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GRADUATE COLLEGE

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BY

JOHN ORSON WARD

Norman, Oklahoma

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AN ANALYTICAL BASIS FOR EVALUATING
MEXICO'S PARTICIPATION IN LAFTA

APPROVED BY

Jim E Reese

Wm d Woodhead

J. L. Robinson

W R Beach

Ed J Price Jr

DISSERTATION COMMITTEE

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TABLE OF CONTENTS

Page

LIST OF TABLES . . . . . .

Chapter

I. AN ANALYTICAL BASIS FOR EVALUATING MEXICO'S PARTICIPATION IN LAFTA 1

The Characteristics of "Inward" Industrialization
The Characteristics of "Outward" Industrialization
Integration as a Tool of National Industrialization
An Analytical Basis for Evaluating Mexico's Participation in LAFTA: A Summary Statement

II. THE INDUSTRIALIZATION OF MEXICO: NEEDS AND PERFORMANCE 34

The Needs for Industrialization in Mexico

III. MEXICO'S "INWARD" INDUSTRIALIZATION: RESTRAINTS TO FUTURE GROWTH. . . . 98

The Income Elasticity of Demand for Industry in Mexico
Industrial Costs, Prices, and Utilization of Industrial Capacity
Income Distribution and Regional Dualism in Mexico
The Import Substitution Process in Mexico
Conclusions

Chapter		Page
IV.	THE CONTRIBUTION OF THE EXTERNAL SECTOR TO MEXICO'S DEVELOPMENT AND INDUSTRIALIZATION	146
	Import Needs, "Outward" Industrialization, and Export Performance	
	"Outward" Industrialization: The Promotion of Manufactured Exports in Mexico	
	Final Remarks	
V.	LAFTA AS A TOOL OF NATIONAL INDUSTRIALIZATION: THE MEXICAN EXPERIENCE	259
	Mexico and Latin American Integration: The Benefits and Costs of Participation	264
	The Restructuring of LAFTA's Mechanisms of Trade Liberalization.	
VI.	CONCLUSIONS	321
BIBLIOGRAPHY		327

LIST OF TABLES

Table		Page
1.	Commerce of LAFTA, 1960-1968 (Millions of U. S. Dollars)	25
2.	LAFTA's Intra-Regional Trade and Commercial Balances (Millions of U. S. Dollars)	26
3.	National Account and Population Statistics for Latin America - 1968.	37
4.	Mexico's Population Growth in Selected Major Urban Areas (Thousands of Persons)	39
5.	Mexico's Demographic Growth (Thousands of Persons).	40
6.	Mexico's Economically Active Population by Field of Activity (Thousand of Persons)	47
7.	Mexico's Urban Population Changes and Urban Employment	50
8.	Growth of Agricultural Output for LAFTA Members	55
9.	Mineral Production for the Major Mineral Producing Countries of Latin America (Petroleum excluded, 1963 prices). . . .	57
10.	The Stimulus of Latin American Industry to Development (1950 Prices).	60

Table		Page
11.	Growth of GDP Per Capita for Latin America (Constant 1960 prices)	62
12.	Mexico's Economic Development Since 1940 (In Billions of Pesos)	65
13.	Structural Changes among Selected Mexican Industries (Percentages based on Constant Pesos)	67
14.	United States' Direct Investment in Latin America, 1963-1968 (Current U. S. Prices)	77
15.	Mexico's Economic Growth: 1963-1968 (Current Prices Billions of Pesos) . . .	86
16.	Growth Rates of Inputs, Outputs, and Productivity in Selected Latin American Countries	90
17.	Mexican Gross Domestic Product by Sector (Billions of Pesos, 1950 Prices).	99
18.	Mexico's Industrial Coefficient	101
19.	Distribution of Monthly Income by Family for Selected States of Mexico (Pesos) . .	121
20.	The Growth of Per Capita Incomes for the Federal District and the Provinces of Mexico (Millions of Pesos, 1960 Prices)	123
21.	Mexico's Distribution of Income 1963-1964	125
22.	The Composition of Mexico's Imports by Groups of Products 1940-1967 (Group Imports as a Percentage of Total Imports)	134

Table		Page
23.	Estimates of Mexican Import Coefficients for Manufacturing (Current Pesos) . . .	139
24.	The Income Elasticity of Demand for Imports and the Prospensity to Export of Argentina, Brazil, Mexico (Percentage changes are based on Current Dollar)	154
25.	Mexico's Declining Share of World Exports (Exports, FOB, in millions of U. S. Dollars)	157
26.	Mexico's Balances of Payments, 1963-1969 (Millions of Pesos, Current Prices). . .	161
27.	Latin America's Long-Term Capital Inflows and Investment Income Outflows for the Period 1961-1968 (Millions of Dollars, Current Prices).	167
28.	Direct Foreign Investment and Remittances in Mexico (Millions of Pesos, Current Prices)	170
29.	Principal Commodity Exports for Selected Latin American Countries for 1968 (Millions of Dollars, Current Prices) . .	174
30.	The Direction of Mexico's Trade in 1968 (Millions of Pesos)	177
31.	The Price Statility of Major Mexican Commodity exports (1963 = 100)	183
32.	The Comparative Price Stability of Mexico's Exports (1958 = 100)	188
33.	Projected 1970 Income Elasticities of demand for Selected Primary Products .	194

Table		Page
34.	The Reliability of Terms of Trade Indices--Argentina (1958 = 100)	217
35.	Regional Commodity Terms of Trade (TOT) and Income Terms of Trade (TOT) (Base 1963 = 100).	219
36.	The Commodity Terms of Trade and Income Terms of Trade for Mexico and Selected Latin American Countries (1958 = 100) .	220
37.	Manufactured Goods in Mexico's World Trade (Thousands of Pesos)	236
38.	Value of Exported Manufactured Products in 1967 by NABALAC Section and by Percentages of Total Trade for Latin America and the Rest of the World. . . .	253
39.	The Composition of LAFTA Trade in Negotiated Products by Country for the Period 1962-1967 (Thousands of Dollars	269
40.	LAFTA Trade in Manufactured Products - 1967 (Thousands of U. S. Dollars). . . .	275
41.	The Composition of Mexico's Exports to LAFTA Members in 1968 (Thousands of Pesos)	278
42.	The Commercial Balance of Mexico with the Countries of LAFTA (Thousands of Pesos, Current Prices)	292
43.	Mexico's Trade in LAFTA in 1969 by Country (Thousands of Pesos)	294
44.	The Short-Run Costs and Benefits of Mexico's Participation in LAFTA in 1968 (Thousands of Pesos).	298

CHAPTER I

AN ANALYTICAL BASIS FOR EVALUATING MEXICO'S PARTICIPATION IN LAFTA

Economic integration schemes among less-developed countries have essentially evolved out of the inability of traditional tools of industrialization to generate a satisfactory rate or structuring of national industrialization for those countries. As Sidney Dell cites, "The case for a common market in Latin America, as in any underdeveloped region, is that future economic growth presupposes a large amount of industrial development and that such development would be facilitated if the barriers to trade within the region could be reduced or eliminated."[1] It was this desire to institute an alternative regional tool of industrialization which prompted the founding of the Latin American Free Trade Association (LAFTA) by the Treaty of Montevideo in 1960.

Mexico's decision to join LAFTA in 1960 was also predicated on the desire of Mexico's development planners to gain access to an

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[1]Sidney Dell, A Latin American Common Market? (London: Oxford University Press, 1966), p. 18.

alternative tool of industrialization. A development planner in a country such as Mexico must be aware of the various development needs of his country. He must also be aware of the various development "tools" he can use to satisfy those development needs. The greater the number of tools that a development planner has available for his use, the greater will be the chance that he can satisfy the development needs of his country with the least cost and friction.

The topics of concern in this paper are Mexico's development needs with respect to industrialization, and those tools that the Mexican planner can employ to satisfy Mexico's industrial needs. These various tools, which can be generally characterized as being either "inward" or "outward" tools of industrialization, have their own characteristics. The fact that a specific tool has provided a satisfactory solution to any one development problem in no way implies that such a tool will prove a satisfactory solution to any other development problem. Moreover, each tool generates its own particular costs and each tool has its own particular restraints.

Mexico's participation in LAFTA is one of those tools of industrialization referred to above. But the Mexican planner has in many cases used this tool of industrialization without fully understanding the implications of its use and the advantages or disadvantages that it offer over alternative tools of industrialization. Daniel M. Schydlowsky, in discussing the use of integration as a tool of

industrialization, has observed that,

> . . . it is necessary for each country to have a national policy for regional economic integration. Such policies in most cases exist only in the weakest explicit form and the process of policy forming is often almost a random one in which concrete information and rational evaluation of alternatives have a minimal part.[2]

Before the objectives of this paper are stated, it would be best to briefly discuss some of the general characteristics of the various tools of industrialization available to the Mexican and Latin American development planner.

The Characteristics of "Inward" Industrialization

"Inward" industrialization in the simplest terms means the promotion of national industrialization solely within the framework of a country's domestic market. This might be done through the pursuance of import substitution (IS) or through the use of any tools (i. e., subsidies, tax incentives, etc.) directed at promoting the expansion of domestic industries via their sales to the domestic market.

Until the early 1930's the development policies of the various Latin American nations, in most cases, were not industrially oriented, in that development essentially revolved around the earnings of traditional exports for satisfying domestic and infrastructure needs for

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[2]Daniel M. Schydlowsky, "Analytical Basis for a National Policy on Regional Economic Integration in Latin America," Journal of Common Market Studies, Vol. VI, No. 2 (December, 1967), p. 179.

manufactured goods through imports. It is estimated that in 1929 twenty-five per cent of the goods consumed in Latin America were imported.[3] Domestic industry was usually promoted by a spontaneous substitution of domestic production for imports due to domestic cost advantages for such products as foodstuffs, beverages, textiles, clothing, and cement. Industry also developed around the secondary processing of primary products for export. Industrial growth was, however, rather limited to the above light industries.

The Latin American nations began more actively to turn to "inward" means of development in the early 1930's due to the decline in their export earnings resulting from the depression. To satisfy a growing demand for manufactured goods it was necessary to promote domestic manufacturing of these goods through protective tariffs and quantitative restrictions on imports. During World War II, while export earnings were high, the foreign supply of manufactured goods was curtailed, thus stimulating domestic industry through a spontaneous import-substitution with active government support. Those industries generated during this period continued to largely consist of nondurable consumer goods industries with the beginnings of basic industries (steel, chemicals, etc.) emerging in the larger countries of

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[3] United Nations (U. N.), Economic Commission for Latin America, The Process of Industrial Development in Latin America (E/CN. 12/716/Rev. 1), 1966, p. 21.

Latin America.

In the period between the Second World War and the end of the Korean conflict, export earnings continued to grow steadily, but the demand for imports generally grew at a faster rate, pressing hard the ability of these countries to finance such imports--the capacity to import. During this period forced import substitution was extensively used in the areas of non-durable consumer goods, basic industry, and in some durable consumer goods to reduce import needs and take pressure off their export sectors which continued to be oriented toward primary product exports. This active IS was also necessary to provide employment for a rapidly growing urban population.

In the manner outlined above domestic industry generated by "inward" tools assumed a much larger role in the development of the Latin American nations. To many, industrialization became synonymous with development. Import substitution, which was initally necessitated because of either a lack of supply of manufactured imports or the inability of export earnings and domestic supply to keep pace with the growing demand for manufactured goods, increasingly became viewed as a tool of industrialization in its own right. Imports as a percentage of total consumption for the region fell from twenty-five per cent in 1929 to an estimated ten per cent in 1960.[4] It is estimated

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[4] Ibid., p. 21.

that for Argentina, Brazil, Chile, Colombia, and Mexico import substitution generated thirty-six per cent of total industry from 1929 to 1960.[5]

During the early part of the 1960's the general policy of industrialization for Latin America continued to revolve around the expansion of domestic demand for manufactures and import substitution, with a heavy reliance on export earning from traditional export sectors to provide needed inputs of imported capital and raw materials to the newly created domestic industries.

Using the Latin American experience, several observations can be made concerning the general characteristics of these "inward" tools of industrialization.

The import substitution process stems from: (1) the need to accelerate industrialization and (2) the necessity to reduce import needs because of the inability of the external sector to sufficiently expand the capacity to import. IS at any point in time is due to autonomous action, i.e., independent of the evolution of internal demand. IS can be either spontaneous or forces. IS is spontaneous if it is prompted by cost advantages or an externally caused contraction in the supply of imports. IS is forced if it is prompted by artificial cost advantages created by government intervention in the form

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[5]Ibid., p. 26.

of import tariffs or quantitative restrictions. While IS is at any one time independent of the evolution of internal demand, the dynamic growth of IS of course is a function of the growth of internal demand. As new imports are necessitated by changes in the pattern of consumer demand and the IS process itself, assuming domestic production does not completely satisfy that demand, new areas of possible IS are created.

The two factors physically limiting the degree to which IS can be used are the size of the import coefficient, i.e., imports divided by consumption, and the types of industries for which sufficient import coefficients exist.

The import coefficient for Latin America is approximately thirteen per cent. This would appear to be a rather small margin for the future use of IS. For several countries of the region (Chile, Argentina, and Uruguay) import coefficients have already reached such a low level that further IS will be insignificant.[6] Assuming that the IS process can be extended till the import coefficient reaches perhaps six per cent, based upon import coefficients for developed countries, it does not appear that IS will be able to generate the kind of stimulus to industrialization as it has in the past.

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[6] Organization of American States, (OAS), The Alliance for Progress and Latin American Development Prospects: A Five Year Review, 1961-1965 (Baltimore: Johns Hopkins Press for the OAS, 1967), p. 33.

The second factor physically limiting the use of IS is the type of industry for which satisfactory import coefficients remain. To cite Raul Prebisch:

> The stage of easy substitution is past. It was relatively simple to substitute domestic production for imports of individual items of current consumption and of some durable consumer and capital goods, and there is little margin left for substitution in this field in most of Latin America. We are now moving into the stage of import substitution in respect of intermediate products of durable consumer or capital goods, which, besides being difficult to manufacture, require markets much larger than those of the individual Latin American countries.[7]

In such industries as metal transforming, where sixty per cent of the regions consumption consists of imports, IS is limited by both the national market size, and the technology required to institute such industries.[8] As an autonomous stimulus to industrialization, IS would appear to have a limited future use for some Latin American countries.

For most of the Latin American countries, there also exist structural restraints to the expansion of domestic demand, in the form of regressive patterns of income distribution and regional dualism.

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[7] United Nations, Economic Commission for Latin America, Towards a Dynamic Development Policy for Latin America (E/CN. 12/680), 1963, p. 69.

[8] U. N., The Process of Industrial Development in Latin America, p. 110.

The ECLA cites that:

> The share of total private consumption in the Latin American countries absorbed by expenditure on foodstuffs--is so large that in several instances it exceeds one-half and in no case falls below one-third. . . . Manufactured goods other than food account for rather small proportions of total consumption, ranging from about 25 per cent to a little over 35 per cent in those countries of the region where per capita income is highest. These characteristics of demand for consumer manufactures are determined not only by each country's average per capita income, but also by its income distribution patterns. [9]

In the case of Mexico where 51.2 per cent of private consumption expenditures are for food[10] and fifty per cent of the families of Mexico receive only 15.4 per cent of national personal income,[11] this restriction can be severe.

Latin America is also a region abounding in national dualistic situations, inter alia, the North-South problems of Brazil and Mexico and the coast-interior problems of Peru and Colombia. Whole regions of extreme poverty such as exist in the north of Brazil, the south of Mexico, and the interiors of Peru and Colombia, often create conditions in their interaction with more developed regions of the nation that serve to perpetuate their stagnation via Gunnar Myrdal's process

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[9] Ibid., p. 122.

