate interviews, two leading NAFTA negotiators, Pedro Noyola, and Jaime Serra, and the leading negotiator of subsequent trade agreements, Luis de la Calle, all say that it was necessary that Mexico sign an agreement with foreign countries to establish credibility for the trade opening and its policies. Perhaps even more important, an international agreement like NAFTA was necessary because "we couldn't break the deal from inside Mexico," according to Noyola. "The fact we are committed to actors outside made it strong. We can't fool around with this [treaty]."[28]

The agreement also has very strict discipline compared with other international trade arrangements.[29] The commitments are the same for Mexico, the United States, and Canada. De Calle called that equal treatment "revolutionary" for its time since developed and developing countries were simply not treated equally.[30]

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[26] Author interview, Dec. 5, 2014.

[27] Author interview, Dec. 10, 2014.

[28] Author interview, Oct. 7, 2014.

[29] Note that NAFTA has the status of a treaty in Mexico, and is an agreement in the United States.

[30] Author interview, Dec. 1, 2014.

The trade opening "put Mexico in line with western regimes," says Rogelio Ramírez de la O.[31] This bolstered Mexico's credibility abroad and NAFTA's opening of debt and capital markets helped lower the cost of capital in Mexico.

Hundreds of companies from the United States and other countries set up plants or expanded their facilities in Mexico to take advantage of the country's position as a platform for exporting to the world's largest combined market. Diversification of Mexico's production reduced the country's historic dependence on oil which now makes up only 15 percent of exports. Juan Carlos Moreno Brid of UNAM says that Mexico has become very good at exporting manufactured goods. "From 1995 to, say, 2010, we were second only to China with an increasing share in the world market."[32]

Conviction and commitment to the new policy directions characterized the reform period. "The reforms to open the economy and virtually eliminate the state's intervention in resource allocation were drastically enforced," according to Moreno Brid. Central bank governor Agustín Carstens elaborates: "I don't want to be self-congratulatory, but I honestly think that granting autonomy to the central bank and to have governments that have been respectful of this autonomy all this time has been very, very powerful." Continuity of policy has brought predictability to the Mexican economy and stands out as a notable achievement of the reform period. Bringing public debt under control and preserving an autonomous central bank also averted the devastating economic crises that were recurrent through the 1980s and into the mid-1990s, according to Carstens.

Clean Elections

The moves by Zedillo that set the stage for clean elections and pluralism in politics are considered another significant achievement of the reform period and, ultimately, led to election of the first opposition president in 71 years in 2000. "Mexico became a democracy, an imperfect one, but one that is an exceedingly important corollary to an open economy," says Roberto Newell.[33] The Mexican government's ability to keep its hands off the economy was an essential driver of Mexico's competitiveness.

The record of the past 30 years of reforms is positive, but in the face of slackening growth, major and complex challenges lie ahead. "There's no question that all these structural reforms have contributed to increasing competitiveness and, to some extent, to maintaining economic growth—not increasing it because we haven't had any increase in economic growth—but we've maintained a sort of plateau of economic growth," says Andrés Rozental, a career diplomat and

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[31] Author interview, Nov. 10, 2014.

[32] Author interview, Nov. 12, 2014.

[33] Author interview, Nov. 19, 2014.

consultant providing political and economic advice to Mexican and international companies. "We obviously aren't doing enough, we need to grow more, we need to be more competitive, we need to find ways to maximize our competitive advantages."[34]

The following sections of this report offer expert opinions on why the reforms have not produced a more robust and competitive economy, informed perspectives on the next steps laid out by the Peña Nieto reform program, and policy recommendations for enhancing Mexican competitiveness.

"There's no question that all these structural reforms have contributed to increasing competitiveness and, to some extent, to maintaining economic growth—not increasing it because we haven't had any increase in economic growth—but we've maintained a sort of plateau of economic growth."

[34] Author interview, Oct. 29, 2014.

Part 3 - Why the Gap in Performance?

The structural reforms undertaken over the last 30 years have not delivered the growth and competitiveness that citizens and policy makers were hoping for. The experts interviewed for this project agree in broad terms that major factors that explain the gap in performance are the large informal labor sector, lack of government credibility, partial implementation of reforms that stopped short of carrying reforms to their full consequences, low levels of capital accumulation, and income inequality. The reforms were new but played out in the context of a Mexico with entrenched economic structures and practices. The legacy issues that contributed to poor performance of the reforms include lack of competition in key economic sectors, protectionism which fostered a certain complacency among businessmen, and an attitude of pessimism.

Informality

Tens of millions of Mexicans work selling candies, tacos, soft drinks and pirated DVDs in the street; producing handcrafts, clothes, and shoes in modest family workshops; offering services as gardeners, cooks, and domestic helpers; or tilling the land as small farmers. They make up the legions of working poor who are classified as "informal" workers. This informal sector accounts for approximately 57 percent of all employment according to the recent and well-received McKinsey Global Institute report, *A Tale of Two Mexicos*.[35]

"It is precisely the deep division between the two economies that has kept Mexico's growth at disappointingly low levels despite three decades of economic reforms."

Released in March 2014, the McKinsey report quickly gained currency for defining Mexico as a dual economy made up of modern, large, productive, and competitive firms and a huge number of traditional small, unproductive firms, many of which operate as informal enterprises. "It is precisely the deep division between the two economies that has kept Mexico's growth at disappointingly low levels despite three decades of economic reforms," says the report.[36] McKinsey analysts and other observers agree that the high number of workers and the low output of the informal sector are the principal cause of Mexico's low aggregate productivity. And the problem is getting worse. In small traditional firms, productivity is falling by 6.5 percent a year; and, the traditional sector is generating jobs at a faster pace than more productive mid-sized and

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[35] McKinsey Global Institute. "A Tale of Two Mexicos: Growth and prosperity in a two-speed economy." By Eduardo Bolio, Jaana Remes, Tomás Lajous, James Manyika, Morten Rossé and Eugenia Ramirez. March, 2014.

[36] Ibid., p. 2.

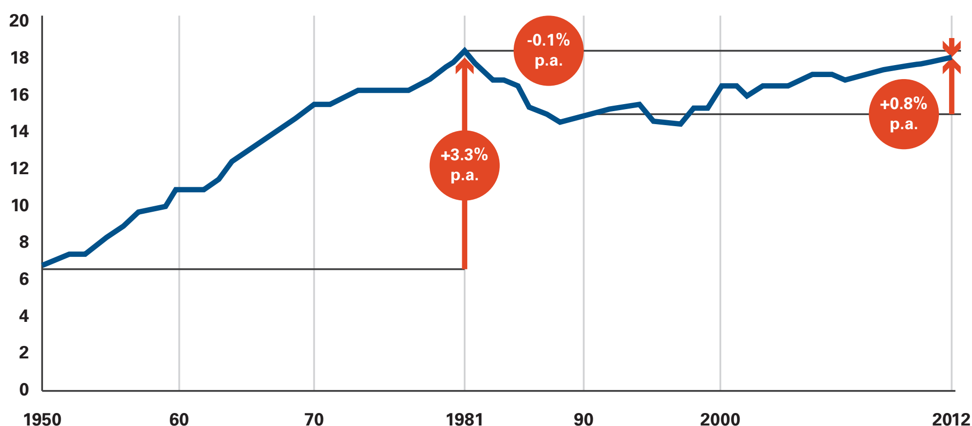
large companies, a trend which is shifting labor from high productivity work to low-productivity work."[37]

The highest consensus figure for productivity growth ranges between less than 1 percent per year growth and negative productivity and many observers believe it is less than zero. The average rate of overall productivity growth since 1980 is 0.8 percent per year, according to the McKinsey study; 0.6 percent in OECD reports; and negative according to Finance Minister Luis Videgaray.

The prevalence of small, informal firms has been studied in-depth in Mexico in the past and is explained by some as a response to rational incentives. The phenomenon is pervasive: not only is close to 60 percent of the labor force made up of informal workers, but between 60 percent and 70 percent of all firms are informal (but also legal—i.e., their workers are registered in the social security system), and these proportions have not changed in the past 25 years.[38] "With the benefit of hindsight, issues associated with informality and productivity were substantially underestimated… the reforms have not tackled that, and it is the main reason productivity stagnated and growth is low," according to Santiago Levy.[39] "The deep issue is there is a large informal sector that continuously interacts with the formal sector and *has no gains in productivity over time*," (emphasis added).

Productivity per worker has fallen from its peak in 1981

GDP per hour worked, in 2012 purchasing power parity dollars



Source: Conference Board Total Economy Database 2013; McKinsey Global Institute analysis, p. 21.

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[37] Ibid., p. 4.

[38] Levy, Santiago. Good Intentions, Bad Outcomes: Social Policy, Informality, and Economic Growth in Mexico. (Washington, D.C.: The Brookings Institution, 2008.), p. 34.

[39] Author interview, Nov. 11, 2014; see also Levy, Santiago. Good Intentions, Bad Outcomes, op. cit.; Busso, Matías, María Victoria Fazio and Santiago Levy, "(In)Formal and (Un)Productive: The Productivity Costs of Excessive Informality in Mexico." (Washington, D.C.: Inter-American Development Bank, 2012), p. 11-13.

Levy finds that the principal cause of widespread informality is the intersection of labor, tax and social security laws "that impact how workers perceive jobs." Not all workers are interested in a formal job, and incentives for becoming formalized are inadequate. In fact, informality increased between 1998 and 2008. He reports that there are "ever more informal firms, so someone is putting capital into them, so the incentives are for people to invest in the informal sector." Levy believes that a reform of public policies "that cause excessive informality" could raise total factor productivity and drive growth. Current regulations for non-salaried labor subsidize informality; and, social programs for informal workers have grown while larger formal firms face high costs when they hire workers.[40] According to Levy, labor costs make up 30 to 40 percent of all firm costs, an amount greater than the cost of electricity and telecommunications combined.[41]

Analysts agree that a range of incentives exist in the economy for informality and point to different explanations for the large number of informal workers. "The economy doesn't grow enough… and the absence of good job opportunities causes people to go into informality," according to Gerardo Esquivel.[42] Curiously, this occurs even though his research shows that if you control for the characteristics of the individuals (education, age, experience, marital status, etc.) formal employment pays better. Esquivel also doubts that an increase in the number of formal workers would translate into greater overall productivity. Formal sector workers with low educational levels and poor access to credit will not necessarily be more productive than informal workers, he says. But, the question is kind of academic. Elevating productivity in the informal sector faces barriers that are unique to that sector, including poor access to business loans that would allow for upgrading equipment or processes. "The fact that (informal firms) have access to very expensive financing is a vicious circle," says Guillermo Ortiz. For example, the average annual rate of interest on loans from microfinance institutions in Mexico is 80 percent or more.

"The economy doesn't grow enough…and the absence of good job opportunities causes people to go into informality."

The large, efficient firms singled out in the McKinsey study as "high velocity" benefit from a number of advantages. Big modern companies are able to dilute the high costs of doing business by virtue of their size, says Carlos Elizondo.[43] A large firm can overcome the handicaps imposed by expensive, low-quality public services such as electricity by building its own generating plants and can afford to maintain a legal department that handles complicated labor legislation and helps avert crippling fines. Despite these and similar advantages, "the high-velocity companies are not big enough to

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[40] Ibid., p. 31, 32.

[41] Author interview, Nov. 11, 2014.

[42] Author interview. Oct. 24, 2014.

[43] Author interview, Dec. 1, 2014; Elizondo Mayer-Serra, Carlos. Por Eso Estamos como Estamos: La economía política de un crecimiento mediocre (Mexico City: Debolsillo, 2013).

pull the rest of the country" along in terms of aggregate productivity, says Elizondo. Indeed, the McKinsey study finds that falling productivity in traditional firms with fewer than ten employees and which make up 42 percent of employment offset productivity gains by modern firms.[44]

Productivity and growth in Mexico can be looked at from a variety of angles, according to Luis de la Calle, head of a consultancy focused on regulations and trade.[45] Geographic location and the source of capital—public or private—make a difference, he argues. The fast-growing regions of Mexico include northern border states and the Bajío region in central Mexico—Aguascalientes and Guanajuato states where manufacturing clusters have proliferated—and in those areas GDP per capita has risen 40 percent since 2004.

By contrast, in the gulf coast state of Campeche, the average rate of growth in the last 20 years has been negative. About that negative growth rate? "It's impossible! Well…Pemex did it," quips de la Calle, referring to the steady decline of output at Cantarell, the oil monopoly's largest offshore field in the Bay of Campeche.

De la Calle points to misallocated capital as an enormous drag on growth and offers this analysis. Pemex has invested the equivalent of two percent of GDP annually in recent years but has not increased oil production. If investment in the informal sector is assumed to be even less productive and totals an additional two percent of GDP, the sum of poorly allocated capital equals 20 percent of total annual investment in Mexico.

