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Mexico and Contemplation of NAFTA: Is the Government Abdicating the Rectoria del Estado

Jorge Camil

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I. INTRODUCTION

Rectoría del Estado, or the government's vested right to exercise the stewardship of the economy, was enshrined as a constitutional law principle on February 3, 1983, as a consequence of constitutional amendments enacted during the administration of President Miguel de la Madrid.[1] The process that led to this presidential initiative, however, commenced in 1910, when the thrust of the Mexican Revolution shifted from the democratization of the electoral process[2] to the promotion of government control over natural resources.[3] Most of the Revolution's goals were achieved with the passage of the 1917 Constitution,[4] which imposed the first set of restrictions on foreign investment and claimed direct government ownership over land, waters, petroleum, and other subsurface mineral deposits.[5] The Constitution also has a high social content, reflecting revolutionary ideals that were transformed into a paternalistic protection of the poor and of the legitimate aspirations of the less privileged social classes.[6]

More than fifty years of virtually unopposed political leadership

† "NAFTA" is the North American Free Trade Agreement. *Rectoría del Estado* is a Mexican constitutional law principle which preserves the executive branch's right to exercise the "stewardship of the economy" to insure, among other things, "an integral economic development that will reinforce democracy and the national sovereignty."

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1. CONSTITUCIÓN POLÍTICA DE LOS ESTADOS UNIDOS MEXICANOS [Constitution] arts. 25, 26 (Mex.) [hereinafter CONST.].

2. The original goal of the 1910 Mexican Revolution was to oust Porfirio Díaz, one of the longest reigning dictators in modern times, and to democratize the electoral process. This revolutionary aspiration is still present today in the motto that precedes the signature of every official communication by Mexican public officers: "Effective Suffrage; No Reelection."

3. CONST. art. 27. *See* Jorge Camil, *Mexico's 1989 Foreign Investment Regulations: The Cornerstone of a New Economic Model*, 12 HOUS. J. INT'L L. 1, 5-7 (1989).

4. CONST. art. 25.

5. CONST. art. 27, paras. 1, 4.

6. The Constitution contains, for instance, provisions governing: (a) general principles of labor law; (b) land holdings by rural communities (*ejidos*); (c) protection of public health;

gave the governments that followed the Revolution an apparent birthright to rule the economy in accordance with prevailing administrative policy. Gradually, but persistently, Mexican political administrations claimed a larger role in the economic process.

This Article presents an overview of the concept of *Rectoría del Estado*, from the enactment of the 1917 Constitution until the current administration of President Salinas de Gortari. The Article reviews the oil expropriation of 1938, the Mexican economic "miracle" of 1940-1970, the fiscal and economic crisis of 1970-1982, and the bank nationalization of 1982, in light of the corresponding administrations' willingness to intervene in Mexico's economic life through either regulation or the promotion of legislation. Finally, this Article addresses the modern concept of *Rectoría del Estado*, as it is exercised by the administration of President Salinas de Gortari. This Article concludes that the current administration is more interested in restoring economic growth than in claiming a stronger political and economic foothold through excessive government regulation, protectionism, and exacerbated nationalism.

II. THE 1938 OIL EXPROPRIATION AND THE CONSOLIDATION OF A "REVOLUTIONARY" NATIONALISM: *RECTORÍA DEL ESTADO* AT AN ALL-TIME HIGH

The 1938 oil expropriation was, without a doubt, the first United States encounter with the exercise of *Rectoría del Estado*. Claiming the preservation of Mexico's oil industry, apparently threatened by the failure of the foreign-owned oil companies to comply with a Mexican Supreme Court ruling on a national labor conflict,[7] President Lázaro Cárdenas expropriated the assets of the foreign companies involved in the Mexican oil industry. The exercise of this constitutional right by the first institutional political administration after the Revolution[8] was, in the opinion of authorized sources,[9] an aggravating factor that some believed at the time could have caused a military

and (d) the right to "dignified and decent housing." These provisions do not represent constitutional rights *per se*, but are rather a basis for further legislative or political action.

7. *Decreto que expropia a favor del patrimonio de la nación, los bienes muebles e inmuebles pertenecientes a las compañías petroleras que se negaron a acatar el laudo del 18 de diciembre de 1937, del Grupo Número 7 de la Junta Federal de Conciliación y Arbitraje*, Diario Oficial [D.O.] Mar. 19, 1938 (statement of purposes).