[10] Ibid., p. 121.

[11] United Nations, Economic Commission For Latin America, "Income Distribution in Latin America," Economic Bulletin For Latin America, XII, No. 2, 1968, pp. 38-44.

of circular causation. In Mexico average family incomes in the northern states range from two to three times greater than average family incomes of the states in the south. [12]

It is quite probable that with such structural deficiencies of demand, the expansion of durable consumer and capital goods industries, which require large markets for efficient production, will be unfavorably affected.

To this point the discussion of the characteristics of "inward" tools of industrialization has centered around those factors delimiting their use in a physical sense. A case can also be constructed for limiting the use of IS and other "inward" policies of industrialization on the basis of the costs generated by the use of these tools. The cost of import substitution is not only to be measured by the marginal price differences between imported goods and IS promoted domestic goods. The promotion of IS and domestic production behind protective tariff walls also creates what has been referred to by the United Nations as, " . . . markets . . . too small to sustain efficient, large-scale methods of production, so that import substitution creates a vicious circle of small markets enforcing production at high

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[12] William O. Freithaler, Mexico's Foreign Trade and Economic Development (New York: Frederick A. Praeger [illegible], 1968), p. 22.

cost."[13] This observation was born out by a 1962 Economic Commission on Latin America (ECLA) study which showed that prices of manufactured goods in Latin America were significantly higher than those in the United States in real terms, i. e., adjusted for disparities in official exchange rates. The only exception occurred in beverages and some pharmaceuticals. The greatest difference in prices was found in capital goods, which were in some cases four times higher in Latin America than in the United States.[14] The injudicious use of IS and other "inward" oriented tools for the promotion of domestic industry (i. e., subsidies, credit, etc.) can create industries incapable of attaining the minimum scales for efficient production, backward and forward intra-industry linkages then only serve to transmit pecuniary diseconomies in the form of high cost and often inferior goods to other national industries.

Not only does the excessive use of "inward" industrialization often result in industries operating at too small a scale to realize size economies, but a rapid expansion of capacity in an industry due to IS often results in that industry operating at undercapacity once

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[13]United Nations, Industrial Development Organization, "The Need for an Export-Oriented Pattern of Industrialization, Industrialization and Productivity, No. 14, 1969, p. 27.

[14]U. N., The Process of Industrial Development in Latin America, p. 129.

that IS margin is expended. The ECLA has reported that capital usage in Latin American industries averaged between forty per cent to eighty-two per cent for the period 1961 to 1964.[15] In summary, it would appear that past success with "inward" industrialization will be difficult to duplicate in Latin America in the future.

The Characteristics of "Outward" Industrialization

"Outward" industrialization refers to promotion of domestic industry through the expansion of manufactured exports either to a particular region or to the world in general. With respect to the future use of "outward" industrialization in Latin America, the Organization of American States (OAS) has observed that,

> For many developing countries, the failure to rapidly establish export-oriented manufacturing industries as a major sector may jeopardize their more general aspirations for a dynamic industrial sector. An improved balance of payments requires policies directed towards a rapid increase in the export of manufactures. The export of manufactures should be an explicit policy objective in the over-all development and industrial plans of developing countries.[16]

The position of the OAS is predicated on the supposed advantages that "outward" industrialization offers over "inward"

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[15] Ibid., p. 68.

[16] United Nations, Industrial Development Organization, "Recent Overall Progress in Industrialization Achieved by Developing Countries," Industrialization and Productivity, No. 13, 1969, p. 8.

industrialization in promoting a viable pattern of national industrialization. A country's export sector faces outward to a world market for manufactured products. A firm that avails itself of this world market by exporting its manufactures can realize economies of scale that could not be realized if that industry solely produced for a narrow protected domestic market. A firm that produces for export is also confronted by the world competition for manufactured exports. Such a firm must, therefore, continually increase its efficiency of production if it is to be successful in exporting its manufactures. Such an incentive to efficiency is not provided to the firm that produces solely for the protected domestic market. "Outward" industrialization, moreover, involves a transformation of the export sector of a less-developed country. In that the traditional export sectors of the various Latin American nations have performed poorly in recent years, such a transformation would certainly not be unwelcome. In the case of Latin America, however, the export sector has in the past been generally viewed from only a balance of payments point of view, with manufactured exports being treated as insignificant spillovers from domestic production. In 1964 exports of manufactured products as a percentage of total exports for the United Kingdom, Japan, and the Netherlands averaged eight-seven per cent, with manufactured exports representing an average of seventeen per cent of the domestic production of manufactured products of these countries. For Argentina,

Brazil, Mexico, and Chile exports of manufactured goods averaged thirteen per cent of their total exports with these manufactured exports averaging only one per cent of their domestic production in 1964. In addition, while capital goods and durable consumer goods represented an average thirty-nine per cent of the manufactured exports of the above three developed nation, these same products represented only an average eight per cent of the manufactured exports of the four Latin American nations. [17]

It would appear that most of the Latin American nations have not significantly availed themselves of this "outward" tool of industrialization. Where they have, it has been in the form of spillovers from domestic production of non-durable consumer goods. From 1955 to 1964, while world exports of manufactured goods increased by 117 per cent and the total less-developed countries' manufactured exports increased by 81 per cent, Latin America's exports of manufactures increased by only 57 per cent. [18]

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[17] United Nations, Latin American Institute for Economic and Social Planning, "Industrial Development Strategy in Latin America," Industrialization and Productivity, No. 13, 1969, p. 42.

[18] U. N., "Recent Over-all Progress . . . ," p. 84.

The failure of Latin America to more actively pursue a policy of "outward" industrialization is made more serious if one considers that for the period 1963 to 1968 world exports increased by 56.4 per cent as compared to a 26 per cent increases in Latin America exports.[19]

Assuming that an "outward" policy of industrialization is desired by a less-developed country, a choice must be made as to what type of "outward" policy is desired. An "outward" policy centered around participation in an integration scheme such as LAFTA is likely to have different characteristics and face different restraints than an "outward" policy generally designed to promote world exports of manufactured goods. The question of what tool a country should use in any given situation will largely depend on the type of manufactures that the country wishes to promote.

The manufactured exports of the Latin American countries to world markets consist largely of textiles, clothing, shoes, beverages, and food products. In these labor-intensive industries Latin America has been able to create a market via comparative advantages, and the fact that these industries were established relatively early in the development of the region.

A pattern of trade such as this serves to reinforce domestic patterns of industrialization, which if unbalanced to begin with, might

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[19]International Monetary Fund, (IMF), International Financial Statistics, XXII, No. 6 (June, 1970), pp. 218-221.

be undesireable. The export of such products will, however, serve to increase the earnings and stability of the export sector and will possibly result in greater efficiency through competition for those industries engaged in such trade. Such industries usually also have a high labor absorption capacity and according to Hal B. Lary such a trade pattern is desireable from the standpoint of short-run growth potential and the pattern of world demand.[20]

While such trade is certainly welcome for the reasons stated, authors, such as Bela Balassa and Hollis B. Chenery, and agencies, such as the Latin American Institute for Economic and Social Planning (LAIESP), have constructed a strong case for redirecting efforts to the promotion of intermediate, capital, and durable consumer goods for export.[21]

The LAIESP urges that less-developed countries attempt to export capital and consumer durable goods for the following reasons: (1) World demand for these products is growing at a significantly faster rate than demand for other products; (2) The largest scales of

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[20]Hal B. Lary, Imports of Manufacturers from Less Developed Countries (New York: National Bureau of Economic Research, 1968), p. 89.

[21]These arguments are contained in: Bala Balassa, Economic Development and Integration (Mexico City: Centro de Estudios Monetarios Latino Americanos, 1965); Hollis B. Chenery, "Patterns of Industrial Growth," American Economic Review, L, No. 4, (September, 1960), pp. 624-654; U.N. "Industrial Development Strategy--," op. cit.

production are required in these industries (such scales exceeding the limits of domestic markets), and the economies of scale, linkages, and advantages of specialization are most marked for these industries; and (3) Transportation costs (which are generally very high for Latin America) have less of an effect on the sale of these high valued items.[22] Finally, the LAIESP observes that:

> . . . although no opportunity should be lost in promoting such exports of labor-intensive non-durable consumer goods . . . the export of capital and non-durable consumer goods is essential to achieve maximum industrialization. If this is not done, the disparity between imports and exports will continue . . . since (a) the increase in world demand for light-industry products is slackening; (b) protectionalist policies tend to concentrate on such goods; and (c) over the long term, light-industries tend to have a less dynamic effect on the rest of the economy, as a result, inter alia, of the fact that their technical content is smaller and the chain of technological inter-relationships shorter.[23]

Assuming that the LAIEST is correct, how is Latin America to promote the export of such sophisticated manufactures? Few of the Latin American countries could compete with the industrialized nations in world markets for the sale of such manufactures. They could, however, promote the export of such manufactures via an integration scheme.

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[22] U. N., "Industrial Development Strategy . . . ," p. 42.

[23] Ibid.

Integration as a Tool of National Industrialization

Integration, as stated in the previous section, is a special "outward" instrument of industrialization. As John Pincus concludes, there are two realistic ways for less-developed countries to expand manufactured export, and both involve preferential systems. The first of these is through customs unions and free trade areas, and the second is through preferences extended from the rich to the poor. In that little can be done to implement the latter approach, increasing weight must be given to the former approach.[24]

LAFTA is a proposed free trade area encompassing eleven nations of Latin America: Argentina, Bolivia, Brazil, Chile, Colombia, Ecuador, Mexico, Paraguay, Peru, Uruguay, and Venezuela (Venezuela and Bolivia joined in 1966). LAFTA has as its intent the establishment of a regional free trade area to encourage greater trade among the countries of the region. This was to have been acomplished by 1973, but as a result of the re-evaluation of LAFTA by the Ninth Conference of LAFTA in 1969, the goal for freeing regional trade is now 1980. The Treaty of Montevideo which established LAFTA in 1960 contains no mechanism assuring the integration of the economies of the signatories to the treaty. It was hoped that some measure

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[24] John Pincus, Trade, Aid, and Development (New York: McGraw-Hill, 1967), pp. 190-210.

of integration might evolve out of greater trade among the member countries. Also, voluntary integration pacts among participants were provided for by the inclusion of Resolution Ninety-nine in the treaty in 1964, which allowed for negotiated integration on a bilateral or multilateral basis.[25] Resolution 202, which set the norms for sub-regional agreements, was another attempt to encourage integration on a voluntary basis.

Despite these attempts to promote integration (the harmonizing of national economies so that a rational, efficient pattern of industrialization evolves) the progress of LAFTA throughout most of the past decade was almost entirely in the direction of a freeing of intra-regional trade with little provision for the rationalization and equalization of that trade.

The member countries with deficient markets, Chile, Colombia, Peru, Uruguay, and Venezuela, and the less developed member countries, Bolivia, Ecuador, and Paraguay[26] have been generally dissatisfied with the largely trade-oriented direction of LAFTA; the

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[25]A copy of the Treaty of Montevideo is contained in Miguel S. Wionczek, ed., Economic Cooperation in Latin America, Africa, and Asia: A Handbook of Documents (Massachusetts: MIT Press, 1969), pp. 43-95.

[26]The classifications of countries with deficient markets and less-developed countries is contained in the Treaty of Montevideo. Uruguay was temporarily given the status of a less-developed member in 1968.

benefits of which, they claim, were being captured by the Big Three of the region: Argentina, Brazil, and Mexico. To improve their competitive position six countries, Chile, Colombia, Peru, Bolivia, Ecuador, and Venezuela, began negotiations in 1967 to form the Andean Group, a subregional integration scheme within the framework of LAFTA. The Andean Group Treaty, which was ratified in 1969 by all initiates except Venezuela, has as its goal not only greater trade among its members, but also a progressive integration of their economies. The Big Three, viewing the formation of the Andean Group as a possible threat to LAFTA's progress as they envisioned progress, countered by increasing negotiations on various complementation agreements and granting liberal preferences to the other member nations so as to make the existing LAFTA framework more attractive. Argentina and Brazil also began formulating a regional group to improve the River Plate Basin which would include Bolivia, Paraguay, and Uruguay.

Despite these maneuverings, LAFTA has evolved into two rather distinct groups espousing two rather distinct philosophies. One group, representing the Big Three, favors a gradual freeing of trade, with the emphasis on manufactured goods, as a first and necessary step toward the integration of the region. This group has been

referred to as the commercialists.[27] The instrument of their policy has been the sectoral meeting wherein regional manufacturers of a particular product line meet to draw up National List Concession proposals to be submitted to their respective governments, to develop bilateral product concessions, and to explore possible areas of complementation.

The second group, the integrationist, consists of the Andean Group members. Uruguay and Paraguay, although sympathetic to the integrationist cause, are still commercially tied to Argentina and Brazil. Venezuela, if it can overcome resistence from high-cost domestic manufacturers, will possibly join the Andean Group. The instrument of the integrationists' policy is the subregional grouping to promote irreversible economic integration among its members as a first and necessary step toward the integration of the whole region. In this respect, their position is similar to the reasoning used in the formation of the Central American Common Market (CACM) as a prerequisite to the participation of the CACM countries in LAFTA.

The evolution of these two groups has resulted in an intensification of trade among the commercialists and a perceptible withdrawal

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[27]A good discussion on the commercialist position and the integrationist position is contained in "A Monthly Report on Latin American Integration," Comercio Exterior de Mexico, XVI, No. 3, (March, 1969), pp. 6-8.

of the integrationist from participation in sectoral meetings. In its 1968 evaluation of LAFTA the Inter-American Committee of the Alliance for Progress (ICAP) cited this almost inevitable and growing gap between the commercialists and the integrationists as the major obstacle to integration. As the ICAP states:

> The larger Latin American countries are not yet prepared to bear the additional burden of aid to the region's less developed nations. . . . It is possible that integration of the region as a whole may have to wait until the headway made in subregional integration has placed all economic entities . . . in a position of equal bargaining strength.[28]

The proposition that an integration scheme, while not as desireable as free world trade, is preferable to the existing nationalistic trade barriers in terms of welfare is widely held by development economist. It is also held by such economists as Miguel Wionczek, that as a second best system, market forces in LAFTA should be at liberty to determine a new allocation of productive services.[29] This view that regional free trade along with a free working of market forces will generate an optimal integration scheme is also held by the commercialists. Unfortunately, under such an arrangement

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[28]"A Monthly Report on Latin American Integration," Comercio Exterior de Mexico, XVI, No. 3 (March, 1969), p. 7.

[29]Miguel Wionczek, "Introduction: Requisites for Viable Integration" in Latin American Economic Integration: Experiences and Prospects, ed. by Miguel Wionczek (New York: Frederick A. Praeger, 1966), p. 7.

the greater part of the benefits, in terms of greater exports, increased industrialization, and the attraction of foreign investment, appear to gravitate to the larger, wealthier members.

The experience of other integration schemes such as the East African Common Market and the CACM would seem to substantiate this observation.