De la Calle questions the widely accepted official figure of negative productivity growth during the last 20 years. He says that, "productivity is wrongly diagnosed because it is measured poorly; capital and GDP are poorly measured," concluding that this throws off productivity figures. Capital measurements are erroneous for three reasons: obsolescence, poor allocation, and idling during business cycles. "When you open the economy, obviously a lot of capital becomes obsolete, and should not be counted in the same proportion." Capital is heterogeneous. "In the last 30 years in Mexico, many low-yield investments have been made, and that is not productive capital," he says, citing inefficient investments in the public and informal sectors. Economic downturns, as in 1995 or 2009, cause businesses to idle some of their capital and reduce production. At these times, "capital is less used but that is false, productivity has fallen. Productivity growth has not been at the level the country needs, but it is not negative as is being portrayed." His is a minority viewpoint.

Moreno Brid of UNAM argues that productivity has been undermined by a weak performance of investment that has led to a reduction in the relationship between capital and labor, as its stock of

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[44] McKinsey Global Institute Op. cit., p. 7.

[45] Author interview. Dec. 1, 2014.

machinery, equipment, and infrastructure has not grown as fast as the labor force. The Mexican economy's failure to expand and modernize its infrastructure and to technologically upgrade its fixed capital has impaired its labor productivity and its international competitiveness.

There is a broad consensus that the relationship of investment to GDP must top 25 percent per year for economic activity to expand persistently at annual rates of 5 percent to 6 percent, says Moreno Brid. Mexico performs poorly by this standard. In the past 35 years, the only times that investment exceeded 25 percent of GDP were in the oil boom years of 1980 and 1981. In all years since then, capital formation has lagged, dipping as low as 17 percent and rarely reaching 23 percent. A related and most worrisome aspect in this matter is the poor performance of public investment, reflected in such a systematic decline that, as a share of GDP, in 2014 it registered one of the lowest levels in decades.

Gross Capital Formation (% of GDP), 1985-2013

Year	Gross Capital Formation
1985	21.17
1986	18.53
1987	19.26
1988	22.56
1989	22.94
1990	23.14
1991	23.32
1992	23.29
1993	18.87
1994	19.57
1995	16.92
1996	18.96
1997	19.57
1998	21.65
1999	21.92
2000	22.5
2001	20.92
2002	19.97
2003	21.88
2004	22.65

2005	22.27
2006	23.44
2007	23.36
2008	24.4
2009	22.87
2010	22.02
2011	22.25
2012	23.19
2013	21.61

Source: World Bank with OECD data.

A Truncated Trade Opening

The first wave of reforms opened Mexico's economy to trade and investment with measures to deregulate and privatize industries, protect foreign investment, and commit to free trade agreements. "The trade liberalization made us competitive, this was in our minds," says Jaime Serra. But, trade liberalization had not taken root in the government. Even after joining GATT, "there was no real commitment to trade liberalization. Policy makers were unsure about the [country's] potential to become truly export-oriented," says Pedro Noyola, who served as deputy minister to NAFTA chief negotiator Serra.

Although the trade opening created by NAFTA was very broad, the agreement did have important limitations. "NAFTA was incomplete from the beginning. It should have been seen as a stepping stone, not the end of the road," says Noyola.

"NAFTA was incomplete from the beginning. It should have been seen as a stepping stone, not the end of the road"

First, it was not a trade agreement that would build ties to link Mexico with an orbit outside the United States as had been hoped. In 1989, then-president Salinas and senior trade officials wanted to create a multilateral trade opening with Europe. While at the World Economic Forum meeting in Davos in January 1990, Salinas saw that Europe was enamored and absorbed with the possibility of integrating Germany after the Berlin Wall came down, and he soon decided to follow the hemispheric vision of President George Bush, according to Noyola.

Second, vital and cross-cutting sectors were taken off the table. Each country in the negotiation came with its own "no-no's," says Noyola. For Mexico, the sacrosanct national oil and electricity

monopolies were kept out of the negotiation and the virtual telephone monopoly, Telmex, was left untouched to give the firm time to recoup the investment made by the consortium led by Carlos Slim when the company was privatized, says Newell, a McKinsey consultant at the time active in designing the privatization.[46]

Once NAFTA was a done deal, banking, telecommunications, and the energy sector remained largely protected from foreign competition. "These services are essential inputs for all sectors, so it doesn't make you very competitive," says Serra. Inputs including energy, telecommunications, and non-tradable services remained protected. As a result, Mexican firms have not benefited from competitive inputs. The telecommunications sector is a notorious case. "The welfare loss attributed to the dysfunctional Mexican telecommunication sector is estimated at USD 129.2 billion (2005-2009) or 1.8 percent GDP per annum," reports the OECD.[47]

During the past 20 years, Mexican firms and consumers have paid a premium price for poor telephone, Internet, and cellular service because the sector has been dominated by a near-monopoly, the Telmex and Telcel subsidiaries of América Móvil. Fixed-line telephony is among the most expensive in the OECD, broadband penetration is low and service is expensive and slow, and international roaming prices are "extremely high."[48]

"Once NAFTA was a done deal, banking, telecommunications, and the energy sector remained largely protected from foreign competition."

Failure to open the energy sector with NAFTA has exacted a heavy toll on the economy. Production of the national oil monopoly Pemex has declined over the last decade. Keeping private investment out of oil and gas effectively restricted development of energy resources by the world's tenth largest oil producing nation, deprived Mexico of modern technology that would allow deep-water exploration, and kept energy costs high. De la Calle believes that the failure to develop Mexico's gas resources continues to limit Mexico's possibilities of becoming a competitive supplier of energy-intensive products such as steel and silicon.

Reform in the banking sector would have had cross-cutting impacts in the economy, says Gerardo Esquivel. Banking penetration—only 27 percent of the population uses banks—is the lowest among the 30 OECD countries and significantly lower than Latin American peers such as Brazil and Chile. Total lending to the private sector is 22 percent of GDP, but only about a third of that

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[46] Author interview, Nov. 19, 2014.

[47] OECD. 2012: OECD Review of Telecommunication Policy and Regulation in Mexico. (OECD Publishing.), p. 9. http://dx.doi.org/10.1787/9789264060111-en

[48] Ibid., p. 30, 33.

goes for business loans, the equivalent of approximately 6 to 7 percent of GDP, says Esquivel. Lending to the federal and state governments allows banks to meet international risk parameters and collecting high banking fees on credit cards is more lucrative than lending for production. The financial sector is dominated by six banks that control about 80 percent of assets and loans. Fees and commissions for financial services are very high by international standards.

Preserving protection for these ITC and other domestic inputs such as labor, land, water and all other non-tradables prevented the reforms from becoming self-sustaining, according to Roberto Newell. "The intention of de la Madrid and Salinas was to extend the life of the political economy, not transform it."[49] The vision was to preserve the strong presidency with enormous powers over the economy—"the final arbiter of most key decisions"—and open the economy while maintaining executive control over key economic sectors, labor and the body politic, says Newell.

The timing of NAFTA and the legacy of protectionism meant that competition had already intensified when Mexico entered world markets. "We stayed closed too long and by the time we started to open, other countries—Asia, etc.—had already taken a lead," says Gurría, the OECD Secretary General.

Mexico's development as a manufacturing platform and exporter is still impressive. In 2014, Mexico's manufacturing sector grew by 4 percent, and auto and aerospace production expanded by 6 percent.[50] Last year, the value of exports from Mexico was $397.7 billion, the equivalent of over 18 percent of total GDP. The leading export in 2014 was vehicles valued at $85.95 billion, or 21.6 percent of exports, followed by electronic equipment worth $80 billion. Between 2010 and 2014, vehicle exports rose by 66.1 percent.[51]

But, there is another story to the millions of automobiles, delivery trucks, computers, and video displays shipped out of Mexico to its top customers—the United States, Canada, Spain and China.[52] Mexico also imports enormous amounts of metal products, machinery and equipment, engines, vehicle parts, wire, integrated circuits, insulated wire, and other inputs as well as gasoline to fuel its export machine.[53] Between 1980 and 2015, imports averaged $120 billion annually.[54] In fact, in 2012 Mexico was the world's eleventh largest exporting nation and the ninth largest importing

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[49] Newell, op. cit., p. 3.

[50] Presentation at a Mexico Institute event at the Wilson Center, Oct. 14, 2014. http://www.wilsoncenter.org/event/the-united-states-and-mexico-partners-competitive-global-economy

[51] Workman, Daniel. "Mexico's Top Exports." http://www.worldstopexports.com/mexicos-top-exports/2636.

[52] Observatory of Economic Complexity. Profile: Mexico. http://atlas.media.mit.edu/profile/country/mex/; http://www.tradingeconomics.com/mexico/balance-of-trade. Consulted Dec. 22, 2014.

[53] Observatory of Economic Complexity, op. cit. consulted April 22, 2015.

[54] http://www.tradingeconomics.com/mexico/imports

nation, according to the WTO.[55] In 2014, México's export goods were valued at $397.65 billion and imports totaled $399.97 billion, making the balance of trade -$2.32 billion, according to ITC statistics.

Mexico's Balance of Trade, 1993-2012 (US$ millions)

Year	Total Exports	Total Imports	Trade Balance
1993	51,832	67,548	-15,716
1994	60,833	79,374	-18,541
1995	79,823	72,475	7,348
1996	96,000	89,469	6,531
1997	110,380	109,798	582
1998	117,500	125,246	-7,746
1999	136,703	142,063	-5,360
2000	166,424	174,473	-8,049
2001	158,542	168,275	-9,733
2002	160,682	168,678	-7,996
2003	165,355	170,958	-5,603
2004	189,200	197,303	-8,103
2005	213,995	221,414	-7,419
2006	250,461	256,205	-5,744
2007	271,875	281,949	-10,074
2008	291,348	308,603	-17,255
2009	229,704	234,385	-4,681
2010	298,473	301,482	-3,009
2011	349,375	350,842	-1,467
2012	370,915	370,746	169

Source: Arnulfo R. Gómez with data from Banco de México.

Many of the imports are parts that are assembled in Mexico and then exported. The amount of value added contained in Mexican exports, then, is relatively low. As recently as 2012, the value of imported materials and parts for the assembly industry totaled $225.78 billion, and the value added by Mexican workers to those components was $52.36 billion. The trade balance reflects this

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[55] World Trade Organization. List of Tables. 2013. https://www.wto.org/english/res_e/statis_e/its2013_e/its13_world_trade_dev_e.pdf, p. 23.

reality. Between 2001 and 2013, the value of imports exceeded exports every year.

Maquila Imports, Value Added and Re-exported Goods (US$ millions)

Year	Imports for re-export	Value Added	Total
1993	21,355	13,746	35,101
1994	32,160	9,389	41,549
1995	41,409	13,977	55,386
1996	50,713	18,501	69,214
1997	60,377	24,741	85,118
1998	69,016	28,585	97,601
1999	79,467	36,146	115,613
2000	97,680	39,576	137,256
2001	87,755	43,674	131,429
2002	87,414	42,269	129,683
2003	85,943	41,457	127,400
2004	98,096	42,396	140,492
2005	105,926	44,951	150,877
2006	121,404	52,767	174,171
2007	154,333	28,884	183,217
2008	173,304	31,846	205,150
2009	140,294	28,889	169,183
2010	187,890	35,120	223,010
2011	210,368	44,676	255,044
2012	225,780	52,369	278,149

Source: Arnulfo R. Gómez with data from the Ministry of Economy.

The low domestic content and low value added in Mexican exports is explained by the history of the in-bond, or maquila, program, says Jaime Serra. Created in 1965, the maquila was intended to encourage foreign corporations to set up shop in Mexico. Permits were given for temporary importation of parts that could be assembled by Mexican workers and then re-exported. The maquila program also prohibited the sale of the assembled goods inside Mexico. Many Mexican manufactured goods today are produced with this formula even though, technically, the maquila program was ended in the seventh year of NAFTA.

The maquila industry naturally clustered along Mexico's northern border from the outset to facilitate the cross-border flows of inputs and final products. Serra points out that this meant that

"the only opening since the '60s was a culture of exporting completely concentrated in the north." Inputs for maquilas were exempt from tariffs if re-exported—a distortion that reduced incentives for local production. "We had decades of protectionism and maquilas that generated the dynamics that are associated with very low Mexican content (which) was because we wanted to open up only partially."

In contrast, the success of the automotive industry is due in good measure to the fact that Mexico's NAFTA negotiators demanded an initial minimum of domestic content in finished products and stipulated that, after a transition period, domestic content must increase from 50 percent to 62.5 percent of the value of every exported vehicle.

