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Mexican Economic Performance during the Echeverría Administration: Bad Luck or Poor Planning?

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INTRODUCTION

In his final presidential message, President Echeverría repeatedly referred to the efforts of his administration to improve Mexico's inequitable income distribution. Two other themes stand out in Echeverría's recapitulation of the objectives of his administration. They are the importance he attached to (1) the growth of the public sector to correct deficiencies in the provision of services (such as education, housing, nutrition and health) to the lower income groups and to compensate for shortfalls in private sector investment, and (2) the efforts made to maintain the value of the Mexican peso with respect to the dollar.¹

Mexico's policy objectives under Echeverría may be briefly outlined as follows:²

1. to increase job creation capacity;
2. to maintain the high growth rate industry has shown in the past;
3. to offset through exports of manufactured goods the foreign exchange needed for the expansion of industry;
4. to achieve a more balanced geographical distribution of industry and create new development policies in backward areas;
5. to orient industrial production more strongly towards the needs of the great majority of the population;
6. to reduce industry as dependent on foreign capital and in particular on the service packages it obtains from transnational enterprises, and
7. to develop its own capital goods industry to neutralize capital for the country from cyclical fluctuations in the world economy.

Javier Marquez summarized some dichotomies of the Mexican economic scene during the Echeverría period. These included:³

1. the desire to use fiscal policy to reform the social scene, but then doing this on an inadequate tax base;
 2. the desire to raise exports, but seeking to do this while maintaining a fixed exchange rate in the face of accelerating inflation;
 3. the desire to strengthen public sector enterprises while trying to maintain their prices at unrealistically low rates, and the striving for greater industrial efficiency under a policy of protectionism. Mexico was forced to address these dilemmas when it embarked on its stabilization programme in 1977.
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The following sections attempt to show how these dichotomies in policy-making when combined with several of the longer run structural trends produced the financial and economic crisis of 1976.

PUBLIC SECTOR EXPANSION

The critical destabilizing decision of the Echeverría administration appears to be that of expanding and relying on the public sector as the main vehicle for economic growth and rectifying social inequalities before developing an adequate tax and revenue generating base. Early in his administration, Echeverría made an effort to increase taxes but failed under sharp opposition from the country's commercial banks and the private sector.⁴ His decision to expand public expenditure despite this setback resulted in the overall public sector deficit which had averaged 2.5 per cent of gross domestic product annually between 1965 and 1970, increasing to an average of 5.7 per cent of GDP in the 1971-76 period. By 1976, the deficit was 9.5 per cent of gross domestic product.

Public sector revenue increased but not commensurately with expenditures; the increase in relation to GDP was from 11.3 per cent as an annual average in the mid to late 1960s to 17 per cent in the 1971-76 period.

One of the more interesting facets of the federal budget during the Echeverría years was the role of the so-called decentralized agencies. In the period 1970-76, 65 per cent of total budgeted revenues came from these organizations (as well as enterprises with state participation). The fact that the public sector depended so heavily on the decentralized agencies and enterprises has several implications. These companies were organized by the government in order to promote economic development. That the public sector depended on them so heavily for revenues meant that with very few exceptions (such as the National Railways System and Conasupo) the prices charged for the goods and services produced and sold by these companies had to be economically sound; i.e., they had to cover current costs and provide funds for expansion.

Current expenditures of the public sector increased from an annual average of less than 6.5 per cent of GDP in the mid to late 1960s to more than 17 per cent of GDP in the final two years of the Echeverría period. Public sector investment expenditures increased from an annual average of less than 6 per cent of GDP in the first year of the Echeverría term to more than 12 per cent in the last year. Since private sector gross fixed investment remained fairly constant at 12 to 13 per cent of GDP between 1971 and 1976, gross fixed investment (public plus private) increased to an annual average of 21.3 per cent of GDP (compared with 18.2 per cent from 1965 to 1970). By contrast, public sector savings as a percentage of GDP declined from the annual average of 3.3 per cent during the mid to late 1960s to 2.6 per cent during the Echeverría term in office.