The East African Common Market was in a near state of collapse in 1965 due to threats by Uganda and Tanganyika to withdraw because Kenya, the wealthiest member, exported sixty per cent of intra-regional exports and seventy per cent of intra-regional manufactured exports. In addition Kenya also possessed 404 of the 474 regional firms. In 1966 Nicaragua and Honduras threatened to withdraw from the CACM because they felt that the wealthier members were capturing most of the regional benefits of integration. They argued that just as free trade has led to greater world inequality, it has led to greater inequality within the CACM.[30]

Placido Garcia Reynosa cites that during the creation of a regional market,

> . . . the problem . . . arises of how to effect the simultaneous integration of the more developed countries . . . while at the same time creating conditions

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[30]Roger D. Hansen, "Political Theory and Regional Integration: The First Ten Years" in The Movement Toward Latin American Unity, ed. by Ronald Hilton (New York: Frederick A. Praeger, 1969), p. 22.

that will permit the emergence of modern industry in the smaller republics.[31]

In the case of LAFTA, given the two existing philosophies, that problem has resulted in the polarization of two groups of participants working for the same goal, but in many cases, employing different means of achieving it.

The trade patterns that have resulted from the use of the existing instruments of trade liberalization in LAFTA have been encouraging from the standpoint of intra-regional export growth and export composition, but they tend to confirm the integrationists' arguments that the benefits of trade liberalization have not been evenly distributed.

Intra-LAFTA trade, although representing only 11.1 per cent of the region's world trade in 1968, has been very dynamic as can be seen in Table 1. The increase in LAFTA trade from 1961 to 1968 (The Treaty of Montevideo went into force in 1961.) accounted for 25.4 per cent of the increase in LAFTA's world trade during this period. It is estimated that ninety to ninety-five per cent of this trade consisted of negotiated products.[32] Referring to Table 2, the largest

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[31] Placido Garcia Reynosa, "Problems of Regional Industrialization" in Latin American Economic Integration: Experiences and Prospects, ed. by Miguel Wionczek (New York: Frederick A. Praeger, 1966), p. 118.

[32] Asociacion Latinoamericana de Libre Comercio, Comite Ejecutivo Permanente, El Comercio Exterior de la ALALC (Cep/Repartido 1161), Montevideo, June 17, 1969, p. 10.

TABLE 1

COMMERCE OF LAFTA, 1960-1968
(Millions of U.S. Dollars)

	+ Exports (FOB) Imports (CIF)		Growth Index 1961 = 100	
Year	LAFTA[a]	Rest of World	LAFTA	Rest of World
1960	715.2	9,706.7	108	95
1961	658.7	10,154.4	100	100
1962	772.4	10,209.9	117	101
1963	932.2	10,202.9	141	100
1964	1,200.7	10,735.5	182	106
1965	1,406.7	10,956.3	214	108
1966	1,457.1	12,318.5	221	121
1967	1,415.3	12,373.6	215	122
1968	1,604.0	12,930.8	244	127

[a]LAFTA trade does not, for purposes of comparison, include Venezuela and Bolivia who joined LAFTA in 1966. Trade data for Chile, Ecuador, and Uruguay is estimated for 1968.

Source: Asociacion Latinoamericana de Libre Comercio, Comite Ejecutivo Permanente, El Comercio Exterior de la ALALC (Cep/Repartido 1161), Montevideo, June 17, 1969, p. 4.

part of total LAFTA intra-regional trade has been conducted by Argentina, Brazil, Chile, Peru, and Mexico--87.6 per cent of LAFTA trade in 1968. In terms of the effect of this trade on the balance of payments of the participants, Argentina and Mexico accumulated an intra-regional trade surplus of 389.8 million dollars, while the rest of the region as a whole accumulated an intra-regional trade deficit of 1,083.7 million dollars during the period 1962 to

TABLE 2

LAFTA's INTRA-REGIONAL TRADE AND COMMERCIAL BALANCES
(Millions of U.S. Dollars)

Year	Trade and Commercial balances	Argentina	Brazil	Colombia	Chile	Ecuador	Mexico	Paraguay	Peru	Uruguay
1962	Exp. FOB	141,4	75,8	7,3	39,4	6,1	16,7	10,9	48,8	8,0
	Imp. CIF	103,2	128,6	12,5	80,5	3,9	6,1	6,1	45,2	34,0
	Balance	38,2	- 52,8	- 5,2	- 41,1	2,2	10,6	4,8	3,6	-26,0
	Per cent of LAFTA trade	31.6	26.3	2.6	15.5	1.3	3.0	2.2	12.1	5.4
1968	Exp. FOB	318,0	186,0	25,3	77,4	19,0	50,0	16,0	43,0	17,0
	Imp. CIF	239,0	210,0	36,4	143,9	17,0	41,0	17,0	98,0	44,1
	Balance	79,9	- 24,0	-11,1	- 66,5	2,0	9,0	- 1,0	-55,0	-27,1
	Per cent of LAFTA trade	34.8	24.6	4.3	13.8	2.2	5.6	5.6	8.8	3.9

Note:

Trade is estimated on incomplete data from Chile, Uruguary, and Ecuador for 1968. Venezuela and Bolivia, who joined LAFTA in 1966, are not contained in this table.

Source: Asociacion Latincamericana de Libre Comercio, Comite Ejecutivo Permanente, El Comercio Exterior de la ALALC (Cep/Repartido 1161), Montevideo, June 17, 1969, p. 14.

1968.[33]

The composition of LAFTA trade as a whole shows a greater measure of diversification than the participants' world trade. For the period 1962 to 1967 forty-six per cent of regional imports consisted of either semi-finished or finished manufactured goods.[34]

The benefits of diversification have, however, accrued largely to the commercialists. While importing seventy-two per cent of the regions manufactured goods exports and sixty-five per cent of combined semi-finished and finished manufactured exports, the commercialist also dominated the export of these goods during the period 1962-1967. For every one hundred dollars of manufactured goods imported from the region, the commercialists exported an average of 140 dollars of manufactured goods to the region.[35]

Not only have regional trade and trade in manufactured goods grown at a significantly faster rate than the regions' world trade and trade in manufactured goods, but the composition of regional trade in

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[33] The difference between the total surplus and deficit represents transportation, credit, and insurance charges.

[34] Asociacion Latinoamericana de Libre Comercio, El Comercio Exterior de la ALALC, p. 17.

[35] Ibid., p. 14.

manufactured goods has deviated from the composition of the regions world trade in manufactured goods which largely consists of non-durable consumer goods. In 1967 the commodity groups including precision instruments, transport equipment, metal transformation products, pulp and paper, plastics, and chemicals represented 63.2 per cent of intra-regional manufactured exports.[36] In these areas of manufacturing where economies of scale are very important, the commercialists, in most cases, have also dominated trade. In 1966, while 68.3 per cent of intra-regional manufactured exports originated from the commercialists, the commercialists exported 79.8 per cent of intra-regional machinery and transport equipment exports.[37]

Besides stimulating trade, especially in the area of manufactured exports, it was hoped that LAFTA, with its enlarged market, would attract a greater amount of foreign investment in manufacturing to the region.

While no data exist to indicate the amount of foreign investment attracted to the region, several specific examples of such an attraction of foreign investment can be cited. The following examples

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[36] "Commodity Patterns of Imports Under LAFTA Concessions," Business Latin America, August 14, 1969, pp. 260-261. Percentages do not include data for Uruguay and Venezuela and data for Bolivia, Ecuador, and Peru is estimated.

[37] "The Structure of Intra-LAFTA Trade," Business Latin America, July 4, 1968, pp. 212-213.

have been taken from various issues of Business Latin America for 1969. In December, 1969 Eastman Kodak announced that it was going to diversify its Latin American operations so that film products would be produced in Mexico, photographic paper in Brazil, and cameras in Argentina. Fifty-five per cent of Mexican and Brazilian production is intended for LAFTA export where sixty to seventy per cent of the market has been opened through LAFTA concessions. This project has so far resulted in a thirty-two million dollar investment in Mexico. In November, 1969 Velcro Industries of Canada announced plans for several fastener factories to be constructed in Uruguay for a six-country LAFTA market. In January, 1969 Bayer of Germany began a twenty million dollar investment program for the Andean Group where acrylic fibers are under concession. In December, 1969 W. R. Grace industries announced a ten million dollar investment in Colombian paper production for the Andean Group. Germany's BASF industries in December, 1969 announced that they would increase investment in chemical industries in Argentina, Brazil, Mexico, Chile, and Colombia from 33 million dollars in 1969 to 270 million in 1975 to supply the needs of the regional market.

These are but a few of the types of investments that have been drawn to the area, but they serve to indicate the attractiveness of LAFTA to certain industries.

It would appear from the above discussion, that LAFTA has generated some significant benefits for its members. All sorts of structural problems, however, remain to be solved, such as the inequality of trade, but as it has been observed by the United Nations Committee on Trade and Development (UNCTAD),

> The problem of expanding trade and of promoting economic co-operation and integration among developing countries can only be tackled in a practical manner if it is viewed in a dynamic perspective. Not all conditions . . . can be fulfilled at the same time. Some requireme[illegible] partially, with the consequenc[illegible]illment of other requirements [illegible]ted.[38]

In view o[illegible]ion in Latin America and the inability [illegible]lization to satisfy those needs, it is likel[illegible] will eventually be solved.

An [illegible]g Mexico's Partici-

[illegible]ary Statement

The three pr[illegible] of this chapter dealt with the general characteristics, as evident in Latin America, of what were termed "inward" and "outward" tools of industrialization. The terms "inward" and "outward" merely reflect the orientation of specific

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[38] United Nations, Conference on Trade and Development, Trade Expansion and Economic Integration among Developing Countries (TD/B/85/Rev. 1), 1967, p. 13.

national industrial plans dealing with industrial promotion, taxes, savings, infrastructure development, and resource allocation.

As an instrument of national industrialization, LAFTA would appear to offer several advantages over other tools of industrialization. While "inward" tools have often generated a high cost and unbalanced industrial structure, and face as restraints, in many cases, a low import coefficient, a market too small to develop many capital goods industries, a poor distribution of income, and regional dualism, LAFTA offers a trade in manufactured goods with a high content of durable consumer and capital goods. This trade moreover, is not restrained by the factors mentioned above. While "inward" industrialization in Latin America has relied upon the earnings of a primary product oriented, poor performing export sector for necessary capital and raw material imports, LAFTA, since it transforms the export sector into a dynamic tool of industrialization, contributes to a stronger export sector.

LAFTA as tool of "outward" industrialization also offers an advantage over the general promotion of manufactured exports to world markets as an instrument of "outward" industrialization in that a member country's exports to LAFTA can avoid the highly protectionist policies and price competition found in world markets.

The degree to which any of the aforementioned general characteristics of the tools of industrialization apply to Mexico, and the

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In view of the needs for industrialization in Latin America and the inability of traditional tools of industrialization to satisfy those needs, it is likely that these structural problems will eventually be solved.

An Analytical Basis for Evaluating Mexico's Participation in LAFTA: A Summary Statement

The three previous sections of this chapter dealt with the general characteristics, as evident in Latin America, of what were termed "inward" and "outward" tools of industrialization. The terms "inward" and "outward" merely reflect the orientation of specific

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The degree to which any of the aforementioned general characteristics of the tools of industrialization apply to Mexico, and the

degree to which Mexico would wish to employ any of the aforementioned tools of industrialization depends, of course, on factors peculiar to Mexico. It is the purpose of this paper to identify those factors which have most influenced Mexico's participation in LAFTA. It is the identification of these factors that constitutes the analytical basis for evaluating Mexico's participation in LAFTA. This identification will be accomplished by answering three questions: (1) Why did Mexico join LAFTA in 1960 after a history of little interaction with its Latin American neighbors, and what benefits did Mexico expect to receive from participation in LAFTA; (2) To what degree has Mexico received those benefits that it expected to receive from participating in LAFTA; and (3) What forces will shape Mexico's participation in LAFTA in the future?

A study such as that outlined above will necessarily entail an exhaustive analysis of the needs for industrialization in Mexico, the obstacles facing further industrialization in Mexico, and the ability of the various tools of industrialization to overcome those obstacles.

In that the needs for industrialization in Mexico and the obstacles facing industrialization in Mexico are similar to the needs for industrialization and the obstacles to that industrialization in other less-developed countries, some insights into the development process in other less-developed countries might also be gained from

the above analysis. Moreover, as a by-product of this investigation several myths and misconceptions concerning the development process in Mexico will be corrected.

CHAPTER II

THE INDUSTRIALIZATION OF MEXICO: NEEDS AND PERFORMANCE

In their evaluation of the reasons for Mexico's participation in LAFTA, Philippe C. Schmitter and Ernst B. Haas examined Mexico's rationale in originally joining LAFTA in 1960 and the factors determining the degree to which Mexico would participate in LAFTA in the period subsequent to the signing of the Treaty of Montevideo. They concluded that Mexico joined LAFTA to alleviate an immediate problem: the slowing down of Mexican industrialization in the face of a rapid population growth rate and an even more rapid rate of urbanization. This dilemma was compounded by a slackening of growth in the export sector which appeared incapable of further providing the necessary capacity to import needed to satisfy industrial needs. Mexico's future participation in LAFTA, in their analysis, would depend upon both the future performance of industrialization, changes in the needs for industry and the structuring of LAFTA.[1]

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[1]Philippe C. Schmitter and Ernst B. Haas, Mexico and Latin American Economic Integration, Institute of International Studies, Research Series No. 5 (Berkley: University of California Press, 1964),

In The Dilemma of Mexico's Development Raymond Vernon expressed this same sentiment in his observation that:

> In the early 1960's . . . Mexico's economy seemed to be approaching a new series of roadblocks. The country's growth appeared to be slowing . . . and the prospects for some new impetus to growth seemed uncertain. If the economy were allowed to drift for very long, the loss of momentum might expose the country to serious political risks and economic losses. On the other hand, practically every major change in policy that offered some promise of stimulating the country's development also seemed to involve a considerable measure of political risk.[2]

The dilemma of Mexico's development, as stated by Raymond Vernon, was how to speed up the industrial process with the least risk to Mexico's political stability. To broaden demand through the redistribution of income or increased goveernment participation would jeopardize the support of the business community, and to liberalize foreign investment restrictions or increase taxes would evoke public mistrust. LAFTA membership emerged from his analysis as a rather risk free approach to reduce the seriousness of this dilemma.

The Needs for Industrialization in Mexico

There is no typical Latin American country, but certain characteristics of Mexico's development during the last twenty years have

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pp. 15-20.

[2]Raymond Vernon, The Dilemma of Mexico's Development (Cambridge: Harvard University Press, 1963), p. 176.

been common of all of Latin America. Among these common characteristics is the need for a rapid rate of industrialization due to a rapid population growth and rate of urbanization, and a poor performing traditional export sector which no longer serves as a significant stimulus to development and is strained to provide sufficient foreign exchange earnings to provide for needed imports of industrial products. The need for a more rapid industrialization is also a function of the poor performance of alternative economic activities such as agriculture and mining. The ECLA cites the above factors as constituting the central needs for a rapid industrialization of Mexico and Latin America as a whole.[3] One aspect of these needs, the state of the external sector, will be reserved for discussion in Chapter IV.

Industry's absorption of labor

Mexico's and Latin America's high population growth rates and rates of urbanization probably constitute the most pressing need for their rapid industrialization. Referring to Table 3 it can be seen that Mexico, along with Venezuela, has experienced the fastest population growth in Latin America in recent years. While the average annual compound population growth rate for the period 1963-1968 for Latin America was approximately 2.8 per cent, the rate for Mexico

[3]U. N., The Process of Industrial Development in Latin America, p. 4.