The dependence on imports has on-going adverse financial and economic effects. The high quantity and value of imports was a source of vulnerability when the peso was pegged to the dollar. In 1993, Ramírez de la O predicted that the NAFTA opening would lead to an increase in imports not matched by the volume of exports and that this would create pressure for a devaluation which, in fact, occurred in December 1994.

"We have been doing very well with exports, why isn't the Mexican economy growing more? The multiplier effect is very low."

Low domestic content also impacts the rate of growth. Serra has calculated the multiplier effect of exports and offers this analysis. "For Mexico, it is 1.7, that is, for every $1 you export, your GDP goes up $1.70." In contrast, the multiplier effects for the United States and Brazil are both over three. "We have been doing very well with exports, why isn't the Mexican economy growing more? The multiplier effect is very low."

Low domestic content means, of course, that fewer Mexican firms become part of the supply chain and fewer jobs are created for Mexican workers than might be with greater integration of Mexican products in the value chain. This structure of trade is due to "the absence of a strategy that allows us to take advantage of the enormous comparative advantages and access we have to the North American market," according to Arnulfo R. Gómez. "The dynamism of our foreign commerce is the result of the corporate policies of multinational companies rather than a national development project that includes promotion of national industry, its competitiveness, a healthy structural and geographic diversification of our exports, and strengthening of our internal market."[56]

Logistical bottlenecks continue to plague the flow of goods to the United States and Canada. In Noyola's view, this is because the concept of a free trade agreement (FTA) "requires rules of trade that make physical logistics complicated." For example, the rules of origin regarding local content

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[56] Gómez, Arnulfo R. Mailing list note. Dec. 22, 2014.

demand that costs be carefully traced, so paperwork proliferates. The agreement in NAFTA to allow Mexican trucks to cross into the United States took years to implement. Only in January, 2015, did the United States prepare to open the border for long-haul deliveries. The transportation sector was not opened sufficiently, says de la Calle, and on the Mexican side, customs procedures and train and airline connections with the United States remain cumbersome. Obstructions such as these contribute to hindering the development of backward linkages that would integrate Mexican suppliers into international value chains.

"One of the most far-ranging impacts of NAFTA has been to deepen the cleavages between regions in Mexico."

One of the most far-ranging impacts of NAFTA has been to deepen the cleavages between regions in Mexico. In general, the divisions between the more industrialized, prosperous, and connected North and the more agricultural, more remote, and poorer South have become sharper and more entrenched over the past 20 years. This regional separation follows the pattern of development of Mexico's railway network a century ago when train lines were built from the capital to the northern mining centers and beyond to the U.S.[57] Inequality between regions increased with NAFTA as the northern states received more foreign direct investment, employment expanded, and income inequality was reduced. Southern states saw little benefit from the trade pact, largely due to their lack of infrastructure and lower qualifications of human capital.[58]

Poor Implementation

The implementation of the most important privatizations thwarted the potential of the reforms to stimulate growth, say many of the experts interviewed. Of the hundreds of privatizations, the most significant by far were the sale to the private sector of the banking system, the national telephone monopoly and highways, and the reform that allowed agrarian reform lands, known as *ejidos,* to be sold. New owners of banks and the telephone company were shielded from competition in their initial years of ownership. The implications for the economy of allowing such strategic industries to operate in a protected environment are discussed in the section on competition below. The failure of the banking nationalization is discussed here as a leading example of poor implementation in the reform process.

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[57] I owe this point to a conversation with Enrique Cárdenas, CEO, Centro de Estudios Espinosa Yglesias, Jan. 7, 2015.

[58] Esquivel, Gerardo, and Fausto Hernández-Trillo. "How Can Reforms Help Deliver Growth in Mexico?" In Liliana Rojas-Suárez, ed., Growing Pains in Latin America. (Washington, D.C.: Center for Global Development), 2009, p. 207.

The initial process of privatization of the banking system, when the state-held commercial banks were sold, is singled out as a key failure by many of the former policy makers and economic observers. In the privatization of the nationalized banking system, 18 banks were auctioned off to Mexican buyers in just thirteen months between June 1991 and July 1992. A widely-held belief is that the banks were privatized badly due to crony capitalism. They were sold to friends of then-President Salinas ostensibly so that they would not be sold to foreigners. Foreign participation in ownership of the privatized banks was restricted to small minority stakes. "We protected (the newly private Mexican banks) through NAFTA, we gave them time in the agreement so that they could recover their investment, and that was an error tied to the political system," according to de la Calle.

Getting high prices for the state-owned banks was a priority, and the new owners were allowed to borrow money to finance the purchases. "No one had to put up capital. They did not risk their assets but rather credit from the other bank," says Francisco Gil Díaz, vice-governor of the central bank at the time. De la Calle explains, "This was done in the spirit of keeping foreigners from buying the banks. Not a very good idea."

> "We protected (the newly private Mexican banks) through NAFTA, we gave them time in the agreement so that they could recover their investment, and that was an error tied to the political system."

Many of the new bankers were stock brokers by trade and did not know banking. The banks came with deteriorated loan portfolios and had lost experienced credit analysts during the nationalization period (1982-1992). Authorities did not fully supervise delinquent loans. "They only counted late payments and not the full value of the credit as non-performing loans," says Gil Díaz. The government encouraged mortgage lending and "the best managed and capitalized banks expanded the (housing) portfolio too rapidly."

The build-up of lending on top of weak capital structures in a setting of high government deficit, unsustainable short-term public debt, and a fixed exchange rate regime made for "a highly combustible environment," says Gil Díaz. When the peso collapsed in 1994, interest rates subsequently shot up to over 100 percent a year, triggering widespread defaults. The overall financial system then collapsed. The Zedillo government led interventions and recapitalizations and assumed bad loan portfolios to salvage the banks, and the U.S. government loaned Mexico $50 billion to keep the economy afloat. Later, between 1998 and 2002, the weak Mexican-owned banks were put on the auction block and were bought predominantly by large foreign banks that took advantage of a legal reform allowing foreigners to hold a majority share in banks. The banking crisis of 1994-95 and bailout ultimately cost Mexico 18 percent of GDP.[59]

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[59] Author interview, Agustín Carstens, Dec. 19, 2014. Newell notes, op. cit., p. 52 , that La Jornada newspaper cited in 2005 a World Bank presentation that estimated the cost at 25% of GDP, but adds the World Bank document is not available on the bank's site.

The financial system was devastated, according to central bank governor Agustín Carstens. From 1994 to 2005, "all attention was (directed) to minimize destruction of the financial system" and rearrange the banking system. As a result, he says, during 15 of the last 20 years, the financial system has not been contributing to growth and that explains part of why growth and productivity have been low in Mexico.

The financial crisis of 1994-95 hollowed out family finances across Mexico, annihilated businesses and jobs, and knocked the wind out of the sails of government efforts to modernize the economy. The crisis also "destroyed an entire program of reform and change" because it interrupted and distracted from rolling out reforms, says Roberto Newell. "The fall-out strengthened nay-sayers and made them look like the ones who knew how to run Mexico."

Left-wing politicians parlayed opposition to the reforms to expand their base and even some sectors of the PRI worked against the reforms. "Privatization is now a bad word because it was considered botched, especially in the case of the bank privatization, which was followed by the 1995 collapse and subsequent bailout, and this put a drag on the momentum of reforms," says Tim Heyman, president of Franklin Templeton Advisory Services Mexico.

> "The banking crisis reduced appetite (for reforms) because it gave neo-liberalism a bad name—unfairly, in my view."

The agricultural reform intended to privatize communal farmlands known as *ejidos* is widely regarded as a failure. This constitutional reform made it possible for individual *ejido* members to sell their land parcels with the notion that private ownership would stimulate investment and increase agricultural production. Only small amounts of land have actually been sold. "It's poorly designed," says de la Calle. To sell a parcel, an individual must obtain approval from the *ejido* commissioner and the *ejido* assembly, who are local powers often driven by political, not economic, motives. Although the Constitution was reformed to allow the lands to be sold, the powers vested in the *ejido* leadership "remained in the Constitution," says de la Calle.

The design of the privatizations of state-owned businesses is also questioned. The Salinas-era privatizations did not seek to develop firms that would become national champions and have links to local suppliers as happened in South Korea with the chaebol conglomerates, says Manuel Molano of IMCO. Instead, the logic of the privatizations was to withdraw the state from businesses in which its presence did not generate added value and reduce public debt. Especially in network businesses, privatizations favored monopolistic behavior. Policy has struggled from the 1990s with competition issues related to network businesses and only in the last few years have some results been achieved in taming these substantial market powers, Molano adds.

Structural reforms slowed down after the banking collapse because “the crisis made policy makers afraid of doing things,” recalls Jaime Serra who lost his post as finance minister after the peso devaluation. “The banking crisis reduced appetite (for reforms) because it gave neo-liberalism a bad name—unfairly, in my view,” says de la Calle. “The problem was a lack of trust in markets; neo-liberalism would have opened the banking sector and we would not have had such a severe crisis, Citi and Chase would have suffered the crisis.”

Ill will toward the privatization in the public mind spread into hostility toward reforms in general. NAFTA is the exception and gained acceptance because consumers benefited from a broader offering of products and lower prices on some goods. In fact, trade liberalization stands out compared to privatizations for its favorable impact on the foundations for growth. Trade liberalization “is the only reform that has had positive effects both on the macroeconomic stability foundation and on competition and the broad sharing of growth benefits,” writes Gerardo Esquivel.[60]

Lack of Competition

The first wave of reforms failed to create a competitive business environment. This was most obvious in three of the most strategic and cross-cutting sectors of the economy—energy, financial services, and telecommunications. The energy sector remained a state monopoly and the entire chain of petroleum and derivatives was closed to private investment. Banks and telephony became private commercial enterprises with the completion of the privatization processes in 1992, but they did not face competition and as a result prices did not come down and services did not meet international standards. In short, according to Gurría, the dominant firms in energy and telecommunications “have been able to extract large rents from consumers and faced weak incentives to invest and improve productivity.”

In terms of information and communications technology, Telmex was granted a concession that allowed it to operate as a monopoly in fixed line service for the first five years after the 1990 privatization. The company has remained a near monopoly ever since. The lack of competition costs Mexican firms and customers and erodes competition in the vital sector which makes interconnectivity possible. A 2012 OECD report estimated that Mexicans paid an extra $129

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[60] Esquivel and Fernández, op. cit., p. 212. The authors refer to the foundations of growth in Latin America identified by a group of analysts coordinated by the Center for Global Development in Washington which are: secure property rights; assuring rights that are equal enough to level the playing field in market transactions; creating sufficient economic and political competition to avert state capture; macroeconomic stability; and sharing of the benefits of growth with the population at large. Liliana Rojas-Suárez, ed., Growing Pains in Latin America. (Washington, D.C.: Center for Global Development), 2009, p. 54-56.

billion for phone services between 2005 and 2009, to say nothing of foregone productivity.[61] "Capture is a *sine qua non* in the telecoms sector, it thwarted the purpose we were after," says Roberto Newell, adding that the strong regulator needed to curb the Telmex virtual monopoly was never created.

New regulations and competition authorities created in 2014 as part of the *Pacto* reforms and legislation may reduce the predominance of Telmex and its Mexican cell phone company, Telcel, but this remains to be seen. During the last 25 years, the cost of Internet to Mexican consumers has been among the highest in the 30 OECD countries.[62] Telephone, cellular, and internet service remain plagued with inefficiencies that leave no business or person untouched or undercharged. "The amount of product a monopoly produces is less than the amount of product a sector with competitive firms produces and monopolies sell their products at higher prices," says Serra, summarizing the "less service for more money" double-drag of Telcel's dominance.

"Greater competition has not affected the dimension of the problem: there are six large banks which hold 90 percent of the credit cards and 90 percent of the bank branches."

After the resale to mostly foreign banks, the banking sector has remained concentrated with six large banks and about 30 very small banks. (The only large Mexican-owned bank is Banorte which in 2012 was ranked third in the system in total assets.) Banking experts argue that the sector is competitive but some analysts say the high fees and rates charged by Mexican banks are indicators of a non-competitive environment. "Greater competition has not affected the dimension of the problem: there are six large banks which hold 90 percent of the credit cards and 90 percent of the bank branches," says Esquivel. Their size allows them to capture clients because their networks are more accessible, they have more branches and ATM fees are lower only if you use the ATM of the bank which holds your account, he adds.

The privatizations of banking and telephony and the toll road concessions (which later required a $3 billion bailout) created a negative impact on essential foundations for growth, according to Esquivel. The monopoly power granted in some cases harmed competition, the discretion and contract renegotiations used in awarding infrastructure concessions weakened property rights, privatizations did not create a level playing field in some markets, and inadequate regulation and supervision of banks helped fuel the banking crisis which fractured economic stability.[63]

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[61] OECD. Review of Telecommunication Policy and Regulation in Mexico. 2012. http://www.oecd.org/sti/broadband/50550219.pdf, p. 9.