8. Lázaro Cárdenas was the first president after the Revolution to comply with the current constitutional six-year presidential term.

9. *See generally* EDUARDO SUÁREZ, COMENTARIOS Y RECUERDOS (1977). In the opinion of Mr. Eduardo Suárez, Treasury Secretary during the expropriation, President Cárdenas

intervention by the United States.[10]

The success of the oil expropriation, coupled with the birth of a strong domestic oil industry, gave President Cárdenas, and the subsequent administrations, a sense of economic and political pride. This pride has been accurately described as "revolutionary nationalism," because such a bold political decision: (a) reduced Mexico's foreign economic dependence; (b) consolidated the constitution's aspirations to have strong government control over natural resources;[11] (c) gave Mexico a position of leadership in Latin America; and (d) allowed Mexico to start building a strong industrial base.

III. THE MEXICAN ECONOMIC "MIRACLE": DEVELOPMENT WITH PRICE AND MONETARY STABILITY

Mexico faced the post-World War II era with considerable foreign exchange reserves, due to the suspension of imports during the conflict. The resulting economic boom was substantially fueled by an economic model which promoted: (a) the birth of a strong Mexican industry; (b) "import substitution;"[12] (c) "industrial integration;"[13] and (d) development with price and monetary stability.[14] For all its protectionist measures on foreign trade, however, the *Desarrollo Estabilizador*[15] was an economic model that allowed for minimal gov-

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was concerned about the effects of the expropriation and feared an act of force on the part of the United States.

10. *Id.* Mr. Eduardo Suárez, also fearful of United States military intervention, convinced President Cárdenas to send a letter to the United States government through the offices of the Mexican ambassador, Mr. Castillo Nájera. Apparently, the President was ready to resign rather than risk being the cause of a military conflict between Mexico and the United States.

11. *See generally* Camil, *supra* note 3.

12. The policy of "import replacement" was designed to induce local manufacturers to change from "the establishment of plans for the mere assembly or final processing of imported parts or intermediate products," into real manufacturing facilities. HENRY K. WRIGHT, FOREIGN ENTERPRISE IN MEXICO 84 (1971).

13. "Industrial integration" is a term "applied in Mexico to the domestic production of a commodity from domestic raw materials and intermediate products and other Mexican-source supplies." *Id.* at 170.

14. This economic model was predicated on the basis that the government would maintain strict price controls and a fixed foreign exchange rate by committing the Central Bank to exchange unlimited amounts of pesos and dollars at a fixed rate of exchange. This caused great confidence in both Mexican and foreign investors by allowing them to calculate, with a great degree of certainty, the foreign exchange rate factor into their investment equation.

15. A more developed version of this economic model is attributed to Mr. Antonio Ortíz Mena, former Secretary of the Treasury under two Mexican presidents, and former Chairman of the Interamerican Development Bank.

ernment intervention in domestic economic matters; a sort of *laissez faire a la mexicana.*

This period of Mexican economic history spanned almost three decades, between 1945 to 1970, and resulted, among other economic benefits,[16] in the largest flow of direct foreign investment. "The growing restrictions on foreign capital did not deter foreign investors from participating in the Mexican industrial boom[.] Fully protected by tariffs, and stimulated by federal tax concessions and other incentives, foreign investors thrived in the Mexican market."[17]

The critics of *Desarrollo Estabilizador* allege that this economic model resulted in: (a) an inefficient and costly Mexican industry that relied too much on protectionism and government subsidies; (b) a cheap Mexican peso that caused excessive consumer spending and capital flight; and (c) social neglect to the detriment of the lower classes.[18]

IV. THE POLITICAL PENDULUM SWINGS TO THE LEFT: DEVELOPMENT WITH EQUITABLE INCOME DISTRIBUTION

The second foreign encounter with the Mexican concept of *Rectoría del Estado* came with the passage of the Foreign Investment Law in 1973.[19] As a consequence of this legislation, foreign investors were generally precluded from acquiring a controlling interest in Mexican corporations for almost fifteen years following its enactment. "In a major departure from long-standing government policy, the [Echeverría] administration abandoned the economic model based on development with price and monetary stability and embarked on a new policy that emphasized a more equitable income distribution."[20]

The Echeverría administration was engaged, almost from the be-

16. Other recognized benefits of *Desarrollo Estabilizador* were: (a) political stability; (b) the consolidation of a large Mexican industrial base; (c) sustained rates of growth of approximately 6% per annum; and (d) very low inflation rates.