TABLE 3

NATIONAL ACCOUNT AND POPULATION STATISTICS FOR LATIN AMERICA - 1968

Country or region	GNP		
	Total 1968 (Billions of U.S. dollars)	Five-year percentage increase (constant prices)	Per cent of Latin American total GNP
Argentina	15.41[a]	15.0	14.1
Bolivia	0.80	33.0[b]	0.7
Brazil	22.11[a]	14.0[b]	20.2
Chile	6.31[a]	23.0	5.8
Colombia	5.50	24.0	5.0
Ecuador	1.46	28.0	1.3
Mexico	26.77	42.0[c]	24.4
Paraguay	0.52[a]	22.0	0.5
Peru	4.05[a]	29.0	3.7
Uruguay	1.30[a]	4.0[b, c]	1.2
Venezuela	8.50	27.0	7.8
Total LAFTA	92.73	25.0	84.7
Total CACM	4.55	37.0	4.2
Total Caribbean	12.25	27.0	11.2
Total Latin America	109.53	25.0	100.0

Notes:

Currency figures are converted at official exchange rates except for Argentina, Brazil, Chile, Colombia, and Peru for which an implicit trade rate was used. a) estimated using 1967 prices. b) 1961-1966. c) GPD used. d) estimated using 1966 prices.

Sources: "Market indicators for 26 Latin American Countries," Business Latin America, December 18, 1969, pp. 404-405; "Population Census," Review of the Economic Situation of Mexico, XLVI, No. 534. (May, 1970), pp. 122-128.

TABLE 3--Continued

Per capita national income (U. S. dollars)	Population		
	Total (Millions end of year)	Five-year percentage increase	Per cent urban (towns of 2,500) and over
652	23.62	8.0	78.0
147	4.68	14.0	35.0
180	88.21	16.0	48.0
545	9.35	13.0	71.0
278	19.83	17.0	56.0
220	5.69	18.0	48.0
512	47.27	19.0	62.0
193	2.23	17.0	35.0
351[d]	12.77	17.0	49.0
464	2.82	6.0	79.0
801	9.69	19.0	72.0
363	226.15	16.0	. .
276	14.0	18.0	. .
435	26.1	18.0	. .
365	226.30	15.0	. .

TABLE 4

MEXICO'S POPULATION GROWTH IN SELECTED MAJOR URBAN AREAS
(Thousands of Persons)

Area	Year	Total population	Percentage change over the reported periods
Nation	1930*	16,553	. .
	1940	19,654	18.73
	1950*	25,791	31.23
	1960	36,046	39.76
	1969	48,930	35.74
Federal	1930	1,230	. .
District	1940	1,758	42.93
	1950	3,050	73.49
	1960	4,871	59.70
	1969	7,006	43.83
Monterrey	1930	137	. .
	1940	190	38.69
	1950	339	78.42
	1960	601	77.28
	1969	830	38.10
Guadalajara	1930	185	. .
	1940	237	28.11
	1950	380	60.33
	1960	740	94.73
	1969	1,196	61.62

Note:

*Population reported at mid-year.

Source: Calculated from: Mexico, Secretaria de Industria y Comercio, Anuario Estadistico de los Estados Unidos Mexicanos, 1966-1967, Mexico, D.F.: Talleres Graficos de la Nación, 1969 and "Population," Comercio Exterior de Mexico, XVI, No. 4 (April, 1970), p. 19.

TABLE 5

MEXICO'S DEMOGRAPHIC GROWTH
(Thousands of Persons)

Year	Total population	Per cent of total population		Annual rate of growth in population		
		Urban	Rural	Total	Urban	Rural
1900	13,607	19.4	80.6	. .	. .	. .
1930	16,553	33.5	66.5	. .	. .	. .
1950	25,791	42.6	57.4	. .	. .	. .
1960	36,046	50.7	49.3	. .	. .	. .
1961	37,268	51.7	48.3	3.39	5.27	1.45
1962	38,543	52.6	47.4	3.42	5.26	1.45
1963	39,871	53.5	46.5	3.45	5.24	1.46
1964	41,253	54.4	45.6	3.47	5.21	1.46
1965	42,689	55.3	44.7	3.48	5.17	1.46
1966	44,145	56.1	43.9	3.41	5.00	1.45
1967	45,671	57.0	43.0	3.46	5.03	1.45
1968	47,270	. .	. .	3.50	. .	. .
1969	48,930	62.0*	38.0*	3.51	. .	. .

Note:

For the years 1900, 1930, and 1950 population is reported at mid-year. For all other years population is reported at end of year. Urban population consists of persons living in towns or cities having more than 2,500 residents.

*Preliminary estimates.

Sources: Calculated from: Mexico, Secretaria de Industria y Comercio, Anuario Estadistico de los Estados Unidos Mexicanos, 1966-1967, (Mexico, D.F.: Talleres Graficos de la Nación, 1969) and "Population Census," Review of the Economic Situation of Mexico, XLVI, No. 534 (May, 1970), pp. 122-128.

was a phenomenal 3.5 per cent. Referring to Table 4 it can be seen that for Mexico the rate of population growth more than doubled from the period 1930-1940 to the period 1950-1960. Population growth for the period 1960-1969 maintained approximately the same rate as for the previous decade, that rate being the highest in Latin America. Referring to Table 5 it can be observed that the rate of urban population growth in Mexico has been significantly faster than the general rate of population growth. Urban population growth was 5.03 per cent as compared to a 3.46 per cent total population growth in 1966. It would appear that through the first six years of the past decade, the rate of urbanization was slowing. Urban population growth declined from 5.27 per cent in 1961 to 5.03 per cent in 1966. Recent census data indicates, however, that urbanization has speeded up in more recent years with urban population constituting sixty-two per cent of total population in 1969.

This phenomena of urbanization, as indicated by Table 3, has not only been confined to Mexico in that four of the eleven LAFTA members rank above Mexico in their degree of urbanization (Argentina, Chile, Uruguay, and Venezuela). It is apparent from Table 4 that the growth Mexico's major urban areas, the Federal District, Monterey, and Guadalajara, has slowed during the last two decades, but this must be compared to the growth of the suburban areas of these metropolises. The populations of San Nicolas de los Garza and

Guadalupe, satellite communities of Monterey, grew during the period 1960 to 1969 by 170.4 per cent and 301.3 per cent respectively. In 1969 40.5 per cent of Mexico's population lived in cities of over 100,000 persons. Of the fifty-three cities in Mexico with populations over 100,000 thirty-two cities grew by more than fifty per cent during the period 1960-1969.[4]

Besides the obvious burden that such a pattern of population growth, as experienced by Latin America and by Mexico, imposes on development goals such as the OAS goal of increasing per capita product by a minimum of 2.5 per cent per year for the Latin American nations, this pattern of population growth has two other main implications. First, the high rate of urban growth experienced by a country such as Mexico must be parallelled by a high rate of industrial growth and employment if urban unemployment and the growth of various non-productive "services" (i.e., selling lottery tickets) are to be avoided. Second, the rapid expansion of urban areas results in a more widely diversified demand for consumer manufactured goods than the country usually can efficiently supply at that stage in its development.

The process of industrialization in Latin America as a whole has not kept pace with the process of urbanization. It is roughly estimated that between 1925 and 1960 industry absorbed only a little

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[4]"Population," Comercio Exterior de Mexico, XVI, No. 4 (April, 1970), pp. 19-20.

more than 23 per cent of the 23 million persons added to the urban labor force, and 15 per cent of the 36 million persons added to total employment in Latin America.[5] An ECLA study points out that the industrial absorption of labor (industry is synonymous with manufacturing in the study) has not only been deficient, but it has also been declining with respect to its share of total non-agricultural employment. In 1925 the industrial employment share of non-agricultural employment for Latin America was 35.4 per cent. In 1960, however, the share had declined to 27.1 per cent. Only two nations, of those studied, increased their industrial employment share of non-agricultural employment during the 1950's and these countries were Mexico and Venezuela. Venezuela's increase during the period 1950 to 1960 amounted to less than one per cent while Mexico's increase during the same period amounted to 1.8 per cent (28.2 per cent to 30.0 per cent).[6]

During the period 1960-1967 the labor absorbing ability of the industrial sector for Latin America as a whole was less than it had been during the period 1950-1960. The average annual growth of

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[5]Donald Solar, "The Case Against Latin American Integration: Economic and Political Factors" in The Movement Toward Latin American Unity, ed. by Ronald Hilton (New York: Frederick A. Praeger, 1969), p. 120.

[6]U.N., The Process of Industrial Development in Latin America, p. 37.

industrial employment for the period 1950-1960 was 2.4 per cent. During the period 1960-1967 estimated average annual growth of industrial employment in Latin America was 2.1 per cent.[7] With population growing at an approximate 2.8 per cent per year in Latin America during the period 1963-1968, increases in industrial employment did not keep pace with general increases in population. This trend prompted the Economic Commission for Latin America (ECLA) to state that, "These figures are already significant to indicate that one of the outstanding features of industrialization in Latin America is a marked failure to contribute sufficient employment to permit the absorption of the rapidly growing labour force."[8]

The slowdown in the ability of Latin American industry to absorb labor can be partially explained by structural changes that have taken place in Latin American industry. Most of the industrial growth of the period 1925-1960 was through expansion of factory activities, and very little through the expansion of more labor absorbing artisan activities. Although manufacturing employment during this period increased from 4.4 million persons to 9.7 million persons,

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[7]United Nation, Economic Commission for Latin America, Economic Survey of Latin America, 1967. (E/CN. 12/808/Rev. 1), 1969, pp. 40-41.

[8]U. N., The Process of Industrial Development in Latin America, p. 38.

74.5 per cent of this increase was in factory employment. The ECLA has estimated that if artisan activities had grown as fast as factory activities, industrial employment would have grown by an additional five million persons. [9]

The general results of the slow rate of labor absorption by industry in Latin America are indicated by the estimate that forty per cent of the Latin American work force is under-employed (i.e., either partially or totally unemployed). Unemployment in major urban areas is high: 6.5 per cent in Buenos Aires, 8.5 per cent in Montevideo, and 7.6 per cent in Santiago. This poor performance of industry has not only resulted in a declining share of industrial employment in nonagricultural employment. Whereas manufacturing employed 14.2 per cent of the total labor force of Latin America in 1950, it employed 13.8 per cent of the total labor force in 1965. [10]

Like Latin America as a whole, Mexico incurred a declining share of industrial employment in total nonagricultural employment during the period 1925-1950. Although industry was able to increase its share of employment with respect to total employment because of a slowdown in agricultural employment growth, growth in teriary

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[9] U.N., The Process of Industrial Development in Latin America, p. 41.

[10] "Regional Affairs," Comercio Exterior de Mexico, Vol. XVI, No. 2, (February, 1969), p. 17.

employment was more rapid than growth in industrial employment.

Mexico also incurred the shift from artisan to factory employment in industry common to Latin America. Artisan employment constituted seventy per cent of the industrial labor force in 1925, but by 1960 artisan employment was only thirty-six per cent of the Mexican labor force (the lowest percentage in Latin America).[11]

Although such a shift from labor-intensive-industry to relatively less labor-intensive industry is an important determininant of the ability of industry to absorb labor, its significance is relative to the growth rate of the emergent industrial activity. The impact that such a structural change in industry has on the absorption of labor also depends on the productivity of the workers in the two types of industry. It would therefore not be unusual to have a restructuring of industry taking place such as that which has occurred in Mexico or Latin America while the ability of industry to absorb labor was increasing. This was, in fact, the experience of Mexico after 1950.

From 1950 to 1960 the total growth of manufacturing employment was 60.0 per cent as compared to a rise in total employment of 35.8 per cent. (Table 6) This represented a slowdown of growth in

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[11]Fernando H. Cardoza and José Luis Reyna, "Industrialization, Occupational Structure, and Social Stratification in Latin America," in Constructive Change in Latin America, ed. by Cole Blasier (Pittsburg: University of Pittsburg Press, 1968), p. 38.

TABLE 6

MEXICO'S ECONOMICALLY ACTIVE POPULATION BY FIELD OF ACTIVITY
(Thousand of Persons)

Activity	1940	1950	1960	1965	1969*
Total	5,858.1	8,345.2	11,332.0	13,427.0	16,141
Agriculture, fishing forestry	3,830.9	4,823.9	6,144.9	6,866.7	7,442.0
Per cent of total	65.4	57.8	54.2	51.4	46.1
Extractive industries	106.7	97.1	141.8	172.3	278.0
Per cent of total	1.8	1.2	1.2	1.3	1.7
Manufacturing	630.3	972.5	1,556.3	2,045.1	2,825.0
Per cent of total	10.6	11.7	13.7	15.3	17.5
Construction	Included	244.5	408.4	528.6	753.0
Per cent of total	in manu-facturing	2.7	3.6	4.3	4.7
Electricity, gas, etc.	9.3	25.0	41.4	52.5	87.0
Per cent of total	0.2	0.3	0.8	0.4	0.5
Commerce	552.5	684.1	1,074.6	1,377.4	1,837.0
Per cent of total	9.5	8.2	9.5	10.3	11.4

Note: *Data for 1969 is provisional.

TABLE 6--Continued

Activity	1940	1950	1960	1965	1969*
Transportation	149.5	210.6	357.1	482.4	659.0
Per cent of total	2.6	2.5	3.1	3.6	4.1
Services	415.3	879.4	1,525.7	1,848.2	2,260.0
Per cent of total	7.1	10.5	13.5	13.8	14.0
Others	163.7	355.0	81.8	. .	. .
Per cent of total	2.8	4.3	0.4	. .	. .

Sources: Calculated from: Mexico, Secretaria de Industria y Comercio, Anuario Estadistico de los Estados Unidos Mexicanos, 1966-1967 (Mexico, D.F.: Talleres Gráficos de la Nación, 1969), Mexico, Secretaria de Industria y Comercio, Revista de Estadistica (Mexico, D.F.: Talleres Gráficos de la Nación, June, 1967), "Mexico's Occupationa Structure," Review of the Economic Situation of Mexico, XLV, No. 529 (December, 1969), pp. 10-15.

total employment in that growth in total employment for the period 1940-1950 was 44.3 per cent. The growth of manufacturing employment during the period 1950-1960 of 60.0 per cent represented an increase over growth during the previous decade which totaled 54.3 per cent. As a result of this higher growth rate, and the lower growth rate of other employment activities. Manufacturing employment increased its share of total employment from 11.7 per cent in 1950 to 13.7 per cent in 1960. Manufacturing employment also increased its share of nonagricultural employment from 28.2 per cent in 1950 to 30.0 per cent in 1960.

Although employment in manufacturing grew at a faster rate during the period 1950-1960 than it had during the previous decade, and although industry increased its share of nonagricultural employment, its performance appears to have been less than satisfactory considering the needs for increased manufacturing employment during that period. Referring to Table 7 it can be observed that during the period 1950-1960, urban population grew at a faster rate (61.20 per cent) than employment in manufacturing (60.03 per cent). In that the urban population is highly dependent on manufacturing for employment, the above statistics are most significant. It would appear that manufacturing employment was not able to even keep pace with

TABLE 7

MEXICO'S URBAN POPULATION CHANGES AND URBAN EMPLOYMENT

Item	Percentage change 1950-1960	Percentage change 1960-1965	Percentage[a] change 1965-1969
Total population	39.76	18.43	14.61
Urban population	61.20	29.04	28.50
Total employment	35.79	18.48	20.21
Employment in manufacturing	60.03	31.42	38.15
Employment in commerce	57.08	28.11	33.40
Employment in services	73.49	21.01	22.29
(Percentage change in manufacturing employment ÷ percentage change in urban population)	0.98	1.08	1.34
(Percentage change in total employment ÷ percentage change in total population)	0.90	1.00	1.38

[a]Urban employment is based on an estimated change from 1968.