The federal government's budget was such that the balance of current receipts over current expenditures covered 76 per cent of capital expenditures in 1971, but only 24 per cent in 1975. The ratio of current expenditures to current revenue, which had averaged 84 per cent in the 1965-70 period, averaged 90 per cent between 1971 and 1976. Since current revenue tends to be between 97 per cent and more than 99 per cent of total budgetary revenue of the federal

government, this savings decline inevitably resulted in increased federal government deficits to finance investment which was itself growing.

The largest increases in current federal government expenditures in the Echeverría period were for transfers, most of which went to public enterprises. The most important of these under budgetary control are the oil company (PEMEX), the electricity companies, and the railways. Clearly a substantial subsidy element was (and still is) involved in the operations of many of these enterprises resulting in a significant drain on the federal budget.

In fact transfers to these enterprises increased from 2.3 per cent of GDP in the period 1960-68 to 3.4 per cent in 1973-76. The largest subsidies were geared towards: (1) reducing energy prices (oil, fuel and electricity); (2) operating the railroads; and (3) lowering food prices. Subsidies from the central government to public sector enterprises and to the private sector in the form of reduced prices averaged 5.3 per cent of GDP in the 1973-76 period, compared with 3.5 per cent of GDP from 1969-1976.

As a consequence of the spending-savings disparity, the annual borrowing requirement rose from about 3 per cent of GDP in the previous presidential administration to 8 per cent in the final years of the Echeverría period. Of this, more than two-thirds came from internal sources and less than one-third from external sources.

One of the best descriptions of this strategy was given in July 1976 by the Mexican Ministry of Finance and Public Credit.⁵

The policy of public indebtedness which has been followed by the Government of Mexico is based on the desire to expand productive activities and on an effort to improve the standard of living of and offer a more equitable life to a population growing at a considerable rate.

As is the case with most developing countries, internal savings in Mexico are insufficient to meet the levels of investment required. Furthermore, our export derived income does not cover the foreign currency requirements generated by our import needs. The complementary resources (i.e. from international financial markets) are required by our struggle to achieve a rate of capital formation that will enable us to attain a high rate of economic growth and a sustained increase in the levels of our exports.

Between 1971 and 1976 Mexico's federal government budget deficit went from 4.8 billion pesos (1 per cent of GDP) to 57.4 billion pesos (3.8 per cent of GDP); public sector investment (expressed in 1960 prices) more than doubled during that period while private investment increased by only 16 per cent. The number of state-owned corporations expanded from 86 in 1970 to 740 in 1976. By the end of the Echeverría period, public enterprises dominated the oil, electricity, steel, petrochemicals, banking, transportation, and communications industries, with the public sector accounting for around 45 per cent of GDP.

In short the costs associated with Echeverría's budgetary decisions and the emphasis on increasing the public sector were (1) massive budget deficits; (2) considerable crowding out of the private sector from bank credit; (3) rising inflation; (4) a growing internal and external debt; and (5) eventually massive capital flight, reflecting the lack of confidence in government policy.⁶

The decline in private sector confidence was reflected in capital flight

estimated at \$4 billion in the eighteen months preceding the devaluation. From December 1975 to December 1976 the increase in peso liabilities of the banking system was only 10 per cent (less than half the percentage increase of the previous twelve months) whereas liabilities denominated in foreign currencies increased by 72 per cent (more than double the percentage increase in the previous twelve months). Reserve requirements on dollar deposits were 100 per cent compared with about 40 per cent for peso deposits. The disintermediation is apparent from data starting in 1972, but the process accelerated in 1976. The 'dollarization' in 1976 took a quantum leap and reflected the crisis mentality that existed.⁷

BALANCE OF PAYMENTS DETERIORATION

The key elements in Mexico's balance of payments after 1965 were the growing deficit in merchandise trade during the later 1960s and the acceleration of the deficit beginning in 1974. This pattern was certainly associated with Mexico's accumulating inflation (leading to the overvaluation of the peso). Money supply increases (M1, cash plus demand deposits) were also considerably larger in the 1970-76 period than in the late 1960s (19 per cent annually compared with 11 per cent) and clearly much of this demand spilled over into imports.