[62] Ibid., p. 32.

[63] Ibid., p. 211. He refers to the foundations of growth in Latin America identified in Liliana Rojas-Suárez, ed., Growing Pains in Latin America, op cit., p. 54-56.

After seven decades with a closed, protected economy, Mexico produced a large number of uncompetitive businesses and a class of entrepreneurs more focused on developing contacts than products. “We developed a generation that knew the Mexican style—‘know-who’ is more important than ‘know- how’ because you are not subject to competition,” says Jaime Serra. Furthermore, the quality and scale of production are poor and low because the maquila system kept competitive imports out.

Although an anti-trust commission (the Comisión Federal de Competencia, or CFC) was set up in 1993, it was unable to break the power of Telmex as an incumbent monopoly. Similarly, in its 20 years of operation, the CFC was not perceived as having introduced significant regulatory changes or decisions that promoted competition in the economy. “The anti-trust legislation has been modified in a very gradual way and up to now we are getting to a position where [newly constituted competition commission] Cofece has real teeth to tackle issues of competition together with the Federal Telecommunications Institute (IFT),” says central bank governor Carstens. The creation of Cofece with stronger powers, part of the Peña Nieto *Pacto* reforms, is widely expected to issue findings and decisions that will enhance competition.

Incentives

Whether Mexico’s economy offers adequate incentives is a matter of debate. Many of the people interviewed feel that Mexico offers ample opportunities for investment and growth. But, several economic analysts singled out a number of factors that create poor incentives.

With the exception of large companies, “incentives for companies are not high and many of the most lucrative activities are close to the government,” says Elizondo. Government spending amounts to 25 percent of GDP, so many firms are implicitly encouraged to focus on winning government contracts.

The existing incentives for the financial system do not promote lending, says Esquivel. Lending to the federal and state governments allows banks to make a profit taking virtually no risk and meet the Basel risk requirements, he argues. “Banks don’t need to lend to make a profit,” he says. Commissions on ATM usage and high interest rates, especially those charged on consumer credit (an APR of 66 percent per year in an economy with 4 percent annual inflation), assure further strong profits. Interest on business loans is around 14 percent—“because there’s no demand”—and mortgages pay about 10 percent annual interest.

Banks are encouraged to lend to construction, services and agriculture, and all these sectors make low contributions to productivity, says Manuel Molano.

Fiscal policy and labor law foster a “Peter Pan syndrome” in which firms refuse to grow in order to avoid paying taxes and avert the creation of a strong workers’ union, says Molano.

Several of the outcomes of reforms create incentives for corruption, according to interviewees. Alongside the structural reforms, federal transfers to governors and mayors continue apace and are not transparent. There is no accountability vis-à-vis the enormous sums in the transfers.

The reform of communal lands known as the *ejido* creates an incentive for mayors to take land away from *ejido* farmers because municipalities are granted the right to part of the lands when those properties are slated to receive urban services, says de la Calle.

Savings, Investment, and Industrial Policy

Investment, public and private, is critical for stimulating growth in developing economies and the performance of savings and investment in the last 20 years in Mexico has been poor. "The two main obstacles to Mexico's economic growth are lack of investment and inequality," says Moreno Brid. Fiscal reform did not free the government from its dependency on oil revenues, and failure to expand sources of taxes meant that the government was weak in terms of financing counter-cyclical policies, he adds.

Three of the four sources of aggregate demand—consumption, investment, and government expenditure—have been "very sluggish" over the last 20 years in contrast with the export sector which has been growing at double digits with NAFTA, says Serra. Investment in sectors not related to trade has been low. Domestic investment in exports has underperformed, and domestic investment in non-tradables has been poor, he says.

> "The two main obstacles to Mexico's economic growth are lack of investment and inequality."

The dismantling of industrial policy has meant that government funds and development bank loans were no longer available for stimulating particular sectors. The maquila system of assembly has been promoted through government policy. With a few notable exceptions, the maquila has failed to produce domestic value added, says Molano. Mexico must import significant volumes of intermediate inputs to keep producing exports.

Inequality

Income inequality has improved but only marginally by many estimates, and has in fact worsened in recent years, according to the OECD. The persistence of a high level of inequality holds back growth. OECD Secretary General Angel Gurría reported in January that an increase in inequality caused Mexico to lose more than 10 percentage points of GDP growth since the 1980s. A new

rhetoric and emphasis about the impact of inequality is emerging from multilateral institutions, suggesting that this issue will gain importance in explaining why economies underperform.

Moreno Brid of UNAM stresses that inequality is one of the principal obstacles to growth. “We would have a potentially robust market if we took inequality seriously,” he says. However, the share of wages relative to GDP has been dropping for years and real wages have also declined. A new fiscal reform is urgently needed aimed at increasing public investment (without raising the deficit) and at reducing income inequality, he says.

Poverty headcount ratio at national poverty line, 1989-2012

Year	Poverty headcount ratio
1989	53.5
1992	53.1
1994	52.4
1996	69
1998	63.7
2000	53.6
2002	50
2004	47.2
2005	47
2006	42.9
2008	47.8
2010	51.1
2012	52.3

Source: World Bank

Low Morale

The record of the first wave reforms is mixed, as described by the creators and experts engaged in this economic shift over the last 30 years. Punctuated by crises, the reform process has been interrupted at times and the economy has suffered often severe setbacks. The morale and outlook of Mexicans have also suffered as a consequence. The country “lost faith in its ability to stay on course, the cost has been tremendous, it changed our behavior, perception, and whether you can trust our government,” says Newell. The harsh aftermath of crises created a “willingness to believe that everything bad that can happen will happen,” he says. “We’re more pessimistic inside Mexico than people are about Mexico who are outside. That’s been that way for a long time, I don’t know why,” says Rozental. Low morale has economic implications, at the very least, acting as a brake on entrepreneurship and investment.

Part 4 - The Crossroads Today: The Competitiveness Mandate

"It is time to move, Mexico," President Enrique Peña Nieto said bluntly in his inaugural address on December 1, 2012. He called on Mexicans to participate in a great transformation and "change everything that needs to be changed: people, the mentality, institutions." The next day, the president showed how he would get Mexico moving. Peña Nieto and heads of the three leading political parties announced a "Pact for Mexico" that committed them to advancing 95 initiatives to enhance democratic governance, improve transparency, accountability, and combat corruption, reform the justice system and reduce violence and boost economic growth, employment and competitiveness. With a pen stroke, legislative gridlock that had blocked numerous attempts at reforms since 1997 was wiped away.

This remarkable consensus formed the basis for Peña Nieto's proposals for a package of sweeping constitutional reforms that would transform and modernize the Mexican economy. Anchored in the *Pacto*, the reforms presented to the congress over the next year would open the energy sector to private investment, introduce competition into the telecommunications sector, grant autonomy to a federal anti-trust agency and a telecoms regulator, increase government revenues, expand social safety nets, create incentives for banks to lend to small and medium sized businesses, and upgrade dismal public education by evaluating teachers. The *Pacto* calls on government to create the conditions for Mexico to grow at a rate of more than 5 percent per year and explicitly states that this requires raising public and private investment to more than 25 percent of GDP per year. Within 21 months, in August 2014, all of the constitutional reforms had been approved. Even the sensitive energy reform that would end 75 years of state monopolization of oil was passed with the required two-thirds majority.

"His is the most ambitious set of reforms approved in Mexico in decades."

As Peña Nieto promised, Mexico is indeed poised to move. His is the most ambitious set of reforms approved in Mexico in decades. Taken together, the energy, financial, and telecom reforms could add about 1.8 percent to GDP growth annually, and boost economic growth to 4-5 percent per year in the medium term, between 2018 when Peña Nieto leaves office and 2030, according to projections by Marco Oviedo, research director with Barclays in Mexico City. This would be significant in an economy that has averaged 2.6 percent growth per year for the past two decades, although it would still leave Mexico lagging behind Asian growth rates. The crown jewel, the reform that allows private investment in the nation's oil and gas fields and expands opportunities for the private sector in generation of electricity, went far beyond market expectations. "It's the whole enchilada," says

Andrés Rozental, an advisor to multinationals operating in Latin America. "The implementation is the key to whether it's going to work. Some of my clients in the energy sector think it's going the right way, but they have to see the details, the contracts, royalty payments, and fiscal issues whether the government is going to give Pemex a competitive advantage or not."

The Peña Nieto reform package, taken along with the earlier reforms of the 1980s and 1990s make the decades spanning 1985-2015 "a period of conception and big design change," says Rogelio Ramírez de la O, a former advisor to opposition leader Andrés Manuel López Obrador and president of Ecanal, a consultancy that advises multinational corporations operating in Mexico. In his view, Peña Nieto's reforms are the ones that remained pending for the economy from the first wave of reforms, and in this sense represent continuity from the approach to economic modernization adopted since the mid-1980s.

Continuing macroeconomic stability and the Peña Nieto structural reforms will allow for "establishing the necessary conditions for a significant increase in the potential for growth of the Mexican economy without inflationary pressures," says a central bank outlook presentation from October 2014. Independent economists are encouraged by several aspects of this reform package. Juan Carlos Moreno Brid of UNAM says the reforms implicitly recognize that achieving low inflation and getting the deficit down to manageable levels—central goals of the economic stabilization in the 1980s—are not enough.

The government launched draft legislation to stimulate sustained increases in productivity and competitiveness in September 2014, a move which signals a more proactive approach to meeting

Mexico's foremost economic challenges. "Today, all nations have active instruments of economic promotion," said finance minister Luis Videgaray. The law sets a 20-year horizon for government planning and measures that complement the current wave of structural reforms. The bill aims to turn back the constant drop in productivity and achieve steady increases in the productivity "of labor and of all factors of production," said the finance minister. Specific objectives of the law are to promote the formation of value chains and stimulate entrepreneurship and innovation.

The government certainly has a mandate. Mexico's competitiveness rankings sit stubbornly in a middle range. Overall, Mexico slipped from position 53 in 2012-13 to 61 in 2014-15 in the World Economic Forum competitiveness rankings of 148 nations. In the categories of labor market efficiency and security, the country rated 113 and 135, in those rankings, respectively. The World Bank Doing Business ranking places Mexico 53 among 189 economies, and the property registry and tax-paying rankings, respectively, were 150 and 118.

> "Mexico's competitiveness rankings sit stubbornly in a middle range."

Taken as a whole, Mexico's economy underperforms and lacks dynamism. Productivity gains have been marginal, oil output and reserves of crude oil have slumped, penetration of banking and credit remain low, trained talent often leaves the country, and students perform poorly on standardized global tests. Large, modern sectors of the economy remain dominated by duopolies or quasi-monopolies, there are fewer listed companies today than a decade ago, and the number of fast-growing companies is small.

Now is the time to implement the structural reforms and deploy additional strategies to get Mexico on the move.

Part 5 - Moving Mexico: Policy Recommendations

There is no doubt that the current wave of Peña Nieto reforms creates new conditions that improve the potential for increased growth, productivity, and competitiveness in Mexico's economy. The president has pledged to raise growth to 5 percent per year by 2018, his last year in office. The wave of reforms that began 30 years ago has fallen short of expectations on many fronts. As a result, informed observers are keenly aware that even an unprecedented consensus reform package requires a host of supporting measures, all of which must be legislated and then put into practice. Peña Nieto "grew up knowing reforms, he doesn't understand that implementation is going to be hard, that the reforms have to affect all the interests that put Peña where he is," says Luis Rubio. Full-scale implementation will mean reducing the privileges and economic benefits or incumbency enjoyed by many powerful interest groups that have dominated and even controlled sectors of the economy for decades.

> "The president has pledged to raise growth to 5 percent per year by 2018, his last year in office."

Implementing the reforms properly will be neither simple nor easy. Experts say that the reforms address many but not all of the issues requiring attention to set the economy right. The Peña Nieto reforms demand additional enabling policies and regulatory measures and enforcement if Mexico's economy is to be competitive in the 21st century. In addition, other complementary measures are needed to complete Mexico's transformation into a modern, efficient, and productive economy.

Policy proposals were gathered from the experts interviewed. Each person was asked to offer three to five recommendations of priority policies to be carried out now in the context of the current reform package in order to boost growth, productivity, and competitiveness.

There was broad consensus that the highest priority actions to be taken by government are, in the following order: establishing the rule of law and improving citizen security (six former policy makers, six analysts), improving the public education system (three former policy makers, four opinion shapers), rigorous implementation of all the reforms (two former policy makers, two analysts) including the measures to promote competition (three policy makers, 2 analysts), developing transparency (five analysts, one policy maker) and combating corruption (three analysts, one policy maker), and various reforms to the fiscal reform (four policy makers, two analysts). Two analysts called for government to build trust with citizens. Many comments that came forth in interviews reflect a concern about mistrust of public institutions. For example, interviewees cited

citizen mistrust of the judiciary and the tax system, doubts about how public funds are spent, and the processes by which the energy sector will be opened to private investment.