Source: Table 5 and Table 6.

urban population increases during this period. [12]

[12]This point often made by the ECLA, assumes that growth of the urban labor force is roughly equivalent to growth of urban population. This obviously may not be the case. The significance of the point may, therefore, be overstated.

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Although employment in services grew at a slower rate during the 1950's than it had during the 1940's (73 per cent versus 111 per cent) its growth rate during the 1950's was still higher than that of manufacturing employment. Whereas service employment was ninety per cent as great as manufacturing employment in 1950, it was ninety-eight per cent as great as manufacturing employment in 1960. If the whole tertiary sector (services, transportation, commerce, electricity and gas, and construction) employment is compared to employment in manufacturing, tertiary employment was 2.4 times greater than manufacturing employment in 1960.

During the period 1960-1969 the ability of manufacturing to absorb labor was significantly greater than it had been during the period 1950-1960. While manufacturing employment increased by 60.0 per cent during the period 1950-1960, from 1960-1969 manufacturing employment increased by 81.6 per cent. Manufacturing employment as a percentage share of total nonagricultural employment also increased--from 30 per cent in 1960 to 32.47 per cent in 1969.

Unlike the period 1950-1960, employment in manufacturing during the period 1960-1969 grew at a significantly faster rate than growth in urban population.

Referring again to Table 7 the ratio of growth in manufacturing employment to growth in urban population was 1.08 for the period

1960-1965 and 1.34 for the period 1965-1969 (as opposed to 0.98 during the period 1950-1960). Moreover, this rapid improvement in the labor absorbing ability of manufacturing coincided with an increase in the ability of total employment to absorb total labor force growth. While the percentage of the total Mexican population employed had declined from 32.35 per cent in 1950 to 31.43 per cent in 1960, the percentage of the total population employed in 1969 stood at 32.98 per cent.[13] It is also significant to note that manufacturing employment grew at a faster rate than service employment during the periods 1960-1965 and 1965-1969.

Several conclusions can be drawn for Latin America in general and Mexico in particular from the above analysis of the ability of industry to absorb a rapidly growing population, which is becoming increasingly urban. First, the rapid growth of population, and the rapid urbanization of that population in Latin America and Mexico has required and will continue to require rapid increases in industry's ability to absorb labor if the growth of marginally productive services and unemployment is to be avoided.

For Latin America in general, the growth of industry has not satisfied the needs for industrial growth. In fact, the ability of industry to absorb labor in Latin America diminished in recent years.

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[13] Calculated from Table 5 and Table 6.

The result has been a proliferation of service industries and rather high levels of unemployment.

Mexican industry exhibited the type of lethargy common to Latin American industry until 1950. From 1950 to 1960, however, the growth of Mexican industry, while still not satisfactory, showed a marked upswing. This occurred, unfortunately, during a downswing in the growth of alternative employment activities with the result that a smaller per cent of the Mexican population was employed in 1960 than in 1950.

The upswing in industrial employment which had occurred during the 1950's accelerated rapidly during the 1960's. During the period 1965 to 1969, increases in industrial employment were significantly exceeding increases in urban population. Also, this took place while increases in total employment were exceeding increases in total population.

It would appear, therefore, that unlike Latin America as a whole, Mexico has achieved a rate of industrial growth relatively sufficient to satisfy its employment needs for industrialization.

The performance of alternative economic activities

Industrial growth is not only important from the standpoint of providing employment to a growing population. Also to be considered is the stimulus to the general development of a nation afforded by

industrial growth.

The need for a high rate of industrial growth in Latin America as a stimulus to development is accentuated if one considers the performance of alternative economic activities (i. e., agriculture and the extractive industries) in stimulating development. Agriculture and the extractive industries as stimuli to development have been largely ineffectual for Latin America as a whole.

Growth in agricultural output during the period 1960 to 1967, as presented in Table 8, was marginal for all but two of the LAFTA members, Mexico and Venezuela whose average percentage increase in output for the period 1960-1967 were 4. 9 per cent and 5. 5 per cent respectively.

The slugishness displayed in agricultural production among LAFTA members is common to Latin America as a whole, and the seriousness of this poor performance by agriculture is reflected in the fact that agricultural production per inhabitant for Latin America declined by 8. 8 per cent from 1958 to 1966. [14]

It would appear that mining in Latin America has a potential for growth above that which has been achieved if it is considered that Latin America possesses twenty per cent of world reserves of bauxite, thirty per cent of world copper reserves, fifteen per cent

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[14] U. N., Economic Survey of Latin America, 1967, p. 200.

TABLE 8

GROWTH OF AGRICULTURAL OUTPUT
FOR LAFTA MEMBERS

Country	Average percentage increase in output for the period 1960-1967
Argentina	3.0
Bolivia	0.7
Brazil	2.9
Chile	1.9
Colombia	1.9
Ecuador	3.2
Mexico	4.9
Paraguay	2.2
Peru	1.2
Uruguay	-0.8
Venezuela	5.5

Source: United Nations, Department of Economic and Social Affairs, World Economic Survey, 1968, Part 2, (E/4688ST/ECA/119), 1970, p. 80.

of world tin reserves, eighteen per cent of world manganeze reserves, and approximately fifteen per cent of the world's iron, lead, and zinc reserves.[15] The performance of mining has, however, been rather poor. Mining, besides contributing little to employment[16] and

[15]United Nations, Economic Commission for Latin America, "Mining in Latin America," Economic Bulletin for Latin America, XIV, No. 2, 1970, p. 80.

[16]Mining employment as a percentage of total employment in 1965 was 0.3 per cent for Argentina, 0.4 per cent for Brazil, 3.9 per cent for Boliva, 3.5 per cent for Chile, 1.1 per cent for Colombia, 0.8 per cent for Mexico, 1.6 per cent for Peru, and 0.7 per

constituting less than six per cent of GDP for all but two of the major mining countries of Latin America, has grown at a rather slow rate.

Growth in mining production for Latin America averaged only 3. 8 per cent per year for the period 1960 to 1967.[17] But, even this slow rate of growth is deceivingly high if the individual countries' growth rates, as presented in Table 9, are considered. With six of the eight major producers in Latin America having annual growth rates of mining production less then the regional average 3. 8 per cent, and with two of the major producers (Colombia and Venezuela) actually showing substantial declines in mining production, it would appear that mining has not provided much of a stimulus to development in Latin America.

The performance of mining and agriculture in Mexico, within recent years, has displayed the sluggishness typical of these activities in Latin America as a whole. For agriculture, this represented a reversal of past performance. Mexico, in 1965, was the only country in Latin America self sufficient in food. Mexican agricultural production was considered the most efficient in Latin America as a

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cent for Venezuela. These facts are contained in United Nations, Economic Commission for Latin America, "Mining in Latin America," Economic Bulletin for Latin America, XIV, No. 2, 1970, p. 93.

[17] U. N., "Mining in Latin America," p. 84.

TABLE 9

MINERAL PRODUCTION FOR THE MAJOR MINERAL PRODUCING COUNTRIES OF LATIN AMERICA
(Petroleum excluded, 1963 prices)

Country	Per cent growth 1960-1967	Share of GDP 1958	Share of GDP 1967
Argentina	21.1	0.4	0.4
Bolivia	37.2	8.0	9.0
Brazil	94.0	0.2	0.5
Chile	27.1	7.0	6.5
Colombia	11.9	3.7	3.4
Mexico	8.6	2.3	1.5
Peru	8.8	4.0	4.2
Venezuela	17.0	1.8	1.3

Source: United Nations, Economic Commission for Latin America, Economic Survey of Latin America, 1967 (E/CN. 12/808/Rev. 1), 1969, p. 203.

result of massive land reform programs and irrigation projects in the north of Mexico. The growth of Mexican agricultural production from the period 1934-1938 to 1965 was an outstanding 224 per cent (Colombian agriculture achieved the second greatest growth--127 per cent--in Latin America).[18]

From 1960-1967 Mexico showed a rather respectable growth of agricultural production of 4.9 per cent per year.[19] In 1968,

[18]Edmund Flores, "From Land Reform to Industrial Revolution: The Mexican Case," The Developing Economies, VII, No. 1 (March, 1969), p. 83.

[19]Table 8.

however, the annual growth of agricultural production declined to 2.4 per cent, and in 1969 agricultural production increased by only an estimated 1.1 per cent.[20] This downward trend in the growth of agricultural production is also evident if the performance of the national account category of agriculture, forestry, and fishing is considered for the period 1960 to 1969. Annual growth in this category declined from an average annual growth of 4.3 per cent for the period 1960-1965 to 2.3 per cent in 1966 and 2.2 per cent in 1967.[21] As stated earlier, the main component of this category, agriculture, grew by only an estimated 1.1 per cent in 1969. Whether or not this decline in the growth rate of agricultural production represents a trend remains to be seen. It is evident, however, that with agriculture contributing less to Mexico's development, growth in other wealth producing sectors must be accelerated if a rapid rate of development is to be achieved and maintained.

It would not appear that the Mexican extractive industries will be capable of providing such a required growth rate. As it can be seen in Table 9, mineral production for Mexico was only able to increase a total of 8.6 per cent from 1960-1967. As a result the extractive industries' share (petroleum excluded) of GDP declined

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[20] "Report on General Economic Conditions in Mexico in 1969," Comercio Exterior de Mexico, XVI, No. 4 (April, 1970), p. 8.

[21] Table 6.

from 2. 3 per cent in 1958 to 1. 5 per cent in 1967. Although the performance of the extractive industries improved in 1968 and 1969, achieving annual growth rates of 5. 7 per cent and 6. 5 per cent respectively,[22] Mexico it appears will not be able to depend upon the extractive industries to stimulate development.

Put into a framework of generally poor performing alternative wealth producing economic activities, how has industry performed in stimulating economic development (the growth of GDP and per capita GDP)? For Latin America as a whole, the ability of industry to stimulate the growth of GDP has declined with the result that the growth rates of GDP and per capita GDP have declined over the past three decades.

The average annual growth of Latin American GDP and industrial product, as shown in Table 10, have been declining since 1940 from 5. 0 per cent and 6. 8 per cent respectively for the period 1940-1950 to 4. 5 per cent and 5. 4 per cent respectively for the period 1960-1968. The industrial coefficient (annual growth of industrial product over annual growth of GDP) has also been declining, 1. 4 for the period 1940-1950 to 1. 2 for the period 1960-1968. Therefore, not only has the dynamism of overall development and industrialization diminished, but the relative ability of industry to stimulate

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[22] "Report on General Economic Conditions in Mexico in 1969," Comercio Exterior de Mexico, XVI, No. 4 (April, 1970), p. 8.

TABLE 10

THE STIMULUS OF LATIN AMERICAN INDUSTRY TO DEVELOPMENT
(1950 Prices)

Period	Per cent average annual growth of GDP-Latin America	Per cent average annual growth of GIP-Latin America	Industrial coefficient Col. 3 / Col. 2
1940-1950	5.0	6.8	1.4
1950-1960	4.7	6.3	1.3
1960-1968	4.5	5.4	1.2

Source: United Nations, Economic Commission for Latin America, "Industrial Development in Latin America, "Economic Bulletin for Latin America, XIV, No. 2, 1970, p. 5.

overall development, and the stimulus provided by the domestic market to industry have also diminished for Latin America as a whole. This trend, experienced by every country of Latin America except for Colombia, Peru, and Mexico, has prompted the ECLA evaluation that industry, under present conditions, is no longer a driving force of development in most of Latin America.[23]

Significantly, the decline in the growth of industrial product has affected nearly all branches of industry in Latin America, with consumer goods showing the poorest performance. Average annual growth rates of major industries for the periods 1955-1960,

[23] U. N., "Industrial Development in Latin America," p. 5.

and 1960-1965 respectively were as follows: food, beverages, and tobacco, 4.4 per cent and 4.0 per cent; textiles, 3.2 per cent and 2.8 per cent; petrochemicals, 10.0 per cent and 8.8 per cent; basic metal, 9.0 per cent and 8.0 per cent; metal transformation and transportation equipment, 15.0 per cent and 7.3 per cent.[24]

This downward trend in the growth of Latin America's GDP and gross industrial product has obviously had serious effects on the growth of per capita product for the region, considering the regional population growth rate has fluctuated around 2.8 per cent per year in recent years.

For six of the eleven LAFTA members listed in Table 11, per capita product growth rates were higher for the period 1950 to 1955 than for the period 1960 to 1965. For the period 1960 to 1965 only two of the eleven LAFTA members (Mexico and Bolivia) had per capita product growth rates exceeding two per cent, and only two countries (Mexico and Bolivia) had per capita product growth rates exceeding two per cent for each of the years from 1966 to 1968. The pattern of per capita product growth for Latin America as a whole shows a steady slowdown, most severe during the period 1955 to 1960 (the five year period preceeding the formation of LAFTA). Conditions

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[24] Harvey S. Perloff, Alliance for Progress: A Social Invention in the Making (Baltimore: Johns Hopkins Press, 1969), p. 72.

TABLE 11

GROWTH OF GDP PER CAPITA FOR LATIN AMERICA
(Constant 1960 prices)

Country or region	Average annual growth of GDP per capita					
	1950-1955	1955-1960	1960-1965	1966	1967	1968
Argentina	1.4	0.9	1.7	-1.9	0.5	2.0
Bolivia	-1.8	-2.9	2.6	3.9	3.1	4.6
Brazil	2.5	2.9	1.5	1.3	1.7	3.0
Chile	0.9	1.0	1.8	3.4	1.0	1.3
Colombia	2.3	1.1	1.0	2.3	0.5	2.3
Ecuador	2.2	1.2	1.2	2.1	2.5	1.1
Mexico	2.9	2.7	2.6	3.9	3.8	3.9
Paraguay	0.3	-0.1	1.2	-0.2	0.2	2.3
Peru	2.6	2.0	2.7	2.3	0.4	0.1
Uruguay	2.8	-1.1	-0.1	1.4	-3.3	1.8
Venezuela	4.6	2.4	1.2	-1.2	0.1	1.9
Latin America	2.4	1.8	1.7	1.6	1.6	2.5

Note: Data for 1968 is provisional.

Source: Calculated from: United Nations, Economic Commission for Latin America, Economic Survey of Latin America, 1967 (E/CN. 12/808/ Rev. 1), 1964; "Economic Roundup for Latin America," Comercio Exterior de Mexico, XIV, No. 4 (April, 1969), p. 19; "Economic Roundup for Latin America," Comercio Exterior de Mexico, XVI, No. 3 (March, 1969), p. 20.

seemingly improved in 1968, and preliminary estimates indicate that per capita product grew by 2.9 per cent for Latin America in 1969.[25] It is too early, however, to tell if a new upward trend is developing.

[25] "Latin America: Economic Recovery and Social Problems," Comercio Exterior de Mexico, XVI, No. 5 (May, 1970), p. 2.

It is also interesting to note that in 1968, while per capita product increased for the region by an improved 2. 5 per cent, thirteen of the twenty Latin American Republics had growth rates below 2. 5 per cent.[26] Therefore, this mild recovery was shared only by a minority of Latin American countries.

With industrial growth increasingly contributing proportionately less to GDP over the past three decades, and with other wealth producing activities showing little growth, it would appear the OAS minimum goal of a national 2. 5 per cent growth in per capita income is presently beyond the ability of most of the Latin American nations to achieve. The major exception to this observation is, however, Mexico.

Mexico, as seen in Table 3, experienced the greatest real growth, forty-two per cent, of GNP of all LAFTA members for the period 1963 to 1968. Mexico's percentage growth of GNP was nearly three times greater than the GNP growth of Argentina and Brazil, who along with Mexico generate 58. 7 per cent of Latin America's GNP. Mexico was, moreover, the only LAFTA country able to exceed the OAS goal of a 2. 5 per cent annual per capita product increase for all three of the five year periods indicated in Table 11.