In addition, the recession in the United States and elsewhere dampened demand for Mexican exports. Still Mexico's total merchandise exports grew by 37 per cent in 1974, but this was offset by the almost 60 per cent increase in imports. Exports did not grow at all in 1975.

The current account deficit averaged 2.4 per cent of GDP between 1965-70 and 3.7 per cent during 1971-76. In the final two years of the Echeverria administration (1975 and 1976), the current account deficits were 5.1 and 4.3 per cent of GDP. This deficit was financed with a growing level of capital imports.⁸

In terms of the composition of exports, one interesting pattern was that of manufactured goods. Over the five-year period 1971-75 manufactured exports grew by 30 per cent per year, of which about 12 per cent per year was attributable to price increases and 16 per cent per year represented real growth.

In relative terms industrial exports were, however, still a small proportion of total manufacturing output compared with a number of the newly industrializing countries, and in a sense even the relatively low aggregate export figures give a somewhat inflated picture of the overall competitive position of the country's industrial exports; i.e., in the early to mid-1970s nearly half of Mexico's manufactured exports came from plants that assembled products for the US market; these were the border industry plants that relied on inputs imported in-bond from the United States, taking advantage of special provisions in the US tariff that limit import duties for such products to value-added outside the United States. About two-thirds of assembly plant exports consisted of items such as electronic parts, television and communications equipment, while clothing was a smaller item.

Exports outside the border areas were considerably more diversified, with non-electrical machinery, electrical machinery and transport equipment exports amounting to \$270 million (25 per cent of non-assembly plant manufactured exports) in 1975. Most of these exports consisted of parts or components—

automobile engines and parts were the most important. Chemical exports (\$204 million in 1975—19 per cent of non-assembly plant manufactured exports) were largely based on natural resources such as sulphur, lead and zinc. These went mostly to the USA and LAFTA countries. Textile exports based on locally produced henequen and cotton, and food product exports led by molasses and simply-preserved fruits and vegetables were also important. In spite of the concentration of exports within a few sectors, however, many sectors were exporting 10 per cent or more of their output in 1974 (the last year for which these comparative data are available). These sectors included basic chemicals, fertilizers and pharmaceuticals—all principally based on natural resources.

Despite some promising signs in the manufacturing area, however, exports from this sector were not sufficient to offset the general erosion of the country's balance of payments position. The rapid deterioration in the balance of payments in the 1970s stemmed from a number of interrelated factors which can be summed up as the exhaustion of the internal sources of finance needed to sustain the pattern of industrialization followed in the 1960s. The deterioration of industrial funds and its counterpart, the growing dependence on foreign financial sources, is reflected in the rapid increase in (1) the industrial trade deficit (as a proportion of manufacturing production); (2) the growing inability of the agricultural, oil and service sectors to generate the external surpluses needed to finance that deficit; and (3) the resulting expansion of the residual deficit which in turn had to be financed by external sources.

As noted in the previous chapter, Mexico's import substitution strategy was based on the premise that the resulting industrial trade deficit was (1) an inevitable side effect of modernization and rapid development; (2) one that was however manageable and likely to be incurred only during the early stages of industrialization; (3) capable of being financed at least initially out of foreign trade surpluses generated by the more traditional sectors such as agriculture; and (4) likely to eventually be turned into a surplus as a result of a declining import ratio and an increasing ability to export.

While import substitution growth did imply notably high annual rates of growth of industrial output (8 per cent on the average over the period 1950-70) without a rapid deterioration of the balance of payments, industrialization continued to be dependent on the importation of capital equipment. As a result, the foreign trade deficit persisted showing no significant tendency to decrease as a proportion of manufacturing output.