The interviewees do not offer specific action plans for addressing each of their priority issues. This is particularly true in the areas of rule of law, security, and education where their comments reflect the view that comprehensive changes are needed. However, many people mentioned one or two specific policy actions they would propose as part of a broader plan to improve Mexico's performance in the areas that most concern them. Their policy proposals are included here to present their thinking without suggesting that their ideas contain a full-blown program for resolving the problems they identify.

There was a range of ideas and differences of opinion across this group of specialists, and every policy proposal that was offered is included in the recommendations. Some policy proposals were advanced by only one person.

Although the interviewees represent different currents of economic thinking, their views do converge on several key points. The strongest consensus centers on the imperative of establishing the rule of law and improving citizen security, upgrading education, and combating corruption. Many of these economic specialists made strong statements arguing that Mexico must become a country where the rule of law is respected and enforced universally.

"The strongest consensus centers on the imperative of establishing the rule of law and improving citizen security, upgrading education, and combating corruption."

Raising the quality of public education is also widely seen as another urgent priority for Mexico. There is a clear focus on creating skilled workers who are competitive in the global economy. The experts tacitly endorse the policies contained in the education reform—that is, evaluation of teachers' knowledge, hiring and firing based on merit, reduced influence of the teachers' union over schooling, and greater control of public education by the ministry of education.

Greater transparency in government and combatting corruption is the third top priority in terms of the number of times it is cited by interviewees. This is a wide-ranging concern that includes transparency in federal government transfers to states and corruption in licensing of businesses and labor unions.

Policy proposals that would empower Mexican citizens were absent from all but a few of the interviewees. In part, this reflects the fact that the reform leaders and the opinion-makers and economists who track the economy are focused precisely on public policy. Proposals from

interviewees for actions that would empower citizens and integrate them more closely into the work of government are described here. In Mexico's incipient democracy, the process of empowerment requires a deeper government focus on policy outreach and citizens need more training and opportunities for interaction with government.

Rule of Law and Security

Insecurity in Mexico has become one of the two leading concerns of citizens, along with the economy, according to opinion polls. Peña Nieto pledged to reduce violence and create a national police force when he took office. Nearly two years later, the nation was indignant when it came to light that 43 rural normal school students had been kidnapped in September 2014, in Iguala, Guerrero, beaten, tortured, and killed. Their bodies were burned in a nearby municipal dump, according to official investigations. Shortly thereafter, the national gendarmerie was launched and army troops were deployed to the Pacific coast state to establish order. "Those recent events are one more example of the urgent need to strengthen institutions and the rule of law in Mexico. That is the number one priority because rule of law means two things to me: security and freedom. The first obligation of the state is to protect the security of its citizens," says banker Guillermo Ortiz. "The most important thing is to strengthen institutions and the rule of law."

> "The most important thing is to strengthen institutions and the rule of law."

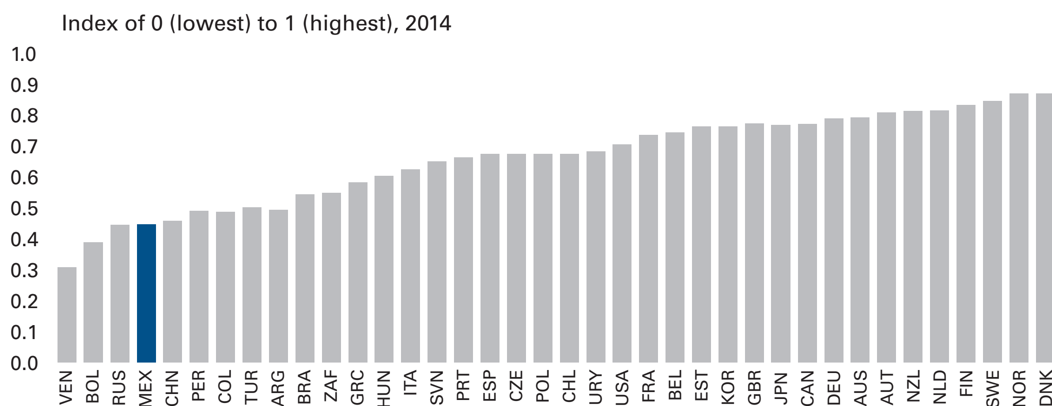
Ortiz is not alone in placing rule of law at the top of public policy priorities for Mexico. Establishing rule of law is "absolutely essential," says Jaime Serra. "This is major, we have to do something serious, otherwise all the programs we carry out are not going to flourish," he adds. The drug war waged by President Calderón from 2006-12, the justice system reform launched in 2008, and recent actions taken by President Peña Nieto have not produced enough results to reassure citizens that they are secure. "You don't see the coherence of all that has been done, you see the activities and not who coordinated that."

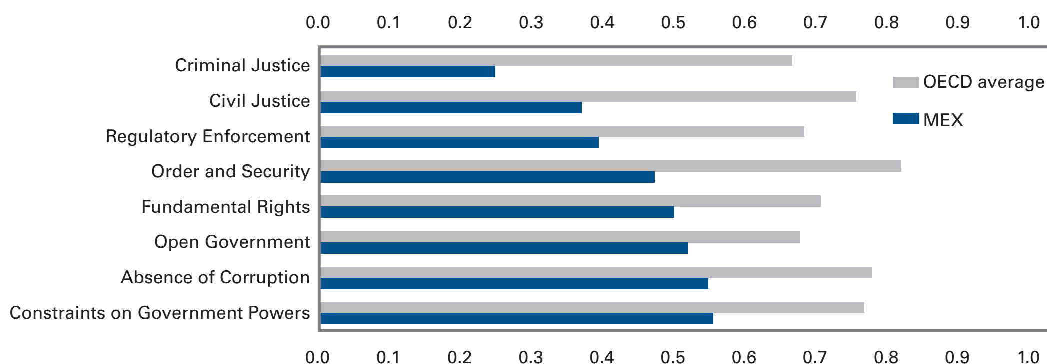
Serra proposes that a justice ministry be created and charged with coordinating all initiatives to improve security. The ministry, which would be headed by a justice czar, would lead efforts to establish rule of law, says Serra. The rule-of-law czar must be a "leader with a magnificent image," and the actions taken in this area should be seen as comprehensive rather than superficial actions that take place in piecemeal fashion.

Enforcing the rule of law and combating impunity require a comprehensive approach and consistent government leadership. Andrés Rozental stresses that the rule of law requires strong judicial institutions. "The first priority to make Mexico competitive is to have a true rule of law and a judiciary that functions, that isn't corrupt, that people can rely on, and that can act as a

counterbalance to the executive and legislative branches. It's better than it was but it's still not where it needs to be." Mexico has been putting in place a judicial reform for the past seven years, but the rate of impunity remains at 98 percent of all crimes. "People don't trust (judicial authorities), the number of crimes reported is low, and the actions taken to resolve them are minimal. It is fundamental to strengthen issues of judicial power--obviously police, everything that has to do with juridical security and protection of citizens," says Ortiz.

Ranking of Rule of Law in Mexico





Source: OECD Economic Surveys, Mexico, January 2015, p. 80, based on data from Rule of Law Index 2014. The World Justice Project.

Having a functioning rule of law in place would permeate all aspects of national and civic life and, of course, impact the economy. The cost paid by citizens and firms to assure security has been estimated at as much as 2.5 percent of GDP, a drain of resources that might be channeled

to promoting businesses and growth. Reform of justice institutions and strengthening of the rule of law should center on efficient resolution of civil, commercial, and criminal matters and also improve the transparency of government procurement, says Gurría. Clear rules allow citizens to give free rein to their entrepreneurial spirit and develop their abilities while a corrupt bureaucracy that creates obstacles "is an important drag on productivity and competitiveness," says Ortiz.

Law enforcement is weak in Mexico, and government authorities must take responsibility for enforcement. "Here, vested interests are in charge and are outside or above the law," says Eduardo Fernández. "The laws are not bad, but they are not enforced or they are applied to some people and not others," he says. Mexico's weak institutions make it possible for powerful interest groups to have their way. He points out how the leading television networks have come to have blocs of federal deputies in congress where they make laws that favor their interests.

> "Having a functioning rule of law in place would permeate all aspects of national and civic life and, of course, impact the economy."

Reforms to police forces are proposed. A meritocracy should be introduced into police forces and decentralization of security forces should be eliminated in favor of centralization of policing, says Roberto Newell. About 100,000 police should be deployed nationwide along with marshals and judges, he says. "It is a state of emergency, not an invitation to behave in an authoritarian fashion," says Newell. A different proposal is offered by Carlos Elizondo who says that eliminating municipal forces would be ill-advised. "The existing instruments must be used to pressure governors and mayors to become involved in the issue of security." The federal government should exercise oversight of spending by state governments and react quickly when there is evidence that a mayor is linked to organized crime, he says.

Several specific suggestions were advanced by interviewees. Judges of state courts should be dependent on federal authorities instead of owing their jobs to state governors who currently appoint judges; this would create more accountability in the judicial system, says Isaac Katz. When the law is enforced, the measures are often overkill. "We have many rules with severe punishments that have a low probability of being enforced," says Manuel Molano. He argues that lighter penalties should be considered but must actually be enforced so that people become aware they may have to pay the cost of disobeying the law. Extortion which is now widespread must be eliminated because it hurts business in general and threatens small businesses in particular, making them unable to invest because of the financial drain caused by paying extortion, says Carlos Heredia.

Education and Human Capital

Many of the policy makers and analysts placed an overhaul of Mexico's education system as the second highest priority for public policy. Recommendations were made for tackling educational deficiencies that go beyond the ambitious measures in the reforms that, if implemented, would establish a meritocracy in public school teaching.

The reform program to use testing of teachers to raise the quality of teaching is a long-term project and its full impact will not be felt for 10 or 20 years. During that time, myriad actions must take place if the education reform is to produce quality public education. Having succeeded at increasing the availability of schooling, the approach must shift to focus on improving the quality of education, says Santiago Levy. This requires proper implementation of the secondary laws to the education reform, teacher evaluations, and a remake of the entire model of forming human capital in primary and secondary schools, he adds.

The "equity and efficiency of education spending" must be improved, says Gurría, which requires refocusing government expenditures on pre-primary, primary, and secondary education along with improving the quality of teaching. "Education has to go from the crèche (child care) all the way through" secondary schooling, he says. Studies now show that children who attended child care program achieve results on standardized PISA tests that put them between six months and two years ahead of their peers who did not go to pre-school.

Mexico's public school curriculum must be reoriented so that students are taught skills that match what the market demands. "The model of education must be changed from a model based on knowledge to a model of competencies—hard, or technical, skills, and soft skills such as leadership and problem-solving," says Luis Serra Barragán. "This is not in the reform, it is not a reform that will detonate improvement in Mexico to be on a par with other countries." The digital gap and knowledge gap must also be closed, says Roberto Newell. Mexican students need to learn English, and their ability in mathematics, sciences, and reading—well below the average for OECD countries—must also be improved.

"Mexico's public school curriculum must be reoriented so that students are taught skills that match what the market demands."

Without these and other changes, Mexico cannot pretend to foster innovation. "To bet on innovation, your educational system has to lead," says Gurría. "Our educational system did not evolve, it was holding us back. And we did not embrace innovation as a culture, as a state of

mind." Support for innovation is scant in Mexico: spending on research and development totals 0.4 percent of GDP, while Korea and Nordic countries invest six to 10 times more in seeking cutting edge knowledge, according to the OECD.

New incentives are needed to reward merit among teachers, in the view of Carlos Heredia. "The reform only changed hiring and firing (practices); what is needed is an incentive that connects the performance of teachers and students." He also advocates that the tools and methods for training teachers and for giving classes must be changed in order to improve the quality of education.

Investment in public universities has not expanded during the last 30 years, says Esquivel, causing ever-greater competition for entry among Mexico's large youth population. As fewer students are admitted relative to applicants, social mobility that was once made possible by acceptance to public institutions of higher education is now limited. Access to university education is poor relative to Mexico's income level, says Esquivel. More scholarships are needed to help qualified students from poor families get a college degree or pursue post-graduate studies.

Corruption and Accountability

Corruption and impunity go hand in hand with lack of rule of law. "The three are in the same basket, you have a system where 'if you don't cheat, you don't get ahead'," says Rozental, quoting a popular Mexican saying. Corruption is costly because it undermines trust in public officials and institutions and it costs between 1.5 and 2.5 percentage points of GDP growth, according to World Bank and OECD estimates. The Peña Nieto proposal to create an anti-corruption prosecutor must be implemented properly, transparency legislation needs to be well designed "and the correct decisions must be taken regarding the evident thieves who are in Mexican politics, and the signal should be sent that this has a price," says Carlos Elizondo.