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[26] "Latin America Recovers," Comercio Exterior de Mexico, XVI, No. 3, (March, 1970), p. 3.

The growth of Mexico's GNP has not exhibited the long term downward trend that has been common to Latin America as a whole. Growth of GNP, as calculated from Table 12, for the period 1950 to 1960 was the same as growth of GNP for the period 1940 to 1950 (80 per cent). Also, the average annual growth of GNP for the period 1960 to 1968, as calculated from Table 12, was 6.53 per cent as compared to an average annual increase in GNP of 6.15 per cent for the period 1950 to 1960. While maintaining the relatively high growth rates of GNP fostered by the Second World War during the 1950's, Mexico was able to accelerate the growth of GNP for the period 1960 to 1968.

The growth of industrial production (manufacturing) has also shown a long run tendency to accelerate over the past two decades. The average annual growth of industrial production increased from 6.60 per cent for the period 1950-1955, to 8.10 per cent for the period 1955-1960, slipping to 7.82 for the period 1960-1965, and up to 8.80 for the period 1965-1969.[27]

The structure of industrial growth

Several aspects of the acceleration in the growth rate of Mexican industry are important to examine. Referring to Table 13,

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[27] Industrial growth rates for 1950-1960 are from; OAS, The Alliance for Progress and Latin American Development Prospects: A Five Year Review, 1961-1965, p. 31. Data for the period 1960-1967

TABLE 12

MEXICO'S ECONOMIC DEVELOPMENT SINCE 1940
(In Billions of Pesos)

Year	Real GNP (1950 prices)	Annual Growth rate of GNP	GNP per capita Growth rates
1940	22.6	. .	. .
1945	30.5	. .	. .
1950	40.6	. .	. .
1951	43.6	7.4	4.3
1952	45.4	4.1	0.8
1953	45.6	0.5	- 2.4
1954	50.4	10.5	7.9
1955	54.8	8.7	5.6
1956	58.2	6.2	3.1
1957	62.7	7.7	4.6
1958	66.2	5.6	2.3
1959	68.1	2.9	- 0.1
1960	73.5	7.9	4.6
1961	76.0	3.4	0.1
1962	79.7	4.8	1.6
1963	84.7	6.3	3.0
1964	93.2	10.0	6.6
1965	98.2	5.4	2.1
1966	105.6	7.5	3.9
1967	112.4	6.4	3.8
1968	120.4	7.1	3.9

Note:

Data for 1968 is provisional. The Banco Nacional's data, while originally taken from government sources, tends to underestimate official government data due to their own corrections. This data will, therefore, be used to indicate general trends rather than to provide specific examples.

Source: "The Cycles of Our Economy," Review of the Economic Situation in Mexico, No. 524 (July, 1969), p. 4.

TABLE 12--Continued

Investment (Current prices)					
Total Investment		Private Investment		Public Investment	
total	annual growth rate	total	annual growth rate	total	annual growth rate
0.7	. .	0.5	. .	0.3	. .
2.2	. .	1.3	. .	2.7	. .
6.0	. .	3.3	. .	2.7	. .
6.7	11.7	3.9	18.2	2.8	3.7
8.0	19.4	4.7	20.5	3.3	17.9
7.7	3.7	4.6	- 2.1	3.1	- 6.1
9.6	24.7	5.4	17.4	4.2	35.5
12.0	25.0	7.6	40.7	4.4	4.8
13.7	14.2	9.1	19.7	4.6	4.5
15.7	14.6	10.1	11.0	5.6	21.7
17.0	8.8	6.0	6.2	10.7	
17.4	2.4	10.9	0.9	6.5	4.8
23.2	33.3	14.4	32.1	8.8	35.4
22.6	- 2.6	12.3	-14.6	10.3	17.0
24.8	9.7	13.4	8.9	11.4	10.7
28.0	12.9	13.6	1.5	14.4	26.3
36.7	31.1	19.1	40.4	17.6	22.2
38.7	5.4	22.6	18.3	16.1	- 8.5
45.5	17.6	24.8	9.7	20.7	28.6
47.7	4.8	25.6	3.2	22.1	6.8
63.5	33.1	39.0	52.3	24.5	10.9

TABLE 13

STRUCTURAL CHANGES AMONG SELECTED MEXICAN INDUSTRIES
(Percentages based on Constant Pesos)

Selected industries	Per cent growth	Per cent growth	Share of total production of listed industries		Projected share of production of listed industries
	1950-1960	1960-1966	1960	1966	1970
Food, beverages and tobacco	95	51	40.0	36.5	29.7
Textiles	39	48	14.3	12.8	9.1
Paper, paper products	92	71	2.9	3.0	2.5
Chemicals	235	92	12.1	14.0	25.1
Basic metals and metal production	257	71	18.7	19.3	21.0
Machinery	154	83	7.3	8.1	8.0
Transportation equipment	124	124	4.7	6.4	4.6

Sources: United Nations, Economic Commission for Latin America, Statistical Bulletin for Latin America, V, No. 2, 1969, p. 144; Projected shares are from "The Structure of Mexico's Industry," Review of the Economic Situation of Mexico, Banco Nacional de Mexico, Vol. XIV, Nos. 519-520 (February and March, 1969), p. 11

it is observed that Mexican industrial growth has been uneven to the extent that the share of industrial production for the major industries listed in Table 13 for consumer non-durable goods such as food, beverages, tobacco, and textiles, have been declining. These four products constituted 54.3 per cent of the total industrial product in 1960, but their share had declined to 49.3 per cent by 1966, and this share is projected to be 36.8 per cent by 1970. This decline in the consumer non-durable goods share of total production for the selected major industries has not been due to a slowing down of their rate of growth, which has in fact increased, but their declining share is rather due to the very high rates of growth achieved by the more sophisticated industrial products listed.

As a point of comparison, growth of food, beverages, and tobacco averaged 7.16 per cent growth per year while total manufacturing grew at an average annual rate of 8.23 per cent for the period 1960 to 1966.[28] This represents a reversal of these products for the period 1948 to 1960, when the growth of food, beverages, and tobacco was faster than the growth of total manufacturing (239 per cent versus

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is from Table 13. Estimated industrial growth rates for 1968 and 1969 are from "Report on General Economic Conditions," Comercio Exterior de Mexico, XVI, No. 4 (April, 1970), p. 6.

[28]Computed from Table 13.

230 per cent).[29] It would appear based on these selected major industries that industrialization, rather than being based on the rapid development of consumer non-durable goods, has instead received its main impetus from more sophisticated industries, such as chemicals, basic metals, and metal production, machinery, and transportation equipment. This trend is also evident for Latin America as a whole. Food, beverage, and tobacco production constituted 35.9 per cent of Gross Industrial Product (GIP) for Latin America in 1950, but their production constituted only 26.3 per cent of gross industrial production in 1968. Textiles, footwear, and clothing constituted 23.2 per cent of Latin American GIP in 1950, and 13.7 per cent of Latin American GIP in 1968.[30] The difference between the experience of Mexico and Latin America, however, is that the restructuring of Mexican industry has taken place while industrial growth has been accelerating while Latin America's restructuring of industry has taken place while industrial growth has been slowing down.

The dilemma

A second aspect of the acceleration of industrial growth in Mexico that bears investigation has to do with what Raymond Vernon

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[29]United Nations, Economic Commission for Latin America, Statistical Bulletin for Latin America, V, No. 2, 1969, p. 144.

[30]U. N., "Industrial Development in Latin America," p. 5.

termed the "Dilemma" of Mexico's development. Several authors, such as Raymond Vernon, writing during the period 1960-1963, felt that Mexico's industrialization and development was approaching stagnation. In the light of the afforementioned long run acceleration of the growth rates of industry and GDP, the logic of their observations, at first thought, is somewhat difficult to comprehend.

Their observations were largely based on the following factors. First, they felt that the constraints restricting the further use of "inward" tools of industrialization in Mexico were rapidly being reached. These constraints, as mentioned before, took the form of: (1) a regressive pattern of income distribution limiting the effectiveness of the domestic market to stimulate industrialization; (2) a low import coefficient limiting the possibilities of further IS, especially for consumer goods; (3) a domestic market too small to allow for the creation of efficient capital goods industries; and (4) a poor performing export sector incapable of providing a satisfactory level of needed foreign exchange for the purchase of capital goods essential to further industrialization.

To Raymond Vernon the fact that these constraints were being rapidly reached was evident from two observations. First, Mexican industry was operating at rather low levels of capacity in the early 1960's as borne out by a study by Comercio Exterior in 1963 which claimed that fifty per cent of Mexican industry was

operating at under capacity.[31] This was viewed as evidence that the domestic market was not expanding rapidly enough to absorb growth in industrial output. It could however, also be viewed as evidence that manufacturers were poor judges of domestic demand. The high costs of Mexican industrial products, especially consumer durable goods and capital goods, as documented in studies conducted by the ECLA was attributed to both an underutilization of capital, and the narrowness of the domestic market which precluded the achievement of potential economies of scale.[32] The presence of these factors, supposidly resulting from the aforementioned constraints, were interpreted, to the degree that they existed, as signs of an inpending stagnation of industrial growth and development.

From the viewpoint of Raymond Vernon writing in the early 1950's, it would appear that the growth of Mexico's economy was indeed slowing. Referring to Table 13, it can be seen that from 1955 to 1962 the growth of Mexico's GNP and per capita GNP was experiencing a downward movement. This is more easily seen by first looking at the behavior of the growth of private investment for this period. From a high private investment growth rate of forty per cent

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[31] "Editorial," Comercio Exterior de Mexico, IX, No. 3 (March, 1963), p. 138.

[32] U. N., The Process of Industrial Development in Latin America, pp. 130-145.

in 1955, the annual private investment growth rate declined to 0. 9 per cent in 1959. Growth of private investment recovered in 1960 by expanding by 32. 1 per cent, but total private investment declined by 14. 6 per cent the following year. Increased rates of public investment tended to reduce the effects of the decline of private investment, during this period but with the result that while in 1955 public investment constituted only 36. 6 per cent of total investment, it constituted 51. 4 per cent of total investment in 1963. The fact that per capita GNP in Mexico grew by less than the OAS goal of 2. 5 per cent growth per year in 1958, 1959, 1961, and 1962 was understandable viewed with great concern.

If the growth of manufacturing is viewed from the periods 1953-1958 and 1958-1963 rather than the periods 1955-1960 and 1960-1965, as was done earlier, a significant slowdown in industrial growth is evident.

While the average annual growth of industrial output was 10. 7 per cent for the period 1953-1958, it was 7. 4 per cent for the period 1958-1963. The food and beverage industry which had grown at an average annual rate of 7. 4 per cent during the period 1953-1958, grew at an average rate of 6. 2 per cent per year for the period 1958-1963. Average annual growth in textiles was 6. 2 per cent and 3. 9 per cent for the two respective periods. Average annual growth in tobacco product output was 4. 0 per cent and 1. 0 per cent for the two

respective periods.[33]

If we add the facts that industrial absorption of labor was not keeping pace with population increases during the period 1958-1963 and Mexico's commodity terms of trade had declined from 100 in 1958 (using an index where 1958 = 100) to 92 in 1962 to the above observations,[34] it is not unreasonable that Raymond Vernon felt that Mexico was facing a serious dilemma. With private investment growth slowing down supposedly because of a lack of investment opportunities due to an already low import coefficient and too narrow a domestic market for the production of sophisticated manufactured goods, how was Mexico to revitalize its development growth?

Raymond Vernon alluded to Mexico's participation in LAFTA as one way of escaping from this dilemma. Philippe C. Schmitter and Ernst B. Haas also observed that this decline in the growth of Mexico's industry and development was a strong motivation in Mexico's decision to join LAFTA. In discussing this dilemma they observed that,

> . . . for those committed to the rapid and forceful resumption of the development process, additional alternatives seemed desirable. Unable to rely exclusively on successful planning . . . certain of the

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[33] United Nations, Department of Economic and Social Affairs, The Growth of World Industry, 1953-1965 (ST/STAT/SER. P/4), 1967, pp. 299-300.

[34] See Table 36 in Chapter III.

> techniques apparently felt that the regional market would offer opportunities for growth which would provide answers to Mexico's immediate difficulties. We suspect that if Mexican national planning has been fully successful before 1959 these technicos might have been less ready to open Mexico up to the unpredictable winds of regional change.[35]

Mexico's development since 1963: Industrial and developmental planning

Obviously, the stagnation of Mexican industry and development as feared by Raymond Vernon, did not materialize. Mexico has, in fact, significantly accelerated industrial growth and development. Mexico was apparently also able to generate a satisfactory industrial labor absorption rate, a pressing problem in the 1950's.

One explanation for Raymond Vernon's somewhat erroneous observations lies in Mexico's business cycle which appears to revolve around the Presidential election in Mexico.

Referring to Table 12 it appears that there was a cyclical movement around the Presidential election years of 1952, 1958, and 1964. Growth rates in private investment and GNP tended to peak around these years, followed by a decline in growth until the next Presidential year. It is quite possible that the cyclical downswing after 1955 was erroneously interpreted by some as being a secular movement toward stagnation.

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[35] Philippe C. Schmitter and Ernst B. Haas, Mexico and Latin American Economic Integration, p. 16.

Raymond Vernon's analysis is not, however, to be dismissed so lightly. The constraints to industrialization and development mentioned by Raymond Vernon, as it will be shown, still exist in Mexico and in some cases they have intensified. For Latin America as a whole, the presence of these constraints has, in fact, contributed to a long-run deterioration of industrial growth.

Mexico has been, however, able to accelerate industrial growth and development growth despite the presence of these constraints. One major reason for Mexico's ability to accelerate the growth of its economy in recent years has been the proximity of Mexico to the United States. In 1969 border tourism and in-country tourism yielded a gross revenue of 15. 1 billion pesos to Mexico. This revenue represented 43. 5 per cent of the external sectors total gross current account income of 34. 8 billion pesos and 4. 2 per cent of an approximate GNP of 355. 7 billion pesos in 1969.[36]

Mexico's Programa de Industrializacion Fronteriza (The Border Industry Program) and similar programs to further industrialize the North of Mexico have been very successful. The need for such programs was intensified in 1964 when the migrant worker (bracero) program was terminated by the United States in 1964, causing high

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[36]"Report of General Economic Conditions in Mexico in 1969," Comercio Exterior de Mexico, XVI, No. 4 (April, 1970), p. 7.

levels of unemployment in the North of Mexico.

The Programa de Industrializacion Fronteriza, established in 1965, represents a new attitude toward foreign investment on the part of Mexico. While placing severe restrictions on direct foreign investment in the interior, and while limiting foreign ownership of Mexico industries to forty-nine per cent in most cases, Mexico has granted concessions to United States firms to establish processing and assembly plants within twelve miles of the border to take advantage of cheaper labor costs in Mexico. The result has been that 147 new plants representing an authorized investment of 14.2 million dollars had been drawn to the area by 1969.[37]

Total U. S. direct investment has, despite Mexican restrictions on foreign investment, shown considerable growth since 1963. The proximity of Mexico to the United States is certainly to be considered a major factor in this growth. United States direct foreign investments to Mexico, in current prices, increased from 907 million dollars in 1963 to 1459 million dollars in 1968, an increase of 60.9 per cent as shown in Table 14. This growth in United States' direct investment to Mexico was nearly twice as great as the total per cent increase in United States' direct investment to Latin America for that

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[37] Lacy H. Hunt, "Industrial Development on the Mexican Border," Business Review, Federal Reserve Bank of Dallas (February, 1970), p. 6.