DETERIORATION DUE TO IMPORT SUBSTITUTION

Many of Mexico's problems in the 1970s can be traced to increasing difficulties associated with the import substitution strategy initiated in the 1950s. This process is examined in greater detail below in an attempt to throw more light on the overall decline in Mexican economic activity in the early 1970s.

Although the level of tariffs in Mexico is generally low in comparison with other developing countries, quantitative controls account for most of the protection afforded domestic producers from foreign competition. Of the quantitative controls import licences introduced in 1948 are by far the most important. By 1970 around 65 per cent of the value of imports and a similar number of import items were covered by some form of import licencing requirement.⁹

Given the structure of protection, raw materials, intermediate goods and capital goods were fairly easy to import and paid lower import duties. Effective production for manufacturing final consumer goods therefore became higher over time than the nominal tariff protection. The pattern of relative prices created by commercial policy gave producers incentives to gradually shift towards production of consumer goods for the domestic market. Nondurable consumer goods decreased their relative share in total imports while imports of machinery and equipment increased their share from 23 per cent in 1940 to 36 per cent in 1970. The infant industry argument was consistently applied and protection, once imposed, was never removed despite the fact that in principle import licensing could only be granted for periods of three to five years.

Unquestionably, protectionism raised the profit rate in manufacturing. In so doing commercial policy discriminated against other sectors where expansion might have produced higher economic benefits. It seems correct to state that import substitution policies protected final consumer goods (especially those produced by traditional manufacturers, who generally satisfied total domestic demand) more than intermediate or capital goods.

After the initial period of import substitution of nondurable consumer goods and certain intermediate goods in the 1940s and 1950s, industrial development tended to shift in the 1960s to new lines of production such as consumer durable goods. In part the shift toward consumer durables was a response to the demand profile created by an increasingly unequal distribution of income; i.e., while the rapidly growing incomes of the upper income groups created new markets for a variety of new consumer durables, the absence of a broad-based middle income group inhibited the normal pattern of broad-based industrial development experienced by the industrial countries at comparable levels of per capita income. The high levels of capital goods imported required by the new industries tended to counterbalance the reduction in the trade deficit made by their direct contribution to import substitution. Moreover, the new durable consumer goods industries were largely developed by foreign capital. Because many of these companies repatriated profits, they had an additional negative impact of the country's balance of payments. Of course the underdevelopment of a capital goods industry all through this period contributed directly to the growing industrial trade deficit.

The relative underdevelopment of the capital goods sector¹⁰ was critical in affecting the country's trade balance, yet the low observed rates of domestic expansion in this area cannot be explained simply in terms of the rapid expansion in demand for consumer durables and thus the relative attractiveness of investment in these areas. Government policy was also a contributing factor through its (1) establishment of a structure of protection, much more favourable to consumer than to capital goods industries; (2) subsidization of capital goods imports; and (3) maintenance of an overvalued exchange rate. In combination these three factors were largely responsible for the high import ratio and income elasticity characterizing the capital goods sector during this period.¹¹

As a result of these developments, the capital goods sector made a major contribution to the expansion of industrial imports and the trade deficit. This pattern occurred despite an overall decline in the ratio of imports to total supply. Finally in the 1970s, the stage of relatively easy domestic substitution

for industrial imports had been completed. At this point the decline in the import ratio could not be sustained.

