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1 Introduction

The purpose of this work is to critically examine macroeconomic policy in Mexico from 1958 to 1986. This period is of special interest as it embodies two distinct, sharply contrasting phases. Between 1958 and 1972, the inflation rate never exceeded 6 percent, while annual output growth averaged 6.7 percent. The period since 1972, by contrast, has been marked by a succession of increasingly severe macroeconomic crises. Figures 1.1–1.3 depict how

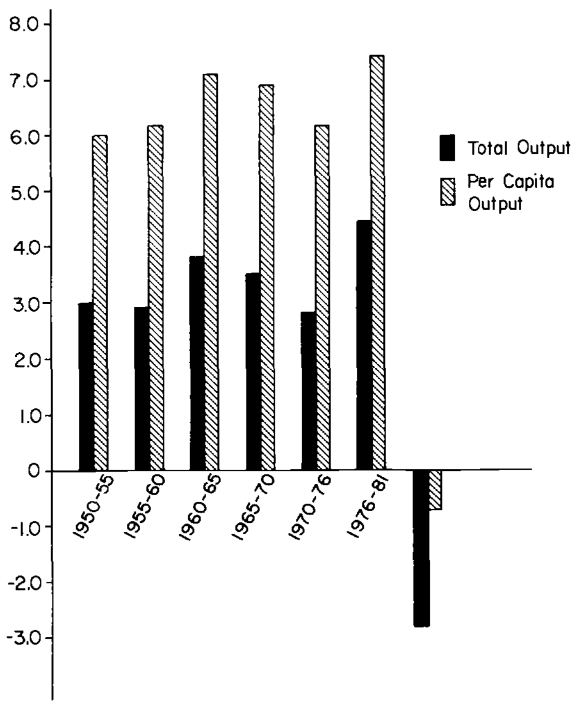

Fig. 1.1 Growth rates of total and per capita real output, 1950–86
Source: Raw data are from *Indicadores Economicos* (Bank of Mexico).

real output, the foreign debt, and inflation have fluctuated. Inflation and the foreign debt began rising rapidly after 1972. During the Echeverría administration the foreign debt increased fourfold to reach $28 billion, and in the last quarter of 1976 a major balance of payments crisis erupted. Just six years later and notwithstanding an enormous increase in oil revenues, the foreign debt had climbed to $88 billion and the country found itself in the grips of a much more threatening crisis: in 1982 the inflation rate jumped to 98 percent, the fiscal deficit was an astounding 17.6 percent of GDP, and neither the public nor the private sector was capable of meeting its scheduled debt service payments.

The adjustment following the 1982 crisis has been and continues to be traumatic. In a country that experienced continuously positive growth from 1933 to 1981, real per capita income has fallen 13.4 percent (as of 1986) and real wages have declined to levels not seen since the early sixties. At the end of 1986, inflation was running well over 100 percent, the investment rate

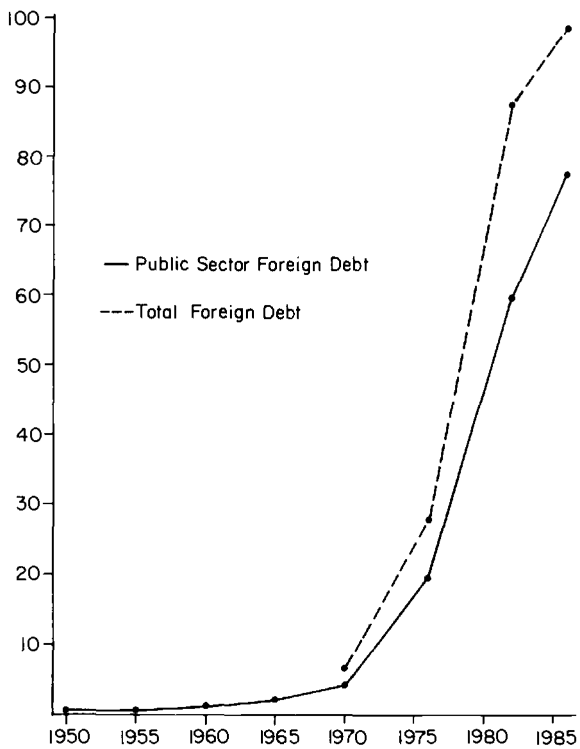

Fig. 1.2 Total foreign debt and public sector foreign debt (billion $)
Source: Raw data are from *Perspectivas Economicas de Mexico* (CIEMEX-WHARTON), various issues.