TABLE 14

UNITED STATES' DIRECT INVESTMENT IN LATIN AMERICA, 1963-1968
(Current U. S. Prices)

Sectors and Countries	Total Investment Millions of U. S. dollars 1963	1968
Manufacturing		
Argentina	454	729
Brazil	664	1,021
Mexico	502	998
Total Latin America	2,213	3,990
Petroleum		
Mexico	65	44
Total Latin America	3,636	3,643
Mining and Smelting		
Mexico	116	112
Total Latin America	1,303	1,875
All Sectors		
Argentina	829	1,148
Brazil	1,132	1,484
Mexico	907	1,459
Total Latin America	9,891	12,989

Note:
"Investment" represents book values after adjustments due to changes in valuation of assets, profits and losses on liquidations, and transfers.

Source: "U. S. Direct Investment in Latin America," Business Latin America, November, 13, 1969, p. 364.

TABLE 14--Continued

Annual increase in investment (Millions of dollars) 1964	1965	1966	1967	1968	Total 1964-1968	Per cent increase in investment
43	120	39	22	51	275	60.6
9	50	123	47	128	357	53.8
105	149	46	88	108	496	98.8
- 9	- 8	- 6	2	. .	- 21	-32.3
75	-165	- 71	- 3	171	7	0.2
12	- 24	4	- 8	12	- 4	- 3.4
45	76	91	193	167	572	43.9
54	109	43	47	66	319	38.5
-138	80	173	80	157	352	31.1
128	147	66	95	116	552	60.9
427	518	612	596	945	3,098	31.3

period. Moreover, most of this investment was directed into manufacturing. The increase in United States direct investment in Mexican manufacturing represented 89. 85 per cent of the total increase of total United States direct investment in Mexico for the period 1963-1968.

While a case can certainly be made for attributing some of Mexico's accelerating economic growth to the proximity of Mexico to the United States, the greatest stimulus to economic growth has undoubtedly been the political stability of Mexico and the effectiveness of Mexico's development planning.

It is difficult to separate the public sector from the private sector in Mexico because of the degree to which the former interacts with the latter. Besides indirectly managing many industries, the government owns the petroleum industry, most electrical power companies, the railroad industry, Altos Hornos de Mexico, S. A. (steel), and Aeronaves de Mexico, S. A. (aviation). The Mexican government through its program of "Mexicanization" also has considerable control over the ownership of private industry if that ownership is foreign. "Mexicanization" is still an active force as a government decree on July 25, 1970 which declared that firms in the steel, cement, glass, fertilizer, cellulose, and aluminum industries must have fifty-one per cent Mexican ownership, will verify.[38]

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[38]"New Mexicanization Decree to Have Far Reaching Consequences," Business Latin America, July 23, 1970, p. 6.

The Mexican government's influence on industrialization and development is greatest, however, in the areas of industrial promotion through price controls, tax exemptions and subsidies, and through the promotion and regulation of investment. Moreover, Mexico has been able to develop long range consistent planning due to the political stability of Mexico and the ability of Mexico's one political party (other parties exist but they have no significant power) to direct the various interest groups of the nation to a common course of action.

In the area of direct government promotion of industry, the Ley de Fomento de Industrias Nuevas y Nesesarias (The Law for the Promotion of New and Necessary Industries) of 1954 offers up to a forty per cent tax exemption for up to ten years for new or necessary industries. The Programa Nacional Fronterizo, instituted in 1961, offers tax exemptions and up to fifty per cent rebates on rail freight for industries selling products in the border area. Firms manufacturing goods for export receive exemptions from export taxes, permanent subsidies, reductions on taxes for imported raw materials and capital federal tax exemptions, and up to fifty per cent rebates on rail freight.[39] The government also publishes lists of imported products for which domestic production might be substituted under

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[39]"Industrial Promotion," Review of the Economic Situation of Mexico, XLV, No. 528 (November, 1969), p. 15.

protection. The National Productivity Center offers technical assistance to industry and promotes the adoption of new technology through subsidy. The degree to which Mexican industry has absorbed new technology has been indicated by a marked increase in worker productivity and the rapid growth of remittances of royalties and other payment for technical services to foreign countries.[40]

Mexico's ability to promote capital formation through both public and private investment has certainly been a major factor promoting the high growth rates of industry and GDP.

As it can be seen from Table 12, public investment (in current prices) increased at an average annual rate of 16.6 per cent from 1960 to 1968 as compared to an average annual rate of increase of 10.8 per cent for the period 1950 to 1960. The public investment program for 1969 assigned forty per cent of its 27.5 billion peso budget to industrial promotion. In keeping with the government's emphasis on industrialization, approximately thirty-three per cent of total budgeted federal expenditures of an estimated forty billion pesos for 1969 were applied to economic development with an additional sixteen per cent

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[40] In an United Nations report on the progress of a study on the transfer of technology to Mexico it was cited that remittances on technology transfers grew at an average annual rate of 13.3 per cent for the period 1959-1962, with such remittances representing 39.4 per cent of total foreign remittances of 123 million dollars in 1962. It was felt that this per cent was highly underestimated. United Nations, Economic and Social Council, Arrangements for the Transfer of Operative Technology to Developing Countries, Progress Report of the Secretary General (E/4452/ADD.3), March, 1968, p. 7.

applied to communications and transportation.[41]

The government promotes private capital formation in several ways. The Plan for Immediate Action for the period 1963 to 1965 is an example of joint public and private investment planning. This joint plan instituted in 1963 called for an immediate eighty billion peso infusion of investment funds into key sectors of the economy in response to the slowdown in Mexico's growth during the period 1958 to 1962.

This investment was approximately half public and half private. The public sector scheduled 37. 9 per cent of its investment for industrial development, and the private sector scheduled 40. 6 per cent of its investment share for industrial development.[42] Mexico also allows significant tax reductions on reinvested retained earnings and liberal depreciation allowances for key industries. As a result, it has been estimated that major firms reinvest an average of eighty per cent of their earnings.[43]

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[41]"Budget, Investment, Economic Policy, and Outlook for 1969," Comercio Exterior de Mexico, XVI, No. 2 (February, 1969), p. 3.

[42]Joseph S. LaCascia, Capital Formation and Economic Development in Mexico (New York: Frederick A. Praeger, 1969), p. 23.

[43]Antonin Basch, Financing Economic Development (New York: Macmillan Company, 1964), p. 213.

The government's most important means of promoting private investment, however, is found in Mexico's financial institutions. The performance of Mexico in its organization of development financing through these institutions, within a broad framework of financial and monetary stability, has been a key factor in Mexico's growth. The largest financial institutions are the Banco de Mexico (the central bank) and Nacional Financiera, S. A. (the national development bank instituted in 1934). The Banco de Mexico controls credit and, either directly or indirectly, provides funds for development programs. The Banco de Mexico also provides considerable technical aid to various development programs.

Nacional Financiera, S. A. operates to channel savings into capital formation by means of security issuances backed by the Banco de Mexico. Nacional Financiera, S. A. as a development bank finances infrastructure and industrial development, and offers technical aid to industry. In this capacity Nacional Financiera, S. A. offers long-term credits to industries for establishment and expansion, and in some cases wholly develops high risk industries to be sold out to private interests once they are established.[44] Total financing by Nacional Financiera, S. A. grew from 13. 6 billion pesos in 1960 to 26. 5 billion pesos by 1966. The average annual increase in Nacional

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[44]LaCascia, Capital Formation and Economic Development in Mexico, p. 41.

Financiera, S. A. financing of 12.6 per cent for the period 1960 to 1966 was certainly a major factor in Mexico's development during this period.[45]

Mexico also possesses a highly developed and regulated private banking system consisting of commercial banks and industrial development banks (financieras) serving to promote capital formation.

The impact of these financial institutions and investment promotion policies in recent years is reflected by the fact that gross fixed investment as a per cent of GNP increased from 14.8 per cent in 1950 to 15.1 per cent in 1960 to 20.0 per cent in 1969.[46] This increased investment was, moreover, achieved with relative price stability in Mexico (prices rose at an average annual rate of 3.4 per cent for the period 1963 to 1969).[47]

How was the dilemma of Mexico's development overcome? It would appear that Mexico's accelerated growth since 1963 has been achieved not so much by a removal of those constraints limiting the extent to which "inward" instruments of development can be effectively used as it was achieved by a more efficient and effective use of the "inward" tools within those constraints.

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[45] Ibid., p. 40.

[46] IMF, International Monetary Statistics, XXIII, No. 6 (June, 1970), pp. 218-221.

[47] Ibid.

Demand elements of growth

The most dynamic demand elements of development growth, as shown in Table 15, for the period 1963 to 1968 were gross fixed investment and public consumption. Although private consumption showed considerable expansion, 68.8 per cent for the period, gross fixed investment and public consumption expanded by 113.8 per cent for the period. Gross fixed investment and public consumption as a per cent of private consumption increased from 26 per cent in 1963 to 33 per cent in 1968.

While public investment had been the most dynamic element of Mexico's demand growth from 1958-1963 (public investment increased by 132.2 per cent during this period as compared to 25.9 per increase in private investment for that period as computed from Table 12), private investment increased at a rate (186.8 per cent) twice as great as the rate of increase in public investment (80.1 per cent) during the period 1963-1968. One major factor accounting for this growth must certainly have been Mexico's political and economic stability, and the effectiveness of Mexico's development planning.[48]

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[48]Joseph S. LaCascia in Capital Formation and Economic Development in Mexico, op. cit., presents a convincing case for attributing most of Mexico's growth after 1963 to the effectiveness of Mexico's financial institutions in promoting investment and industrialization.

TABLE 15

MEXICO'S ECONOMIC GROWTH: 1963-1968
(Current Prices
Billions of Pesos)

	1963	1968	Total per cent Change 1963-1968
Supply			
GDP	194.8	340.6	74.8
Imports	20.9	33.9	62.2
Demand			
Exports	20.9	31.1	48.8
Gross fixed investment	28.0	63.5	126.8
Private	13.6	39.0	186.8
Public	14.4	24.5	70.1
Total consumption			
Private	152.3	257.1	68.8
Public	11.2	20.3	80.3

Note:
Factor payments abroad and increases in stocks have been omitted. Total supply does not, therefore, equal total demand.

Source: International Monetary Fund, International Financial Statistics, XXIII, No. 6 (June, 1970), p. 220, and Table 12.

Supply elements of growth

Henry J. Bruton in his article "Productivity Growth in Latin America"[49] discussed the effects of high rates of capital formation, such as those achieved by Mexico, on the growth of productivity of the factors of production and on production itself. He observed that there exists a very strong relationship between capital growth and growth of GDP in most developed and less-developed countries. This relationship does not exist, however, for the larger Latin American countries with the exception of Mexico.

One of the reasons for the slow growth of GDP in those countries studied was their low level of productivity growth which was virtually zero for the period 1955-1964 for Latin America as a whole (in the case of Argentina it was negative).[50] The reasons for this low productivity growth were cited as: (1) a growing inappropriateness of the input mix of production favoring a rapid accumulation of capital due to factor market defects; (2) a growing inappropriateness of the composition of output in that productive activity was not based on cost considerations but rather it was based on protectionalist policies; and (3) a decline in competition.[51]

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[49]Henry J. Bruton, "Productivity Growth in Latin America," American Economic Review, LVII, No. 5 (December, 1967), p. 1103.

[50]Ibid., p. 1115.

[51]Ibid.

Professor Bruton's analysis was based on the relationship: $r_p = r_a + ar_k + br_l$, which represents the logarithmic differentiation of the Cobb-Douglas production function. The notations r_p, r_a, r_k, and r_l refer to annual proportionate rates of growth of GDP, productivity, capital, and labor. Defining productivity in this way, i.e., as a residual factor representing growth in GDP not explained by increases in factors, allows a determination of the degree to which factor quality is improved and factors are better utilized. Productivity in this sense might be interpreted as including technology, education, planning, etc. The notations a and b refer to the share of output accruing to capital (0.50 for Mexico according to Professor Bruton) and the share of output accruing to labor. Table 16 gives the results of Professor Bruton's application of this relationship to the countries listed.

As a point of comparison to the data listed for r_a and r_a/r_p in Table 16, the average r_a and r_a/r_p for twelve developed countries studied was 2.8 and 0.58 respectively.[52] The overall average r_a and r_a/r_p for the Latin American countries in Table 16 was 1.4 and 0.26 respectively. Apparently, productivity growth as a determinin-ant of growth of GDP was relatively insignificant in the Latin American countries as a whole in comparison to the developed countries.

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[52] Ibid., p. 1102.

Moreover, productivity actually declined in Argentina and Brazil from 1955 to 1963.

Professor Bruton's findings are largely contrary to the belief that underdeveloped countries in their period of modernization with high rates of capital formation can achieve rapid productivity increases. In the case of the Latin American countries, except for Mexico, high rates of capital formation were associated with low rate of productivity growth.

The lack of a significant and positive relationship between r_a and r_k was also found by Bruton in the developed countries, but for different reasons. Growth of productivity in the developed countries was found to be an autonomous technological factor. Growth in productivity for the Latin American countries was found to be significantly related to growth in GDP.[53]

The significance of this relationship becomes clear after investigating the nature of capital formation in Latin America. High levels of capital formation in Latin America are promoted in several ways. First, overvalued currencies in the Latin American countries make capital imports more attractive than increased labor usage as a means of increasing output than would be true if such overvaluation did not exist. Under protectionalist import substitution, products

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[53] Ibid., p. 1109.

TABLE 16

GROWTH RATES OF INPUTS, OUTPUTS, AND PRODUCTIVITY IN SELECTED LATIN AMERICAN COUNTRIES

Country and period	r_p	r_k	r_l	r_a	r_a/r_p
Argentina					
1940-1945	2.9	0.0	2.1	1.6	0.55
1946-1951	3.4	3.9	2.4	0.4	0.12
1955-1959	1.7	3.4	1.5	-0.6	-0.35
1960-1964	1.2	4.6	0.0	-0.6	-0.50
Brazil					
1940-1945	3.2	2.2	1.7	1.3	0.41
1946-1953	5.6	5.9	2.4	1.6	0.29
1955-1959	5.6	5.2	2.8	1.7	0.30
1960-1963	5.0	5.1	2.8	1.2	0.24
Chile					
1940-1945	2.7	0.9	1.8	1.4	0.52
1946-1953	3.9	3.0	2.1	1.4	0.36
1955-1959	3.0	3.4	2.5	0.1	0.03
1960-1964	4.0	4.8	1.4	0.9	0.23
Colombia					
1940-1945	2.8	1.5	1.8	1.1	0.39
1946-1953	5.2	4.0	2.1	2.3	0.44
1955-1959	4.0	4.9	2.6	0.4	0.10
1960-1964	4.5	4.3	2.0	1.5	0.33
Mexico					
1940-1945	9.0	1.7	2.8	6.7	0.74
1946-1953	5.0	4.9	2.6	1.2	0.24
1955-1959	5.7	4.2	3.1	2.0	0.35
1960-1964	6.2	4.2	2.5	2.8	0.45
1965-1969*	6.8	3.9	3.4	3.1	0.46

Notes:

*Data for the period 1965-1969 for Mexico was derived using Professor Bruton's factor shares estimates and depreciation on r_k estimates applied to IMF data.