17. Camil, *supra* note 3, at 7-8.

18. *See generally* ROGER D. HANSEN, THE POLITICS OF MEXICAN DEVELOPMENT (1974). President Salinas recently became one of the stern critics of *Desarrollo Establiizador*. *See infra* note 42 and accompanying text.

19. *Ley para Promover la Inversión Mexicana y Regular la Inversión Extranjera*, D.O. Mar. 9, 1973 [hereinafter F.I.L.]. The F.I.L. was passed amidst considerable debate by the investment community and allegations by the United States ambassador that Mexico was changing the "rules of the game." CARLOS TELLO, LA POLÍTICA ECONÓMICA EN MÉXICO 58 (4th ed. 1980).

20. Camil, *supra* note 3, at 8.

ginning, in a frenzy of legislative and regulatory activities apparently aimed at creating an environment in which the new economic benefits could be shared by all Mexican citizens. Consequently, "the government expanded its areas of endeavor, subsidized the price of its goods and services, and evoked the same kind of nationalism that spurred economic growth in the 1940s."[21]

V. THE NATIONALIZATION OF THE BANKING SYSTEM: CÁRDENAS REVISITED?

The fiscal deficit that started during the Echeverría administration[22] was considerably intensified during the subsequent administration of President José López Portillo.[23] Relying on the newly discovered oil, as well as on the excessive liquidity of the international money markets, in 1976 the López Portillo administration commenced a borrowing spree that would increase the foreign debt almost five times over the following six years.[24] Mexico became one of the world's largest debtors amidst economic confusion caused by: (a) the substantial fall in the international oil prices; (b) the ninety billion dollar external debt; (c) the devaluation of the Mexican peso; (d) the nationalization of commercial banks; (e) the mandatory conversion of all domestic dollar deposits into pesos; and (f) the imposition of foreign exchange controls for the first time in modern Mexico.[25]

The President's decision to nationalize the commercial banks was an extreme exercise of *Rectoría del Estado* that polarized domestic public opinion, alienated the domestic investment community, and brought to an abrupt end a dream of economic wealth[26] based on a volatile commodity[27] and an unrealistic growth financed with bor-

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21. *Id.* at 9.

22. The Echeverría administration increased the level of external debt by five times in six years to a total of $20 billion. Moreover, this administration created a welfare state based on government growth, subsidized goods and services, and foreign debt. *See generally* ROSARIO GREEN, ESTADO Y BANCA TRANSNACIONAL EN MÉXICO (1981).

23. Official figures estimated the 1982 aggregate public and private external debt at the end of the López Portillo administration at $87.6 billion. *See* TIMOTHY HEYMAN, INVESTING IN MEXICO 8 (1989).

24. *Id.*

25. *See* Camil, *supra* note 3, at 12.

26. Considering Mexico's vast oil reserves, President López Portillo, early in his administration, warned the Mexican people that they should be prepared to administer their newly-found wealth.

27. The price of Mexican oil fell from $38.50 per barrel in 1981 to $12 per barrel in 1985 and 1986. HEYMAN, *supra* note 23, at 31.

rowed funds.[28]

In the euphoria following the bank nationalization, the official rhetoric made an early attempt to compare President López Portillo's decision with Lázaro Cárdenas's historic expropriation. The substantial differences, however, became apparent almost immediately. The bank nationalization did not affect the interests of the foreign investment community, but did affect Mexican investors holding a controlling interest in the banks. In fact, the nationalization came somehow as a blessing for the international banking community with substantial exposure in Mexico's commercial banks. One of the immediate legal results of the nationalization was that the government became responsible for the nationalized institutions' foreign debt. Moreover, the bank nationalization and the simultaneous imposition of foreign exchange controls[29] were never included in the political platform of the President's own party. They had been a part of the political platform of the leftist parties that obtained, due to President López Portillo's surprising actions, two of their most important goals. In addition, the bank nationalization was not a political exercise of sovereignty to protect the Mexican soil from foreign economic intervention, but, rather, an internal political action that brought to a head-on collision what some regarded as a long-lasting dispute between the public and the private sectors for the control of the Mexican nation.[30]

VI. *Rectoría del Estado* Is Enshrined in the Mexican Constitution

President Miguel de la Madrid, a former constitutional law professor, made his imprint in the Mexican legal system by submitting a congressional initiative to amend the Constitution and include a chapter on economic law.[31] The amendments resulted in the principle of *Rectoría del Estado* and suggested a considerable increase in the powers of the executive branch to:

> . . . insure an integral economic development that will reinforce democracy and the national sovereignty, while promoting growth, employment, and a more equitable income distribution in order to allow the exercise of freedom and dignity of all individuals, groups

28. *See* Heyman, *supra* note 23 and accompanying text.