Government spending must be made more transparent, particularly the enormous federal transfers to state governments, says Isaac Katz. Transparency would improve the efficiency of public expenditures, and zero-based budgeting could be a means for increasing accountability of government because it requires analysis of the results of federal programs, he says. Mexican citizens must be educated over time to know what questions to ask of their authorities to inculcate transparency in the body politic, says Serra Barragán.

"Corruption is greater now because there is no chain of command" as when PRI remained a dominant and disciplined political force in the last decades of the 20th century, according to Eduardo Fernández. The strategy for combating corruption, and particularly the misuse of the huge federal transfers to state governments, would be to concentrate more power at the federal level, in the opinion of Fernández. Discretionary powers of state governors should be removed, and their

spending of federal funds should be subject to federal-level audits in which congress participates, he proposes.

Interviewees cited institutions that must be targeted for combating corruption, including labor unions and the police force. Corruption among traffic policemen who often take bribes for overlooking driving violations would be reduced, and traffic rules would be enforced, if every officer were allowed to issue tickets and to keep 20 percent of the fines, says Rozental.

Implementation of the Reforms

Whether and how the reforms are implemented is a common preoccupation among the experts. "Implement the reforms, that would be my recommendation," says Francisco Gil Díaz, adding that it is of vital importance that the energy and telecommunications reforms be carried out in full. The reform package is like a big ship that must be navigated across the high seas and brought to port safely, says Santiago Levy, suggesting that getting the legislation and implementation right will involve some rough sailing.

The top priority for the OECD's Gurría would be to "fully implement the current reform package with close monitoring at a high political level, and strengthen administrative capacity and quality of governance at all levels of government." The reforms are complex and their success requires applying many technical measures and lining up proper support from government and independent agencies to create an optimal enabling environment.

The approach taken to carrying out the reforms is vital for their success and, indeed, for modernizing the state and its relationship to economic policy. The state must "move from a government that thinks its role is setting rules to a government that thinks its role is implementing rules," says Newell.

> "The state must move from a government that thinks its role is setting rules to a government that thinks its role is implementing rules."

The energy reform is expected to have the most far-reaching impact on economic performance. "Achieving a smooth landing for the energy reform will open the door for bringing investment and making linkages to the economy that can lower costs" such as the price of electricity, a vital input for the manufacturing sector, says Carlos Elizondo, recently appointed as an independent member of the governing board of Pemex.

The telecoms reform implies implementation of many technical measures and tight oversight and enforcement by the new supervisor-regulator, Ifetel (IFT), says Francisco Gil Díaz, CEO for Mexico and Central America of Telefónica, the largest rival in Mexico of the América Móvil wireless

services giant. Several early decisions of IFT "endanger the success of the telecommunications reforms," says Gil Díaz. He cites the failure to address the Telmex interconnection rates contested by other providers, a missed deadline to investigate dominance of some players in telecoms market segments, and short consultation periods on cost modeling which don't allow enough time for concessionaires to formulate correctly their comments. More action is needed to make it clear that the reform will take effect in such a way that a level playing field is created in telecommunications.

Reform of the Fiscal Reform

Tax policy is controversial. President Peña Nieto's tax policy took effect in January 2014, making it the first of his reforms to produce observable effects. The measures to raise taxes on upper incomes to 37 percent from 35 percent and increase taxes on businesses have caused the reform to take the blame for slowing growth in the first two quarters of last year. However, the reform also produced an increase of more than 3 percent in federal tax revenue during 2014 along with criticism that the new tax laws have eroded Mexicans' ability to save.

Tax policy requires a new approach overall plus a host of specific reforms, say many of the interviewees. The leading method for raising taxes should shift from the current focus on taxing income of firms and individuals to a greater emphasis on taxing consumption, say three former finance ministers, several former policy makers, and a number of academics. Taxes on income should be lowered and the Value Added Tax (VAT) should be applied to all consumption, say Eduardo Fernández, Santiago Levy and Viridiana Ríos. This would mean that the VAT would be applied to food and medicines which are currently exempt. This proposal echoes an approach floated by previous administrations but which has been blocked repeatedly by the left-leaning PRD party.

In 2012, Levy calculated that if the VAT were applied to food and medicine, revenues would rise by 3.3 percent of GDP. He proposes that general taxes be used to create a universal social security system that would apply equally to formal and informal workers and reduce the incentives for individuals and firms to remain in the less productive informal sector.

An alternative view came from three experts who called for a progressive system of income tax that would levy higher taxes on the wealthy. Tax exemptions which traditionally favor Mexico's biggest corporations and largest fortunes should be eliminated, says Moreno Brid. He also proposes creating a social pact between the public and private sector in which both parties agree to invest more.

For Luis de la Calle, the number one public policy priority is to collect property tax. "The great fiscal and political reform in Mexico is the property tax reform." The tax is hardly collected outside

Mexico City, he says. Nationwide, Mexico collects the equivalent of 0.8 percent of GDP in property tax compared to about 3 percent raised in modern countries, according to his figures. If the tax were paid, it would generate more revenue than would be raised by charging VAT on food and medicine.

> "The great fiscal and political reform in Mexico is the property tax reform."

Better enforcement and some specific new taxes are required. Tax evasion must be reduced. "Green taxes" should be promoted through increasing taxes on emissions and other environmental hazards, says Angel Gurría.

Experts raise questions about the sustainability of fiscal policy. The energy reform projects a continuous decline of government dependence on Pemex oil revenues. This means the state must raise additional monies to make up for transfers from Pemex that have funded up to 38 percent of the budget annually in recent years. While taxes on private investment in oil and gas will boost government coffers, and the 2014 income tax reform may continue to produce increased federal revenues, the government could still be pressed in the future to raise enough to make up for a drop in income from Pemex.

Fiscal management and a balanced budget could be derailed if the pension regime is not reformed, says Newell. He calculates that the mandatory contribution set for formal sector workers to pay in to individual pension funds (Afores) is insufficient to fund a reasonable pension. The paid-in contribution of workers should be increased to about 20 percent of their income throughout their working life if they are to receive 70 percent of their final income during retirement, he says. Political pressure from an expanding population of poor pensioners could create a de facto financial obligation for the government. "You have to look into the future and ask: did we avoid a fiscal crisis (after the 1997 pension reform) or just postpone it?"

A host of measures are proposed by Manuel Molano of IMCO to stimulate business and production. More business deductions should be offered to proprietors of small enterprises to induce them to formalize their firms and enter the tax rolls. Reduced taxes should be offered for purchases of machinery that will help raise productivity of firms; and discounts should be offered on sales made to formal firms. Molano also proposes that current fiscal policies that create an incentive for high levels of investment in housing should be reduced to channel investment into more productive sectors. He believes that the current 35 percent tax rate on rental properties drives landlords into informality. By lowering the effective tax to a rate of 15 percent and allowing deductions of maintenance costs, more landlords would pay taxes.

Infrastructure is singled out as an area requiring reform. Often, infrastructure projects are funded based on poor planning and ultimately produce inadequate benefits. More spending on infrastructure

is needed to enhance Mexico's competitiveness; but, the highways, ports and railways to be built should be selected based on a comprehensive plan built around a vision aimed at stimulating regional development, says Gerardo Esquivel. A little pork barrel spending would be healthy, he suggests, if the view is to create ports, airports, and multi-modal connections in underserved regions, such as the south and southeast of Mexico. Lesser amounts of carefully targeted spending in infrastructure can produce positive results, says Serra Barragán of CIDAC. "Infrastructure is an area where small things can make the difference."

Capital Accumulation and Industrial Policy

Voices in favor of an industrial policy, or strengthening development banks, come from different camps and the new Peña Nieto initiative for productivity suggests that government will now venture into this realm. Opinion for a government-led industrial policy is not universal, however; some of the leading technocrats from the Salinas period still favor a laissez-faire approach that relies on the autonomous anti-trust authority to create competitive markets.

> "Mexico's development banks can play an important role in advancing industrial policy by extending guarantees to private commercial banks for lending that reaches informal enterprises."

A policy of achieving high capital accumulation during the next 20 years is needed to reach higher growth, says Ramírez de la O. Investment and reinvestment should reach levels like those seen during the 1950s and 1960s. An important caveat, though, is that a government program to stimulate high capital accumulation must be accompanied by adequate funding for social safety nets. Sectors in which Mexico can still induce a high rate of capital accumulation with established Mexican players include the steel industry, mining, domestic transportation, a few shipping companies and agricultural products such as tomatoes and avocadoes, he says.

Mexico appears to be on the road to adopting an industrial policy, albeit timid, says Moreno Brid. The government initiative to promote productivity seeks to integrate small and medium enterprises into large-scale value chains and strengthen the domestic economy. This policy departure is a welcome move which offers an opportunity to push the development of linkages between international or transnational firms and Mexican producers, creating a host of local suppliers, says Moreno Brid. "Governments, in coordination with the private sector, should not be afraid of choosing sectors" for applying policies to advance industrial development, he says, noting that such policies have been pursued in the US, the UK, many OECD countries, and China and other Asian economies.

Industrial policy should be designed to stimulate growth and increase value added in the export sector, says David Ibarra. A specific proposal is to set up a center to promote productivity and

technology in export industries, particularly in automobile production, says Ibarra. Mexico's development banks can play an important role in advancing industrial policy by extending guarantees to private commercial banks for lending that reaches informal enterprises, says Ortiz.

Jaime Serra, former trade minister, largely defends the approach adopted 30 years ago. Industrial policy should focus on promoting competition with measures such as a strong mandate for the anti-trust commission, Cofece. Protectionist measures like the allocation of a minimum of 25 percent of machinery, logistics, labor, and services reserved for local Mexican suppliers in the energy reform should be eliminated, he says.

Competition

The Peña Nieto reforms for a stronger anti-trust commission (Cofece) and a regulator to stimulate competition in the telecommunications industry (IFT) are seen as significant moves to reduce the power of near-monopolies and oligopolies in strategic sectors of the economy. A competitive business environment would bring marginal pricing to bear on the entire economy and destroy monopolies through everyday pricing, says Noyola.

More regulation and enforcement of competition are necessary to make the reforms work so that Mexicans benefit from having greater choice, better quality, and lower prices from their service providers. Reducing the cost of network industries including energy, telecoms, and financial services promises substantial savings across many sectors of the economy, says Ortiz. The costs of services provided by these network industries have a multiplier effect on all businesses and the economy as a whole because they are essential inputs for all economic activity.

Opening the energy sector to private investment is a historic move but gas has been left as a monopoly controlled by Pemex, says Gil Díaz. Because gas is an input for so many manufacturing industries, increasing domestic production and lowering its price would be vital for enhancing Mexico's competitiveness. Some analysts propose that the energy sector must be linked to production chains and electricity costs must be lowered.

Even if the business environment becomes competitive and monopolistic and oligopolistic industries lose dominance and inertial advantages in their sectors, Mexico will still have to grapple with monopoly-like powers in the social and political arenas, says Rozental. Unions continue to hold sway over educational policy and contract arrangements and their use of funds, often provided by the government, need to be made transparent.

Back to Basics: Rebuilding Trust

Policies and actions are needed if citizens are to trust government. Some specialists consider this the first step that government must take. "What Mexico needs belongs more in the field of acknowledging the void of leadership, confidence, and mutual trust. There is no mutual trust between government and citizens," says Ramírez de la O. The lack of confidence gives rise to overregulation, excessive red tape, and procedures that take time and money from citizens. For example, an employer must file 132 reports per year to the federal tax authority and social security and workers' housing funds. Similarly, onerous paperwork is required to liquidate a business, says Arnulfo R. Gómez.

> "Policies and actions are needed if citizens are to trust government."

Bold actions could catch the attention of the public and shift the skeptical or cynical spin that typically colors how officials and policies are viewed. Salaries of government officials should be reduced. "Show people you hit their pockets, eliminate perks," says Carlos Heredia. Such a move could be carried out with an executive order, would not require legislation, and would be something that people could relate to, he says. A similar proposal comes from David Ibarra. "Instead of being an impervious elite, senators and deputies should pay attention to promoting the general well-being of citizens," he says. An initiative to reduce paperwork, simplify bureaucracy, and limit new red tape would demonstrate government's concern for serving citizens and could help establish mutual trust, says Ramírez de la O.

A number of people suggested that a good place to start to increase trust between government and citizens is with regulatory regimes. Sweeping changes are proposed. Deregulation is a high priority and it should be examined in relation to "just about everything, including simple things like company formation and the payment of taxes," says Tim Heyman. "The government gives little power to the state's capacity to regulate," and has the attitude the private sector does things better, says Esquivel. Better regulations could result in lower banking fees, he suggests, and have a direct impact on citizens' lives. The capture of regulatory institutions by powerful economic interests must be rolled back to create rules for genuine competition. Streamlining regulations and improving them would go a long way toward improving the business environment and might earn some good will for the government. A retooling of regulations features among the top five priorities of Angel Gurría. "Dismantle the regulations, have better regulations, then have smarter regulations—it does not mean you have a deregulated economy—you have to have a well regulated economy."