This interpretation of the Mexican trade deficit, stressing the pattern of structural change, is consistent with the more orthodox interpretation emphasizing distortions caused by the structure of tariffs and quotas used by the government to promote industrialization as a major factor in Mexican industry's inability to reduce its trade deficit. The orthodox position stresses the excessively high level of protection as a chief contributing factor to inefficiency and thus competitiveness in world markets. Admittedly, industrial exports did grow rapidly after 1965. In fact between 1967 and 1974, a period during which there was an acute deterioration in the balance of payments, the annual rate of growth of manufactured exports increased by 15 per cent. However, most of this increase was from the new border industries and thus did not reflect the overall competitive position of Mexican industry at this time.¹²

CONTRIBUTION OF AGRICULTURE TO THE BALANCE OF PAYMENTS DETERIORATION

Agricultural output increased rapidly in Mexico between 1940 and 1965 due largely to increases in productivity resulting from (1) improved water control methods; (2) land reform; and (3) increased levels of agricultural extension services and agricultural research. During the 1940-65 period, agricultural production expanded at an average annual rate of over 6 per cent per annum in real terms.¹³

In marked contrast output growth subsequently fell to only 1.2 per cent and during the second half of the 1960s agricultural exports mirrored the decline in production. In fact, the country was importing many of its basic grains and oilseeds by 1970. While the causes underlying agriculture's demise are somewhat controversial, three seem to stand out: (1) the decline in public investment in the sector; (2) credit policies; and (3) changes in relative prices.

In particular the reduction in the proportion of public funds budgeted for agricultural investment seems to have played a critical role in agriculture's demise. The share of agriculture in public investment fell from about one-fifth in 1950 to less than one-tenth by 1960, and it was not until the late 1960s when agricultural stagnation was evident that a greater proportion of the government's capital allocations were devoted to the sector. The fall in public investment in agriculture was particularly serious because it appears to have induced a corresponding fall in private investment in the sector. The net result of these trends was a reduction in the share of investment in agriculture in gross fixed capital formation from 14.0 per cent in 1960 to 4.5 per cent in 1970. Significant is the fact that the share of agriculture in value added decreased from 15.9 per cent to 11.6 per cent of the GDP during the same period.

From all accounts the government's diminished role in agriculture was not so much the result of policies that were deliberately discriminatory, but rather simply of circumstances; (1) the expansion of the nationalized sector (with its drain on government funds); (2) a reduction in the income elasticity of tax collection; (3) rigid prices of products supplied by state-owned enterprises (which required more government support); and (4) fixed rates charged by the public utilities necessitating increasing transfer payments from the government.¹⁴

The drain on the government's budget caused by these four factors together with the objective of monetary stability resulted in spending ceilings with agriculture's allocations being determined more and more as a residual after other, more pressing claims had been met.

Probably the factor of next importance in explaining the decline of agriculture is the adverse price effects which producers in the sector faced as a result of the import substitution strategy. Protectionism resulted in an anti-export bias, since export prices were governed by world markets and import substitutes were overpriced compared with world prices. For example in 1970 the effective protection rate of export activities had a minus 5 per cent level, while import substitutes had a plus 39 per cent. The decreasing share of manufactures that were exported is thus not surprising. Price changes due to protectionism contributed to the worsening of relative agricultural prices. Effective protection for agriculture was 1 per cent while for manufacturing it was over 20 per cent.⁶

The decline of agriculture had a number of ramifications. In addition to increasing rural poverty, agriculture's decline also had adverse effects upon the balance of payments. During 1961-65 the agricultural foreign trade surplus financed almost half of the industrial deficit, but by 1974, the deterioration of the sector's trade surplus had reached a point whereby it had ceased to be of any significance. In fact, there is a close correlation between the decline in the agricultural trade balance and the narrowing gap between agricultural production and per capita consumption. While per capita consumption of agricultural goods remained practically unchanged between 1964-65 and 1972-73, per capita production during the same period decreased by 15 per cent.

The decline in per capita agricultural production continued into the 1970s, averaging 12 per cent during 1965-70 and 8 per cent in 1970-75. The effect on agriculture's trade balance at constant prices was also at least as important in the late 1960s as in the early 1970s. However, during the latter period deteriorating terms of trade between agricultural imports and exports brought about a more rapid decline (in current prices) of the trade balance.