29. *Decreto que establece el control generalizado de cambios*, D.O. Sept. 1, 1982.

30. *See generally* Rolando Cordera & Carlos Tello, México: La Disputa Por La Nación (2d ed. 1981). Mr. Tello was appointed by President López Portillo as head of the Central Bank in charge of implementing and supervising the bank nationalization.

31. Const. arts. 25, 26.

and social classes protected by the Constitution.[32]

The amendments also explicitly recognized the federal government's responsibility for central planning of the economy and for the execution of development plans.[33] There was considerable unrest among certain opposition parties and the business community, because the amendments suggested a large increase in the powers of the executive branch to intervene in all aspects of the economy.

VII. MEXICO'S ENTRY INTO GATT AND THE 1984 FOREIGN INVESTMENT GUIDELINES: A TREND REVERSAL TOWARDS A FREE MARKET ECONOMY

Notwithstanding the *Rectoría del Estado* constitutional amendments, which suggested an ever-increasing government intervention on economic matters, President de la Madrid "who governed Mexico from 1982 until 1988, [was] largely responsible for the initial thrust to modernize Mexico's economy through the liberalization of foreign trade."[34] Prompted by Mexico's triple digit inflation and a dramatic economic crisis, the de la Madrid administration made an initial effort to liberalize the foreign investment legislation,[35] restructured Mexico's large external debt,[36] and decided to join GATT.[37] President de la Madrid also curbed the apparently uncontrollable inflation by exercising administrative initiative. As a result, the government, the unions, and the private sector signed an "Economic Solidarity Pact" to control wages, prices, import duties, and the rate of exchange.[38]

VIII. THE SALINAS ADMINISTRATION: A NEW STYLE OF *RECTORÍA DEL ESTADO* IN CONTEMPLATION OF NAFTA

In the light of current events, a superficial observer of Mexico's political process could be tempted to conclude that in the Mexico of Carlos Salinas de Gortari, the executive branch is about to abdicate the stewardship of the Mexican economy. The current administration

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32. CONST. art. 25, para. 1.
33. CONST. art. 26.
34. Camil, *supra* note 3, at 12.
35. *See generally* Sandra F. Maviglia, *Mexico's Guidelines for Foreign Investment: The Selective Promotion of Necessary Industries*, 80 AM. J. INT'L. L. 281 (1986).
36. President de la Madrid made "successive debt renegotiations in each year [during his six-year term of office]." HEYMAN, *supra* note 23, at 4.
37. For a thorough analysis of the circumstances surrounding Mexico's entry into GATT, see generally LUIS MALPICA DE LA MADRID, QÚE ES EL GATT? (1st rev. ed. 1988).
38. *See* Camil, *supra* note 3, at 5 nn. 27-29.

has undertaken to: (a) privatize steel, airlines, telephone services, copper mines, and many other smaller, but equally inefficient, industries; (b) reverse the bank nationalization, in order to privatize Mexico's eighteen commercial banks; (c) pass new foreign investment regulations[39] that considerably facilitate the acceptance of majority foreign capital in Mexican corporations; (d) prosecute corrupt labor leaders[40] in unions that were once considered the life-line of the Mexican political system; (e) implement additional deregulation in transportation, telecommunications, petrochemicals, technology transfer, and truck manufacturing; and (f) enact financial legislation that accepts, for the first time in modern times, foreign equity participation in banking, brokerage houses, factoring companies, bonding institutions, and leasing enterprises.[41] In light of the above mentioned actions, it would certainly appear as if the strong Mexican presidential system were in the process of being dismantled, ending the concept of *Rectoría del Estado* less than ten years after it was enshrined as a principle of Mexican constitutional law.

The truth, however, is that the Mexican presidency is alive and well and stronger than ever. Deregulation, privatization, and liberalization are but a part of Mexico's modernization process to meet the challenge of the 1990s. In the words of President Salinas, Mexico "is proud of its past, but has its eyes on the future."[42] Since his inauguration, President Salinas has been committed to reducing the size of the federal government and has favored massive privatization. This dramatic change in policy, however, has not been prompted by a desire to give away presidential power but, rather, seeks to avoid using public funds to subsidize inefficient government companies.[43] "The archaic concept of an all encompassing federal government is being substituted with a new vision of a modern, more efficient state. The eco-

39. *Reglamento de la Ley para Promover la Inversión Mexicana y Regular la Inversión Extranjera*, D.O. May 16, 1989. For a discussion of the implications and importance of these regulations in the Mexican legal system, see Camil, *supra* note 3.