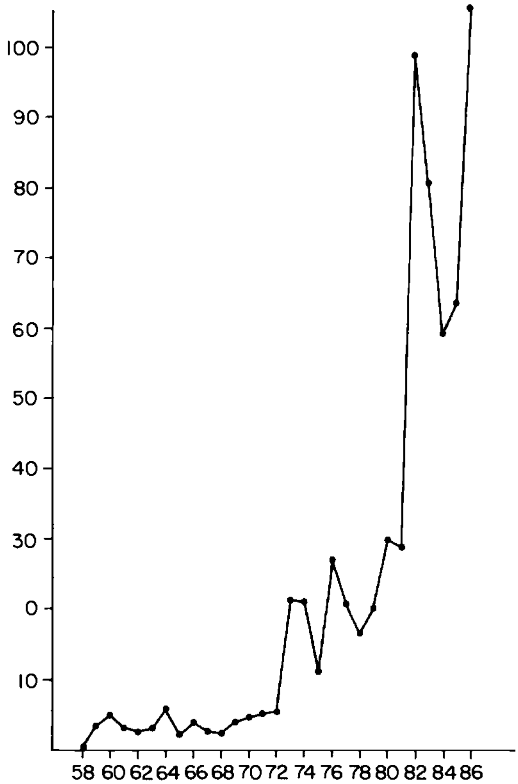

Fig. 1.3 The domestic inflation rate, 1958–86
Source: Raw data are from *Indicadores Economicos* (Bank of Mexico).

was at an historical low, and the foreign debt was $10 billion larger than in 1982. Relations with foreign creditors remain tense; to date there have been three major debt reschedulings.

In chapters 2 through 5 I analyze economic performance during the era of Stabilizing Development and the Echeverría, Lopez Portillo, and De La Madrid administrations. These chapters explore various aspects of recent macroeconomic history. They track the evolution of economic policy and the major macroeconomic variables of interest such as real wages, the foreign debt, capital flight, the fiscal deficit (broken down according to the deficits of the parastatal sector, of financial intermediaries, and of the rest of the government), and different measures of financial intermediation.

In the next two chapters I develop formal economic models in an attempt to gain some insight into the factors responsible for the dismal post-1982 record of falling per capita incomes, low real wages, high inflation, and widespread underemployment. Chapter 6 is an analysis of the repercussions of import compression on real wages and underemployment, while in chapter 7 I investigate the links between capital accumulation, inflation, fiscal deficits, and financial intermediation.

Chapter 8 covers various topics relating to the evolution of the foreign debt, with a detailed discussion of the different debt reschedulings undertaken since 1982 and institutional aspects of the debt management process. The final chapter briefly examines the economy's future prospects and summarizes the main policy implications of the study.

2 The Record of Stabilizing Development

After the devaluation of the peso in 1954, the Mexican economy entered a phase of high growth and low inflation that would last until the end of the sixties. This period has since come to be known as the era of Stabilizing Development (SD). Though it is difficult to pinpoint its exact starting date, there is general agreement that the SD period covered at least the years 1958–70; that is, mainly the administrations of Presidents Adolfo López Mateos (1959–64) and Gustavo Díaz Ordaz (1965–70).

As stated by the then Minister of Finance, Antonio Ortíz Mena, the main objectives of economic policy during SD were to increase private sector savings and capital accumulation, maintain price stability and a fixed parity with the dollar, and increase real wages (Ortíz Mena 1970). These goals were largely achieved (tables 2.1a and 2.1b), leading observers to speak of a "Mexican miracle." The exchange rate was kept fixed at 12.5 pesos per dollar, and the annual inflation rate averaged 3.8 percent. Real output grew at an average rate of 6.7 percent, and the share of gross fixed investment in GDP rose (at 1960 prices) from 16.2 to 20.8 percent. The real industrial sector wage inclusive of fringe benefits grew at an annual average rate of roughly 4 percent. Workers in the urban informal and agricultural sectors also appear to have experienced large real wage gains. (The data bearing on real wages in the latter two sectors will be discussed in section 2.3.2.)

In the next two sections I discuss in detail the macroeconomic, trade, and industrial policies that constituted the SD program.[1] Section 2.3 is a critical examination of the conventional view that the SD strategy was responsible for a severe worsening in underemployment and the distribution of income and that by 1970 it could no longer deliver sustainable, high rates of growth.