Over the 1965-72 period, the effect of the decline in the agricultural surplus was concealed somewhat by the fact that international export prices grew faster than those for imports. Between 1972 and 1975, however, this pattern was reversed, and combined with the continued deterioration in trade balance at constant prices, the surplus in the trade balance measured at current prices was nearly eliminated.¹⁵

OTHER FACTORS RESPONSIBLE FOR THE BALANCE OF PAYMENTS DETERIORATION

The increase in the industrial deficit, together with the erosion of the agricultural surplus, account for a large part of the growing disequilibrium in the trade balance. Other factors contributing to the country's external problems were the slowing down of oil production (up until 1973) to a point where substantial deficits in the oil trade balance began to appear. Finally a number of incentives provided to the service sector did not stimulate development to the point where this sector was able to offset the inability of agriculture to continue its financing of the industrial deficit.

As expected, the growing inability of internal sources to finance the expansion

of industry finally resulted in a rapid increase in foreign debt. Between 1961 and 1965 foreign loans financed only 7 per cent of the industrial deficit; by 1975 this proportion had increased to 66 per cent. As a result net income paid abroad increased from 29 per cent of the deficit on current account in 1960-64 to more than 50 per cent in the 1974-77 period. It appears that the foreign debt was incurred mainly to finance the growing deficits in the current account balance. As noted above, however, these deficits originated with the decline in the trade balance. Current account deficits, therefore, created an equivalent deficit in the balance of net income paid abroad. By the mid-1970s Mexico was falling into a vicious circle whereby the rate of foreign borrowing tended to be determined by the deficits, which were in turn caused at least in part by the very same accumulation of debts.

The failure of industry to generate exports although simultaneously absorbing increased amounts of foreign exchange in the importation of capital and intermediate goods is evidenced by the fact that by 1975 the income arising from the export of manufactures and minerals was not enough even to cover the interest payments on the foreign debt. Between 1960 and 1975 net property income paid abroad as a percentage of manufacturing and mineral exports had doubled.

To summarize, the country's industrialization programme created a set of economic forces tending to cause a deterioration in the trade balance and in the balance of payments on current account. The deterioration became progressively worse in the 1960s and clearly implied the occurrence, sooner or later, of an exchange rate crisis.

While the country's development strategy created an environment conducive to foreign exchange instability, the actual peso crisis of 1976-77 was precipitated by three major factors: (1) the resurgence of domestic inflation; (2) the international economic recession; and (3) finally by a rapid acceleration in capital flight.¹⁶

EFFICIENCY OF POLICY INSTRUMENTS

A survey article on Mexico in the *Economist* contained the following harsh judgment on the Echeverría period:¹⁷

Enter in 1970 President Luis Echeverría, a man whose political instinct far outran his political abilities, whose economic ambitions outran his economics, and whose populism outran his popularity. Exit in 1976 three months after having devalued the peso following 22 years of financial stability, and thereby giving rise to fears for the stability of the whole Mexican system.

In evaluating the Echeverría administration, however, particular attention should be drawn to the fact that a number of developments in the 1960s had made the economy less and less stable and more difficult to manage. The first factor was the growing substitutability between domestic consumption and exports with a major proportion of manufactured goods exported as residuals or surplus (after supplying domestic demand). A similar situation was developing in the mineral and agricultural sectors. The increased potential for substitution of internal for external demand was caused by (1) export diversification into new commodities; and (2) the stagnation of traditional exports such as

sugar, coffee, hard fibres, and minerals. Thus, changes in domestic activity had a significant influence on the current account deficit: (1) imports of capital goods expanded with domestic output; and (2) expanding domestic consumption tended to divert exports towards the home market. Clearly, the more exports became substitutes for domestic goods the greater the chance of external imbalance.