40. In the beginning days of his administration, President Salinas courageously decided to prosecute Mr. Joaquín Hernández Galicia, a.k.a. "La Quina," the all-powerful national leader of the oil workers union.

41. *See* amendments to *Ley General de Organizaciones y Actividades Auxiliares del Crédito* and amendments to *Ley Federal de Instituciones de Fianzas*, D.O. Jan. 3, 1990. *See also* amendments to *Ley del Mercado de Valores*, *Ley de Instituciones de Crédito*, and *Ley para Regular las Agrupaciones Financieras*, D.O. July 18, 1990.

42. President Carlos Salinas de Gortari, Address at the Business Round Table (June 11, 1990), *in* SECRETARÍA DE RELACIONES EXTERIORES, TEXTOS DE POLÍTICA EXTERIOR 39 (1990) [hereinafter Salinas Address].

43. *See* Camil, *supra* note 3, at n.174 and accompanying text.

nomic model adopted by the new administration is predicated upon a federal government concerned with national priorities and not engaged in commercial competition with the private sector."[44]

The president recently recognized that the *Desarrollo Estabilizador,*[45] the economic model that followed World War II, was largely responsible for the fiscal deficit that resulted in Mexico's severe economic crisis in the 1980s.[46] Considering Mexico's great social and economic needs, President Salinas concluded recently that "modernization has ceased to be an option, in order to become an imperative."[47]

Stimulated by the opportunities offered by a North American market, and pressed to expand the democratization of the electoral process, Mexico faces the North American Free Trade Agreement ("NAFTA") with a clear commitment to pursue, among other priorities, the following: (a) the renewal of close ties with the United States; (b) the support and promotion of domestic and foreign private investment; (c) the increase in the level of drug enforcement; (d) the improvement in its record on human rights; and (e) the promotion of stronger environmental protection regulations.

Modernization, however, does not mean a loss of sovereignty. As Mexico's Foreign Secretary has indicated, Mexicans today are watching the most recent events in their country with surprise, but also with enthusiasm. They are willing to assume the responsibilities of the challenge but, above all, they want to continue being Mexicans.[48]

IX. CONCLUSION

The term *Rectoría del Estado* may have been coined by the constitutional amendments initiated by President Miguel de la Madrid, but the concept has been in evolution for the better part of this century as a consequence of an ever-growing intervention exercised by the post-Revolution governments. Virtually unopposed political leadership allowed Mexican presidents to build a strong executive branch that has, to a certain extent, permeated the judicial and legislative

44. *See id.* at 20.
45. *See* Salinas Address, *supra* note 42, at 4-5.
46. *See id.*
47. *See id.* at 5.
48. Fernando Solana (Mexican Foreign Secretary), Address at the celebration of the 180th anniversary of Mexico's Independence (Sept. 16, 1990), *in* SECRETARÍA DE RELACIONES EXTERIORES, TEXTOS DE POLÍTICA EXTERIOR 49 (1990).

branches. Over the past sixty years, Mexican presidents have taken the economy from a revolutionary nationalism to the threshold of NAFTA. The sometimes drastic changes in economic policy have often depended upon the status of the economy, the balance of payments, or the prevailing political sentiment towards foreign investment, and have prompted critics to allege that Mexico is a country which is "reinvented" every six years at the beginning of every political administration. Based on this somewhat unfair allegation, many are concerned about the future of Mexico after Carlos Salinas de Gortari. Will the political pendulum swing back towards a centrally planned economy, strong government intervention, protectionism, and restrictions on foreign trade? This is highly unlikely. The commitments made by President Salinas appear to be irreversible. Under his leadership Mexico has taken the route of modernization because, in the president's own words, "there is no other option." Moreover, if Mexico becomes a part of NAFTA, one of the largest markets in the world, the commitments assumed with the other two participants are not likely to be repudiated by a country that has an impeccable record of fulfilling its international obligations. Although *Rectoría del Estado* may be exercised in the future to fine-tune the Mexican economy in the area of foreign trade, the commitments assumed today will more than likely continue to be honored because they are a part of a modernization process that appears to be, finally, a reality.