Mistrust of government is abetted by the political system which for nearly a century has prohibited successive reelection of the president and most other officials. Discontinuity is institutionalized. Incentives for short-term decision-making are maximized. Credibility of government is eroded.

The worst effects of this policy on public management play out at the municipal level, where mayors are elected to 3-year terms. The president and governors serve 6-year terms. In another historic shift, the political reforms approved in 2013 lift the ban on reelection of mayors (except for Mexico City where the term already is six years). This measure creates incentives for government that is accountable and opens the door to continuity of policies. The benefits could be great. Long-term needs such as upgrading water systems, sewerage, and drainage could come to be favored over flashy public works like sports stadiums. The country's deficient urban infrastructure, including poor municipal water systems, could be better run to offer improved service. At the least, conditions will be in place to allow for planning that takes into consideration future needs of the expanding urban population.

> "Dismantle the regulations, have better regulations, then have smarter regulations—it does not mean you have a deregulated economy—you have to have a well regulated economy"

At the state level, where governors exercise discretion over vast federal transfers, the one-time, 6-year term remains in place. Some states—notably Colima and Yucatán—have successfully improved their administration and planning, says Molano. The key to their strong performance has been the decision to keep in place the same directors of public services from one governor to the next. Better policies can build trust over time.

Financial System and Credit

Mexico's banking system is very small for the needs of the country and the challenge is to increase penetration of banking and expand financial inclusion, says Guillermo Ortiz. Uncertainty about the access of lenders to legal recourse and recovery of assets when credits go bad should be reduced with the Peña Nieto financial system reform and could help lower the cost of credit.

More adjustments are needed to lubricate the financial machinery and expand lending so the economy can grow. Molano suggests that bankruptcy proceedings be expedited by holding auctions to determine the order in which creditors are paid. Today, workers are paid first, the tax authority second, and lenders third. In an auction proceeding, all capital would get equal treatment, the parties would be asked to reduce debt and then receive their payments in the order decided by the auction.

Improved regulation is needed for the financial system, says Esquivel. The number of commissions charged to account-holders should be reduced, regulations are needed to limit the power of collusion among the largest six banks, and a debate should be held about setting caps on interest rates.

Mexico's development banks should lend to economic activity with lower interest rates that are closer to international levels, and abuses of private banks should be regulated, says David Ibarra. He also advocates for an agricultural bank that would lend to producers who hold less than five hectares of land to support small farmers plus make available to them an agricultural insurance program.

Strengthening NAFTA Integration

Former policy makers, especially those who participated in NAFTA and other trade negotiations, and academics argue in favor of deepening Mexico's trade integration with the United States and Canada. Taking an approach that looks at the North American trade area as if it were a customs union "makes you think about what unifies us…the flow of factors of production" and would create a more unified economic region with greater efficiencies, says Pedro Noyola. Better integration in North America would allow the free flow of factors of production by facilitating labor mobility, a regional energy plan, and a regional security plan, he says. Noyola believes that the failure to develop an energy grid and security agenda for North America contributed to the dichotomy of the Mexican economy.

"Better integration in North America would allow the free flow of factors of production by facilitating labor mobility, a regional energy plan, and a regional security plan."

The future of NAFTA depends on the competitiveness of the region, and both an intraregional and extra-regional agenda must be moved forward, says Serra. Within the NAFTA region, a common energy policy must be agreed upon and then implemented; a trilateral program is needed to improve logistics, and trucking and labor mobility must be allowed, he says. In the extra-regional arena, the three NAFTA countries should coordinate when they participate in other trade negotiations. For example, instead of the United States holding its own trade negotiations with the European Union which already has an agreement with Mexico and Canada, "the natural thing would be an agreement between NAFTA and Europe," says Serra. The U.S. Trade Representative has turned down that idea. Serra proposes a clause be negotiated so that the three separate agreements merge into one over time.

Trade policy "should unite us more to the United States, but policy should increase the value added of Mexican exports," says David Ibarra. He proposes that negotiations be undertaken with U.S. firms to make way for an upgrading of Mexican products exported northward.

Trade experts are somewhat circumspect about the Trans-Pacific Partnership (TPP) which would create a twelve-country trade and investment area on both sides of the Pacific. Mexico must participate in the Partnership and bring a significant negotiating agenda to the talks, says Luis de la Calle. "The quantitative benefit is marginal but the qualitative benefit is very large: Mexico must have an offensive trade policy toward Asia and not a defensive trade policy." The TPP marks the turning point, "the beginning of a cultural and psychological change to see Asia offensively," he adds.

Serra foresees that the TPP will cost Mexican exporters because new environmental and labor standards will form part of the agreement. His proposal is that the Mexican team negotiate that all trade and investment flows generated in the North American region be governed by NAFTA rules.

Inclusive Growth and Productivity

The dichotomy between the informal and formal sectors should be eliminated. This is "the only way to have a model of inclusive growth," says Santiago Levy. He proposes that all citizens, formal and informal workers alike, have access to health care, unemployment insurance, social security, pension, and disability plans. This would change incentives and, consequently, productivity. The social safety nets would be financed through extending VAT to food and medicines, and all types of firms, formal and informal, would pay the same labor costs, he says.

Empowerment

Several comments or proposals are directed to empowering Mexicans to act as citizens and demand quality public services from government. The concept that must be adopted is to "stop thinking of people as voters and think of them as tax-payers, people who pay for services," says Molano.

"For poor people, it is very important to charge them property tax because it is the same as telling them they own the land, it recognizes them as property-holders," says de la Calle. The result of affirming their property rights would be that they would then demand better urban services, proper police security, and telephones that work. "Treat them as citizens," he says.

Failure to collect property tax allows mayors to shirk responsibility for raising revenues and to depend instead on federal transfers which are hard to monitor. "Citizens have no incentive to track funds because they are not paying directly," says de la Calle. Since municipal governments don't collect the tax, they don't need to protect property rights. An incentive for modernization of municipal government could be created by conditioning federal transfers based on how much is collected in property tax, he proposes. The proportion of transfer paid would vary with the relative wealth or poverty of the municipality.

Implementation of the education reform offers a good opportunity to take steps to empower parents and allow them to play an active, informed role in promoting and supervising quality teaching for their children. School districts that offer good teaching and produce high-performing students have been identified around the country. The reform should include the creation of programs that take parents from poor school districts on visits to the best school systems to see quality education in action so they can demand this of their school supervisors and teachers at home, says Carlos Heredia.

Part 6 - Conclusions

The leading challenges for Mexico in the immediate future are establishing the rule of law, improving the quality of public education, and combating corruption. The strongest points of consensus among policy makers and analysts were found around these policy areas --some variant of each appeared in every interviewee's top three priorities. Addressing these challenges will require continuity of policy and resource commitments over the medium term. However, experts agree that there must be no delay in starting the process.

The people surveyed endorse the Peña Nieto *Pacto* reforms package. In fact, many of their policy proposals seek to ensure that the reforms are carried out to the letter. Two former finance ministers made forceful calls for the reforms legislation to be translated into appropriate regulations that are then fully enforced. Implementation of the reforms is the number one policy recommendation of both Angel Gurría of the OECD and Francisco Gil Díaz of Telefónica. However, the demand for reform in the Mexican economy extends beyond the Peña Nieto legislation, and quite a few of the policy recommendations propose adopting alternatives to the reform package now in place.

"The leading challenges for Mexico in the immediate future are establishing the rule of law, improving the quality of public education, and combating corruption."

The importance of displacing the rule of privilege and embracing the rule of law runs deep among the experts interviewed and cannot be overemphasized. "I think the only fundamental shift Mexico needs is rule of law and governmental accountability, which are the same. That is the core issue. Until and unless that is settled, no matter what is done, it won't change current trends," says Luis Rubio of CIDAC. Five former policy makers and one analyst all say that the rule of law is the number one priority for reform at this time. They are joined by one former policy maker and five academic analysts who placed rule of law and security among their top priorities for action.

All of the top three priorities require a fundamental shift in the approach taken by government and a metamorphosis in cultural attitudes. Having policies in place that apply equally to all persons and firms is "not yet embedded as a core principle" in Mexico, says Pedro Noyola.

Educational policy must make a dramatic shift to focus on providing quality education that develops skills and competencies which allow Mexicans to find employment and permit Mexican industry to drive growth through innovation. Seven specialists—three former policy makers and four observers—place quality education among their top priorities. The vision of human capital

must be expanded, more women should be brought into the labor force, and Mexico should open the doors to immigration and recruit foreign talent to spur innovation and other key industries, says Gurría.

The culture of concealment, back-room deals, and favoritism in government must be replaced with a practice of disclosure, a discipline of honesty, and a principle of fairness. Transparency and combating corruption is among the top priorities for seven of the interviewees, including two former policy makers and five academics and policy analysts.

The success of the Peña Nieto reforms will depend to an important degree on the response of private businesses and investors to new opportunities. Several executives and investors recently reflected on the new wave of reforms and the overhang left by the reforms of the 1980s and 1990s. They share the concerns of the experts and advocate similar priorities for change.

Few people benefitted from privatization because the process did not include selling shares on the open market. Former President Salinas favored developing corporate champions to have a leader firm in each sector, said Ricardo Peón, former CEO of ING Investment Management Mexico and now an impact investor. Over time, those firms became oligopolies, charging high prices to Mexican consumers.

The history of reform in Mexico, therefore, generates skepticism about the new reforms that, as in the past, are sold to the public with a large dose of optimism. The reform program as it stands keeps the government in the driver's seat on directing economic policy although autonomous competition agencies and the opening of the energy and telecoms sectors will expand the scope of private business in the economy, said Peón.

Despite these concerns, the potential of the Peña Nieto reforms to reshape Mexico's economy is clear to businessmen. "The energy reform will be difficult to implement and will require a huge effort and dedication from most government sectors because, ultimately, it involves dismantling a protected state monopoly and opening most of the petroleum and electricity value chain to market competition," said Ernesto Hanhausen, an investor in energy efficiency projects.

Other conditions must also be in place if the reform potential is to be realized. "We have to have a legal system that works, and that will bring more foreign investment and generate more Mexican investment because a lot of Mexican capital invests elsewhere," said Lars Christianson, a chemical engineer working in the energy sector.

The private sector needs reasonable access to bank lending, and this has historically been a stumbling block. Hanhausen spent ten years seeking loans from commercial banks for projects to conserve energy at large Mexican beach resorts, investments that were totally secured because they would be repaid with the cash flow from the energy savings plus the hotels put up full guarantees on the project costs. Large banks told him they wanted larger projects and small banks did not understand the projects until he trained their staff. A national development bank promised a loan guarantee, but failed to deliver after 18 months. "We were limited in our ability to grow," he said at a lunch with colleagues.

> "The history of reform in Mexico, therefore, generates skepticism about the new reforms that, as in the past, are sold to the public with a large dose of optimism."

Barriers to innovation must be broken down. Regulatory authorities should change their conventional attitude and adopt the philosophy that firms can engage in any activity that is not prohibited in order to open up new areas of invention and production, said Peón. Mexico attracts only minimum private equity capital because family-held companies are prevalent and refuse to give up control to potential investors. "Investment won't necessarily bring about more growth. If we want to reach growth of 7 percent, we need a system of innovation and for that education has to be oriented toward innovation," said Lars Christianson, who leads a UNAM project to market biotech products developed by the university's research engineers.

The in-depth interviews revealed high levels of support for specific priorities for public policy: a tax reform (four former policy makers, and two observers); actions to promote capital accumulation and industrial policy (two former policy makers, two analysts); competition reform to create a strong anti-trust authority and level playing fields in key sectors (three former policy-makers, and two observers); deregulation or more sensible regulations (two former policy makers and two analysts); a variety of policies to build trust and credibility in the executive, legislative, or judiciary branches of government (three former policy makers, and two observers); and a host of actions in commercial and development banks, the judiciary system, and bankruptcy proceedings to make more credit available and lower the cost of loans to businesses and individuals (two former policy makers, and two observers).

For the three former senior trade negotiators, a top priority is to develop a new approach to NAFTA that would deepen integration by creating regional energy and security systems. A greater role for the state in the economy is encouraged by experts who favor an active role for government in setting industrial policy. Roberto Newell backs a shift away from a government centered on setting

rules to a government that executes rules. Finally, two former policy makers, one now a banker, say it is a priority to break down the differences between the formal and informal sectors, providing protection for informal workers through a package of social benefits for all citizens, and better incentives to encourage informal firms to become formal. "Basically, the costs of formality must be reduced, one of the big incentives for the informal sector can be access to the financial system," says Guillermo Ortiz.