The other factor contributing to instability was the gradual undermining of the effectiveness of monetary policy. All through the 1960s the public sector deficit had fluctuated, with a tendency to increase as a percentage of GDP. Because a part of the deficit had to be financed domestically, a gradual upward trend developed in the central bank's reserve ratio until the usefulness of that instrument was greatly diminished. By 1970 deposit banks in Mexico City which handle half of the financial assets of the country had 50 per cent of their liabilities turned in as reserve requirements while the reserve requirement for banks outside Mexico City was 25 per cent. The overall ratio was 30 per cent for savings banks and 20 per cent for financial banks.

In terms of ominous trends:

1. from 1965 to 1970, public savings decreased from 0.056 to 0.038 as a share of the GDP;
2. public investment on the other hand rose from 0.067 to 0.073 in the same period; and
3. savings in financial institutions increased, also on a share basis from 0.044 to 0.057 of the GDP, with half of these being channelled by the central bank into financing the public sector.

In fact, monetary policy was quite effective all through the 1950s and 1960s in controlling the level and composition (between public and private) of credit. This was a period of general excess demand for funds and thus one where as John Koeler has demonstrated any increase in the availability of funds brought about by the monetary authorities would immediately have been either borrowed or invested.

Although at the beginning of the 1960s monetary policy still was an effective anti-recession instrument, by the end of the decade it had largely lost that capacity (assuming that the rapid expansion of financial assets had eliminated any excess demand for loanable funds).¹⁸ In short the management of macro-economic activity was becoming much more difficult through loss of monetary policy as an effective stabilizing instrument. This occurred simultaneously with a growing incompatibility between internal and external equilibrium.

One can outline the increasing incompatibility between domestic and external equilibrium in terms of the following sequence:

1. an increase in public spending raises aggregate demand and gross domestic product;
2. productive capacity becomes strained, imports increase and exports are reduced by growing domestic demand with the current account deficit expanding;
3. the current account deficit thus expands;
4. prices start increasing more rapidly;

5. to restore control of the balance of payments, the government reduces or slows its expenditures decreasing the GDP growth, thus slowing the upward movement of prices and imports;
6. although the rate of growth of imports decreases, the new absolute level of the current account deficit in the balance of payments either stabilizes or expands at a slower rate;
7. even if exports resume their expansion after the stabilization of aggregate demand, they may only prevent the deficit from getting bigger, because an enlarged absolute deficit is necessary to support the higher level of output.

Thus the structure of the system was such that monetary policy, so successful as a stabilizing tool in the 1950s and 1960s, had little power to offset these trends developing towards the early 1970s. As Solis had noted:¹⁹

. . . from this perspective it becomes clear how damaging the 1964 failure of tax reform was, not only because it failed to add a new instrument to the arsenal of policy tools, but also because it accentuated conditions that would eventually cancel the flexibility of reserve requirements, the most powerful existing instrument.

CONCLUSIONS

In retrospect it seems clear that in order to evaluate fairly the Echeverría government's attempts to make development less unequal, one must understand that the tendencies toward inequality, balance of payments disequilibrium, and slowing down of agricultural growth, among others, were in many ways a logical result of the policies followed in the postwar industrialization period. One should not start in 1970 but much earlier. At the same time, the political elements which gave rise to or even forced some key decisions during the period under discussion can be ignored only at serious risk. Finally, much more empirical work is needed on the short-term dynamics of the Mexican economy to prove fully the assertion that government investment displaced private investment activity.

On the other hand the fact remains that most of the Echeverría administration's objectives were not met. If anything, income distribution became more unequal between 1970 and 1976. In this regard, therefore, the Echeverría policy of shared development (*desarrollo compartido*) was no more successful than the policies of his predecessors. The declining trend in agricultural production was not reversed, nor was the import substitution strategy of industrial development with its inherent subsidization of industry at the expense of other sectors fundamentally altered under Echeverría.

Job creation was no more adequate under Echeverría than it was during the 1960s and indeed the problem probably worsened because of the lower rates of economic growth combined with demographic trends of the previous two decades. One accomplishment of the Echeverría scenario, perhaps the one that will have the greatest long-term consequences, was the institution of a population programme. Except in the last days of the administration, there was no attempt to change significantly the land tenure pattern.

In retrospect it appears the economic strategy adopted in the early 1970s

responded to a number of urgent political rather than economic concerns. Mexican leaders have some grounds for their belief that by preserving their established political system, they are enhancing the country's long-term capacity for effective economic management and the promotion of development. In this light Echeverría's economic strategy is best evaluated not as a mere product of arbitrary and irresponsible personal leadership, but as a reasonable rational attempt to reinvigorate that political system, accepting a certain loss of short-term economic equilibrium as the price. Clearly, the short-term economic consequences were far more extensive than anticipated.

NOTES

1. Sidney Weintraub, 'Case Study of Stabilization: Mexico', in William Cline and Sidney Weintraub (eds.) (1981), *Economic Stabilization in Developing Countries*, Brookings Institution (Washington), pp. 272-5.
2. Robert Looney (1978), *Mexico's Economy: A Policy Analysis with Forecasts to 1990*, Westview Press (Boulder, Colorado), Ch. 5.
3. Javier Marquez (1977), 'La Economía Mexicana en 1977 y su Futuro', Madrid, 25 October (mimeo).
4. A fascinating inside account of this episode is provided in Leopoldo Solís (1981), *Economic Policy Reform in Mexico*, Pergamon Press (Elmsford, New York), Ch. 3.
5. Quoted in Carlos Vidali Carbajal (1976), 'Política Tributaria', in *Política Hecendaria y Financiera en Mexico, 1971-1976*, Suplemento de Comercio Exterior (August), pp. 24-5.
6. Cf. Robert Looney (1981), 'Mexico's Fiscal Crisis: A Critique of the Fitzgerald Thesis', paper presented at the Eighth Annual Eastern Economic Association Meetings, 28 April, Philadelphia, Pennsylvania, pp. 7-9.
7. Leroy Laney (1981), 'Currency Substitution: The Mexican Case', *Voice of the Federal Reserve Bank of Dallas* (January), pp. 1-10, gives an excellent analysis of this process.
8. Weintraub (1981), pp. 281-3.
9. A detailed account of industrial policy during this period is given in The World Bank (1979), *Mexico: Manufacturing Sector—Situation, Prospects and Policies*, IBRD (Washington). The following section draws heavily on this report.
10. The long-term problems caused by the underdevelopment of the capital goods sector are documented in L. Solís (1978), 'Industrial Priorities in Mexico', in United Nations Industrial Development Organization, *Industrial Priorities in Developing Countries*, United Nations (New York), pp. 106-7. See also Adriaan ten Kate and Robert Bruce Wallace (1980), *Protection and Economic Development in Mexico*, St. Martin's Press (New York), Ch. 3.
11. Adriaan ten Kate and Robert Wallace (1980), pp. 118-19.
12. Centro de Investigacion y Docencia Economicas (1980), 'The Mexican Economy: Recent Development and Future Prospects', *Cambridge Journal of Economics* (June), pp. 178-9.
13. Eduardo Venezian and William Gamble (1969), *The Agricultural Development of Mexico*, Praeger Publishers (New York), pp. 63-4.
14. Solís (1981), *Economic Policy Reform in Mexico*, pp. 12-13.
15. Centro de Investigacion y Docencia Economicas, op. cit., p. 180.
16. Cf. Robert Looney, *Mexico's Economy*, op. cit., Ch. 8 for a detailed account of the events immediately prior to the devaluation.
17. David Gordon (1978), 'Mexico: A Survey', *The Economist* (22 April), p. 18.
18. The mechanism originally identified in John Koehler (1968), *Economic Policy Making with Limited Information: The Process of Macro-Control in Mexico*, Rand Corporation (Santa Monica).
19. L. Solís, *Economic Policy Reforms in Mexico*, op. cit., p. 34.