A number of policies were proposed by only one or two experts. These include taking a more inclusive approach to the labor force by bringing more women into the work force and actively recruiting foreign talent to come to Mexico to work; changing urban land use policy to introduce planned settlements and obtain cost-effective delivery of water and other services; promoting regional planning and industrial clusters to boost economic growth and job opportunities in underdeveloped regions; revamping agricultural policy to create better incentives for agricultural production; and redirecting subsidies so that small farmers who really need them receive support.

The cost of doing business must be reduced to gain competitiveness and many of the current reforms and policy proposals point in this direction. A functioning anti-trust commission and open energy and telecoms sectors would lower the cost of basic inputs to industry and services. "The competition reform is harder to do than any other because it steps on the wealthy, decision makers, and those who shape politics and policy," says Viridiana Ríos. A financial system built around incentives to lend and supported by agile bankruptcy proceedings would make credit more accessible to business. "Lowering (transaction) costs is like chipping rock," says Isaac Katz, hinting at the degree of effort required in the years ahead.

"Mexico would advance in competitiveness, gain in productivity, and enjoy a more credible government."

Instituting the rule of law, for example, would demand that government complete implementation of the oral trials system launched as part of the 2008 judicial reform, police forces be cleaned up and retrained, district attorneys be professionalized and a career service with decent pay be developed for them, the independence of the judiciary be strengthened, regulatory bodies be free from capture by powerful interest groups, specialized commercial tribunals be set up and run by properly trained judges, and contracts be fulfilled to mention a few essential components of a genuine legal system cited by interviewees. Officials, citizens, and businesses would have to accept that laws are meant to be obeyed and enforced and that violations are punished.

The enormous effort required to implement the changes proposed by the experts interviewed would be compensated by the potential benefits from implementation of proposed reforms and policy approaches. Mexico would advance in competitiveness, gain in productivity, and enjoy

a more credible government. Greater productivity and more competitive industries and higher skilled workers would boost economic growth. Higher economic growth would, in turn, create more opportunities for Mexicans to be employed, raise their standard of living, and feel that a better future is within their grasp.

Mexican citizens show they are ready for change. Across Mexico, country roads are punctuated by speed bumps designed to make drivers slow down as they approach any of thousands of small towns. “The speed bump,” says Luis de la Calle, “symbolizes the absence of rule of law.” But, in the city of San Cristóbal de las Casas, in the state of Chiapas, speed bumps have been replaced by stop signs—and drivers actually stop. “Mexicans,” says de la Calle after a moment’s reflection, “are more modern than their elites.”

Persons Interviewed

Biographical Highlights (1985-2015*)

Policy Makers:

Luis de la Calle

Managing director and founding partner, De la Calle, Madrazo, Mancera, S.C., (CMM) a consulting firm specializing in economics, regulatory processes and international trade. Member, North American Group, Trilateral Commission. Former posts: Undersecretary for international business negotiations, Ministry of Economy; leader of bilateral trade negotiations and regional multilateral negotiations; Minister of Trade, Mexican Embassy in Washington, DC, active in the design of NAFTA.

Agustín Carstens

Governor, Banco de México: 2010-present. Former posts: Minister of Finance, 2006-09; deputy managing director, International Monetary Fund, 2003-06; Treasurer and Director General of Economic Research, Banco de México.

Eduardo Fernández García

Private financial consultant. Former posts: President of National Banking Commission, 1994-2000; designed and implemented bank rescue beginning in 1995; legal affairs responsibilities in Banco de México, 1975-1993.

Francisco Gil Díaz

Director General and Executive President, Telefónica Movistar Mexico and Central America; Former posts: Minister of Finance, 2000-06; director general, Avantel; deputy governor, Banco de México; Undersecretary of Revenue, Finance Ministry.

Angel Gurría

Secretary General, Organisation for Economic Co-operation and Development (OECD); Former posts: Minister of Finance; Minister of Foreign Relations; chief debt negotiator, Ministry of Finance; director general, National Foreign Trade Bank; director general Nacional Financiera development bank.

Santiago Levy

Vice-president for Sectors and Knowledge, Inter-American Development Bank. Member, North American Group, Trilateral Commission. Former posts: director general, Mexican Social Security Institute (2000-05);Undersecretary, Ministry of Finance and Public Credit (1994-2000) and main architect of Progresa-Oportunidades program giving incentives for health, nutrition and education for the poor; President, Federal Competition Commission (1993-94); Director, economic deregulation program, Ministry of Trade and Industrial Promotion (1992-93).

Pedro Noyola

Founding partner and executive director, Aklara, a company that designs and implements auctions to generate savings and transparency in the procurement process. Partner, SAI, a consulting firm specializing in trade, antitrust, and financial and operational restructuring. Former posts: Undersecretary of Trade and Foreign Investment; representative of Mexico in NAFTA negotiations and accession to the OECD; Undersecretary of Finance.

Guillermo Ortiz

President, Advisory Council, Banorte Financial Group; former posts: President, Banorte; Governor, Banco de México (1998-2010); Minister of Finance (1994-97); Minister of Transportation and Communication (1994); Executive Director, International Monetary Fund (1984-88).

Andrés Rozental

President, Rozental y Asociados, a consulting firm advising multinational corporations on Latin American strategy. President, ArcelorMittal Mexico. Member, North American Group, Trilateral Commission. Eminent Ambassador of Mexico. Founding president, Consejo Mexicano de Asuntos Internacionales (COMEXI), the independent Mexican Foreign Affairs Council. Former posts: Undersecretary of Foreign Relations, Ambassador to Great Britain.

Jaime Serra Puche

Founder-President, SAI Consultores, consulting firm specialized in economic competition, international trade, investment and dispute resolution. Deputy Chairman, North American Group, Trilateral Commission. Founder, Aklara, and the NAFTA Fund of Mexico. Former posts: Minister of Finance; Minister of Trade and chief negotiator and signer for Mexico of NAFTA; Undersecretary of Finance.

Policy Consultants:

Roberto Newell

Founder and Managing Director, Instituto Mexicano para la Competitividad, an independent applied research center analyzing and proposing policies to improve Mexico's competitiveness globally (2003-11). Undersecretary for Agribusiness, Ministry of Agriculture (SAGARPA-2003); CEO, Trust for Expropriated Sugar Mills (2002); McKinsey & Co., engagements included advising the Mexican government on the privatizations of Telmex and government-owned banks and the creation of the independent power producers regime (1984-2001).

Analysts, Academics, and Policy Advisors:

Carlos Elizondo Mayer-Serra

Professor and researcher, Center for Economic Research and Teaching (2006-present; 1991-2004); independent board member, Petróleos Mexicanos. Former posts: General Director, Center for Economic Research and Teaching (1995-2004); Ambassador of Mexico to the Organisation for Economic Co-operation and Development (2004-06).

Gerardo Esquivel

Professor of Economics, Colegio de México and Universidad Nacional Autónoma de México. Former posts: Consultant, Ministry of Social Development and Ministry of Economy (2007-08); Consultant, Center for Global Development (2007-08); Advisor, Finance Ministry of Mexico City Government (2004-05); Visiting Researcher, International Monetary Fund and Banco de México; Consultant, World Bank, Inter-American Development Bank, Development Associate and Macroeconomics Researcher, Harvard Institute for International Development.

Federico Estévez

Professor of Political Science, Instituto Tecnológico Autónomo de México.

Arnulfo R. Gómez

Professor of International Trade, Universidad Anáhuac. Former posts: Trade Attaché for Mexico in Costa Rica, Nicaragua, Panama, Quebec and Maritime Provinces of Canada; Manager of Free Trade Agreements for BANCOMEXT (Export Bank); International Trade Manager for PriceWaterhouse; Advisor to the president of the Consejo Mexicano de Hombres de Negocios and to the president of the Mexican Business Council of Foreign Trade, Investment and Technology.

Carlos Heredia

Professor and researcher, International Studies Division, Center for Economic Research and Teaching (CIDE); member, North America Group, Trilateral Commission, advisory board, Mexico Institute, Wilson Center, Mexican Foreign Affairs Council (Comexi). Former posts: Economic and International Affairs Advisor to Governor of Michoacán, Lázaro Cárdenas Batel (2003-08); Director General of Metropolitan Services, Mexico City Government (2000-02); Federal Deputy (1997-2000); economist, Ministry of Finance (1982-84, 1986-88).

Tim Heyman

President and Chief Investment Officer, Franklin Templeton Servicios de Asesoría México, an institutional investment management firm; Chairman and Member of the Board, Franklin Templeton Asset Management Mexico, a fund management company. Former posts: founder and president, Heyman y Asociados S.C., an independent institutional asset manager (1985-2013); President of ING Baring Grupo Financiero (México), and of Baring Casa de Bolsa, the first foreign brokerage in Mexico.

David Ibarra

Board member, Grupo Carso and América Móvil; professor of economics, Universidad Nacional Autónoma de México. Former posts: Advisor to Director General of Pemex (1987-94); Minister of Finance (1977-1982); Director General, Nacional Financiera development bank (1974-76); Director, United Nations Economic Commission for Latin America-Mexico (1970-73).

Isaac Katz

Professor of Economics, Instituto Tecnológico Autónomo de Mexico. Former posts: Advisor to economic policy proposals, Economic Studies, Grupo Financiero Bancomer (1999-2001); Advisor, Operadora de Bolsa, Grupo Financiero Serfin (1995-96); Consultant, Instituto Mexicano de Propiedad Industrial (1991); Consultant, Strategic Planning Office, Banco Nacional de México (1990-91); Consultant, International Finance Corporation (1989); Advisor, Director General of Economic and Social Policy, Ministry of Programming and Budget (1983-85).

Manuel Molano

Deputy Director, Instituto Mexicano para la Competitividad (IMCO) and leader of studies on the financial sector, small business, poverty, labor productivity, agriculture, factor allocation, and competitiveness; co-founder of "México, ¿cómo vamos?", an independent benchmarking organization of a plural group of experts in economics and public policy that tracks Mexico's economic performance, sets goals for improving growth and job creation, and coordinates

efforts to maximize the impact of public policy. Former posts: Director General, FICO, a trust controlling 40% of the sugar, alcohol and molasses market (2004-06); Director of Economic Analysis, Ministry of Agriculture (SAGARPA; 2001-04).

Juan Carlos Moreno Brid

Professor of Economics, Universidad Nacional Autónoma de México (UNAM). Former posts: Deputy Director, United Nationas Economic Commission for Latin America and the Caribbean-Mexico (2005-2015);.Regional Advisor, UNECLAC; Research Associate, David Rockefeller Center for Latin American Studies, Harvard University.

Juan Pardinas

Director General, Instituto Mexicano para la Competitividad (IMCO). Former posts: Researcher, Centro de Investigación para el Desarrollo (CIDAC); profesor at Universidad Nacional Autónoma de México, Instituto Tecnológico Autónomo de México and the London School of Economics; correspondent, CNN en Español in India and Japan.

Rogelio Ramírez de la O

Director and sole partner, Ecanal, a private firm that conducts analysis of economic trends and government policy in Mexico and provides forecasts to multinational companies and other businesses operating in Mexico. Former posts: Honorary head of the economic team advising presidential candidate Andrés Manuel López Obrador (2006).

Viridiana Rios

CEO, México ¿Cómo Vamos?, an independent benchmarking organization of a diverse group of experts in economics and public policy that tracks Mexico's economic performance, sets goals for improving growth and job creation, and coordinates efforts to maximize the impact of public policy; fellow at The Wilson Center. Former posts: senior advisor to the Minister of Finance (2013); advisor to the President's Security Spokesperson (2011). Consultant and researcher for: The Guggenheim Foundation, The Center for US-Mexico Studies (UCSD), the Trans-Border Institute, the United Nations, USAID, The World Bank, Mexico's Security Council, and Mexico's Ministry of Social Development.

Luis Rubio

Chairman, Center of Research for Development (CIDAC), an independent research institution focused on economic and public policy issues; Global Fellow, Mexico Institute, Wilson Center; member, North America Group, Trilateral Commission. Former posts: board of directors, Human Rights Commission of Mexico City.

Luis Serra Barragán

Director of Economic Development, Energy and Climate Change, Centro de Investigación para el Desarrollo A.C. (CIDAC). Former posts: Consultant, EGADE Business School (2014); Advisor, MIDE Jalisco (2014); Senior Researcher, CIDAC (2013-14); Advisor, Energy Board of Reforma Group (2014).

**For reasons of brevity, this summary of career highlights omits the regular opinion columns, media contributions and numerous publications produced by most of the individuals interviewed as well as the scores of professional distinctions and prizes bestowed upon many of the persons who participated in this study. Similarly, the academic credentials of the interviewees have been omitted.*

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