Source: Henry J. Bruton, "Productivity Growth in Latin America," American Economic Review, LVII, No. 5 (December, 1967), Table 1, p1103, International Monetary Fund, International Financial Statistics, XXIII, No. 6 (June, 1970), pp. 218-220.

requiring high levels of capital in their production, such as automobiles, are developed with the result that production depends on a continual flow of capital imports. These new industries are characterized as capital-intensive even though national factor proportions indicate a desired labor intensity. Because of the producers often monopolistic sheltered position there exists little incentive to increase productivity in that high costs are readily absorbed by a strong internal demand.[54]

The ECLA has also cited that the effect of factor market disruptions, caused by overvalued currencies and government subsidies to capital imports by IS industries, has been a very high industrial preference for capital usage to expand output in Latin America.[55]

Industry, developed in the manner described above, operates under conditions of over-capacity, i.e., underutilization and capacity. This underutilization is not due to a lack of demand. Instead, such industry operates under conditions of over capacity because it has little financial incentive to use its capital more intensely. Growth in productivity (r_a) is then to be associated with a better utilization of capacity rather than an expansion of that capacity through high levels of investment. It is, therefore the proportionate growth of

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[54] Ibid., p. 1112.

[55] U.N., The Process of Industrial Development in Latin America, p. 44.

GDP (r_p) rather than the growth of r_k which determines the level of r_a.[56]

If this observation is true for the case of Mexico, then Mexico's accelerating growth has been the result of a better utilization of capacity as well as an enlargement of capacity. It can be observed from Table 16 that, according to the author's estimates, the residual r_a was certainly an important factor in Mexico's growth for the period 1965-1969.

It was pointed out in this chapter that Mexico's needs for industrialization are great in terms of both a rapidly growing, increasingly urban population, and the inability of other economic activities to adequately stimulate development. These needs also exist for Latin America as a whole. The present instruments for accelerating industrialization are essentially "inward," both for Mexico and Latin America as a whole. The question asked in this chapter was: How have these tools performed in satisfying both Mexico's and Latin America's needs for industrialization?

In the case of Latin America, "inward" industrialization efforts have produced poor results. Not only have growth rates of industrial product and GDP been low, but they have actually

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[56] Professor Bruton verifies this observation for Latin America by taking the regressions of r_p on r_a and r_k on r_a. The former was significant and the latter was not significant.

deteriorated over the past three decades. Industrialization in Latin America has obviously not kept pace with the needs for industrialization in Latin America. Alternative tools of industrialization, such as the promotion of manufactured exports to world markets or LAFTA, should under such circumstances achieve high levels of participation.

In the case of Mexico, the growth of industry and the growth of GDP have been rapid enough to satisfactorily absorb urban population increases, and maintain a rate of increase in per capita product in excess of the OAS goal of 2.5 per cent growth per year. The growth of Mexican industry has, moreover, resulted in an industrial structure more conducive to development than had existed before. Unlike the general Latin American experience, Mexico's growth of industrial product and GDP has accelerated over the past several decades.

The dilemma of Mexico's development, as propounded by Raymond Vernon, appears to have not been much of a dilemma at all. Looking at industrial growth and growth of GDP since 1963, evidence of an incipient dilemma can scarcely be found. Can it therefore be said that Mexico has circumvented the limitations of "inward" policies of industrialization on development found in other Latin American countries.

As stated before, the constraints limiting the use of "inward" policies of industrialization in Mexico are still present, as it will be

discussed in the next chapter, and in some cases these constraints have become greater. Mexico's growth during the past seven years has involved a refinement in the use of "inward" tools rather than an elimination of the constraints to the effectiveness of an "inward" policy of industrialization. In other words, Mexico has used existing market potential more efficiently and intensively to achieve rapid growth rather than expanding that potential.

CHAPTER III

MEXICO'S "INWARD" INDUSTRIALIZATION: RESTRAINTS TO FUTURE GROWTH

While Mexico's industrial growth in recent years has been satisfactory in terms of satisfying the needs for industry discussed in the last chapter, the industry generated in Mexico does exhibit some of the undesireable traits associated with an "inward" development of industry as discussed in Chapter I. High costs of production, a lack of quality in production, underutilization of capacity, and high profit margins are characteristics present, to some extent, in most Mexican industries.

The existence of these undesirable by-products of industrial growth has precipitated somewhat of a conflict in Mexico's development planning. An editorial in Comercio Exterior de Mexico in 1968 observed that,

> Though the industrial protectionalist policy has been a basic factor in Mexico's industrial development, at the present time and in a number of industrial sectors, certain negative results of the policy are beginning to make themselves felt. Notably, high production costs fostered by lack of competition; adequate distribution of resources; prices divorced from international

> competion partly reflecting high production costs and frequently producing excessive profits; a distorted production structure created by the protection given superfluous or anti-economic industrial activities, and an incapacity to compete internationally as much for differences in quality as in price.
>
> The only possible valid policy . . . would be a basic revision of production structures and levels for the purpose of restoring their true objective--industrial development--and preventing any further distortion of the country's economic evolution. [1]

The question raised in this editorial is whether Mexico can afford current rapid industrial growth via protectionalism within a limited market if that growth creates conditions which might eventually undermine the further ability of industry to expand.

Another major cause of concern to Mexico's development planners is the question of how far can an "inward" oriented development of industry be carried before the physical limitations or restraints of the domestic market are reached. Extension of the domestic market is not just a function of the growth of per capita income and population, it is also a function of the distribution of that income. In Mexico, a poor pattern of income distribution can impose a severe restraint on market expansion. In an editorial in Comercio Exterior de Mexico concerning President Ordaz's State of the Union address in 1969 it was observed that,

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[1] "Protectionism and Industry," Comercio Exterior de Mexico, XIV, No. 11 (November, 1968), p. 2.

> The measures of economic policy and the concrete actions outlined in the report, are evidence of an awareness that Mexico's economic development strategy . . . requires a shift in economic policy emphasis towards the redistribution of wealth, since any further sharpening of the imbalance that characterizes the country's development would endanger not only the progress already achieved, but the very continuity of the development process.[2]

The Mexican development planner is also concerned about the future use of IS as a means of achieving dynamic industrialization. Mexico's overall import coefficient is continually declining, thus diminishing the overall potential stimulus that IS can exert on industrialization. In many consumer durable and non-durable industries and in many basic industries, the possibilities of import substitution have been exhausted. In highly sophisticated industries where import coefficients are high, the market size required to operate efficiently is often larger than the potential domestic market. This results in either no IS, or IS at extremely high costs. Virtually all Mexican planners agree that the easy stages of IS are over and that future IS must be carefully planned and will probably provide a diminishing stimulus to overall development in the future.

The above question all have to do with the prospect of promoting future industrial growth through "inward" instruments of

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[2]"Economic Development Strategy," Comercio Exterior de Mexico, XV, No. 10 (October, 1969), p. 3.

industrialization. To what degree is future industrial growth possible in view of the physical limitations discussed, and to what degree is industrial growth via "in-ward" instruments desirable in view of the high costs of the industries generated? In the remainder of this chapter these questions will be investigated, and at least some partial answers to these questions will be suggested.

The Income Elasticity of Demand for Industry in Mexico

One overall indicator of the ability of the domestic market to stimulate industrial growth is the industrial coefficient. It would seem logical that the industrial coefficient, which is a rough indicator of the income elasticity of demand for manufactured goods, should be relatively high and growing for a less developed country such as Mexico or any other Latin American country.

Referring back to Table 10 in Chapter II it was pointed out, however, that Latin America's industrial coefficient $\frac{\text{(Percentage change in GIP)}}{\text{(Percentage change in GDP)}}$ has declined over the past several decades, indicating a diminishing response of industrial growth to growth in GDP. A declining industrial coefficient, which might be hesitantly interpreted as a declining income elasticity of demand for industry (assuming that industrial supply limitations are minimal), is also to be found in Mexico's development since 1955.

TABLE 17

MEXICAN GROSS DOMESTIC PRODUCT BY SECTOR
(Billions of Pesos, 1950 Prices)

Year	Sectors			
	Agriculture, Forestry, Hunting and Fishing		Mining, Quarrying, Construction, Electricity, Gas and Water	
	Value	Percentage Change	Value	Percentage Change
1953	9.5	. .	3.2	. .
1955	12.2	. .	3.8	. .
1958	13.8	. .	4.5	. .
1959	13.3	- 3.6	4.7	4.4
1960	14.0	5.3	5.1	8.5
1961	14.4	2.9	5.2	1.9
1962	15.2	4.2	5.2	. .c
1963	15.5	2.0	5.9	11.3
1964	16.5	6.4	6.6	11.8
1965	17.3	4.8	6.6	. .c
1966	17.7	2.3	7.3	9.0
1967	18.1	2.2	8.0	8.7
1953-1967	. .	90.0	. .	150.0

[a]Manufacturing includes extraction of crude petroleum.

[b]Services includes transportation, commerce, service, and public administration.

[c]Negligible growth.

Source: Calculated from: United Nations, Department of Economic and Social Affairs, Yearbook of National Account Statistics, 1968, I, 1969.

TABLE 17--Continued

Sectors					
Manufacturing[a]		Gross Domestic Product (GDP)		Services[b]	
Value	Percentage Change	Value	Percentage Change	Value	Percentage Change
11.0	. .	46.0	. .	22.3	. .
13.1	. .	55.3	. .	26.2	. .
16.5	. .	66.9	. .	32.1	. .
18.0	9.0	68.8	2.8	32.8	2.2
19.5	8.3	74.3	8.0	35.7	8.8
20.3	4.1	76.9	3.5	37.0	3.6
21.5	5.9	80.7	4.9	38.8	4.8
23.4	8.8	85.9	6.4	41.1	5.9
26.6	13.6	94.7	10.2	45.0	9.4
28.4	6.7	99.7	5.3	47.4	5.3
31.3	10.2	107.2	7.5	50.9	7.3
34.0	8.6	114.4	6.7	54.3	6.6
. .	209.0	. .	148.7	. .	143.0

It is evident from Table 17 that the manufacturing sector has been the most dynamic sector of Mexico's economy since 1953. The Mexican industrial coefficient for the period 1953-1967 was 1.41 $\frac{(209 \text{ per cent})}{(149 \text{ per cent})}$. This coefficient is significantly greater than the Latin American coefficient of 1.2 for the period 1960-1968. Mexico's industrial coefficient has, however, been declining in recent years. Referring to Table 18, it is observed that the Mexican industrial coefficient declined from 1.42 for the period 1955-1960 to 1.33 for the period 1960-1965. In more recent years, 1965 to 1969, the industrial coefficient has averaged 1.32.

TABLE 18

MEXICO'S INDUSTRIAL COEFFICIENT

Period	Percentage growth of GDP for the period	Percentage growth of gross industrial product for the period	Industrial coefficient $\frac{\text{Col. 3}}{\text{Col. 2}}$
1955-1960	34.3	48.8	1.42
1960-1965	34.2	45.6	1.33
1965-1969	31.6	40.5	1.32

Sources: "Report on General Economic Conditions in Mexico in 1969" Comercio Exterior de Mexico, XVI, No. 4 (April, 1970), p. 6; Table 17.

Mexico's declining industrial coefficient has not generated much concern because the decline has occurred while the growth of

industrial product and GDP have been accelerating (1960-1969). In the case of Latin America as a whole, the industrial coefficient has declined while growth rates of industrial product and GDP have been decelerating. In that a cause and effect relationship can be implied in the latter case, the declining industrial coefficient for Latin America as a whole has been a major concern of the development planner.

The ECLA has pointed out that a diminishing response of industrial growth to growth in the market for industrial products (assuming that the income generated from GDP represents the domestic market) might be interpreted as reflecting a weakening ability of the domestic market to stimulate industrial growth, which in turn will lessen the contribution of industry to the growth of the domestic market.[3] If the above interpretation of a declining industrial coefficient is plausible, then Mexico's declining industrial coefficient might be interpreted as reflecting the effects of the aforementioned restraints to the effectiveness of "inward" instruments of industrialization.

The above observation has, in fact, been made by the ECLA. The ECLA has observed that while Mexico's rate of industrial growth has been rapid, it has not been satisfactory with respect to what industrial growth should be, considering Mexico's population, income level, degree of urbanization, and import coefficients. Mexico's

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[3]U. N., The Process of Industrial Development in Latin America, p. 48.

domestic market, the ECLA concludes, has not satisfactorily stimulated industrial growth to its potential level because of structural defects in the Mexican market of the type discussed at the beginning of this chapter.[4]

Many factors go into explaining Mexico's declining industrial coefficient and not all of these factors involve the strength or weakness of the market. It is therefore impossible to state with certainty that the above observations are correct. But, if the industrial coefficient does, in fact, indicate the responsiveness of industrial growth to growth in the market for industrial products, then a decline in the industrial coefficient should be a source of concern to the Mexican development planner regardless of present levels of industrial growth.

Industrial Costs, Prices, and Utilization of Industrial Capacity

In any less-developed country industrialization achieved through protectionalism invariably results in large degree of high cost, inefficient industry, and certain distortions in the product and factor markets. The degree to which these undesirable by-products of "inward" industrialization exist will obviously have an effect on a country's preference for further "inward" industrialization.

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[4] Ibid., p. 53.

Information on industrial costs and capacity usage is very scarce in Mexico, therefore, a general appraisal of the degree to which Mexico's industries exhibit high costs and underutilization of capacity cannot be made. Information on costs and capacity utilization does exist, however, for a limited number of industries, and some insights into the structure of Mexico's industry can be gained by examining this information.

It should first be pointed out that high private production costs within a protected market such as exists in Mexico, are not the true measure of national costs of industrialization. The social costs of such high cost industry are much higher than private costs. The most obvious difference between social and private costs being government expenditures on industrial promotion which would, in view of the discussion of industrial promotion in the last chapter, appear to be quite significant.

The factors most responsible for high private costs (prices) of production in Mexico are postulated to be:

1. The existence of factor market distortions which result in increasingly high rates of capital accumulation by industry;

2. The lack of incentives and ability to adequately utilize capital;

3. The lack of competition within protected markets which contributes to extremely high profit margins for industry;

4. The inability of some industries to generate potential economies of scale due to the smallness of the domestic market and their underutilization of existing industrial capacity.

Factor market distortions

Henry Bruton has pointed out that, contrary to the implication of the factor proportions theorem, Latin American industry is not relatively labor-intensive. It is in fact rather capital-intensive with capital output ratios for Latin American industry being comparable to those found for industry in more highly developed countries.[5] This has been due in part to technological assimulation consisting of the incorporation of production techniques designed for economies with an entirely different set of productive resources, usually reflecting a shortage of labor. Furthermore, adoption of capital intensive techniques is often viewed as a way of compensating for shortages of skilled labor required in more sophisticated industries. The growing capital intensity of Latin American and Mexican industry has also been strengthened by sharp distortions in the prices of the factors of production in relation to the levels that may be considered as representative of their social cost. Private capital costs because of a preferential treatment of capital imports and subsidies to domestic producers

[5]Bruton, "Productivity Growth in Latin America," p. 1102.

of capital, are substantially lower than social capital costs thus encouraging a high capital usage by industry. Labor cost increases, such as Mexico's recently announced twenty per cent increase in the minimum wage,[6] serve to further increase the capital intensity of industry. In response to Mexico's announced twenty per cent increase in the minimum wage, for example, the Chemical Industry Chamber forecasted a much higher degree of automation in the chemical industry.[7] In anticipation of a higher minimum wage the artificial fiber textile industry has achieved eighty per cent automation despite low labor costs in Mexico by Western standards.[8]

If electrical consumption is a rough indicator of the degree of capital usage in an industry, then comparing increases in electricity consumed to increases in employment for a specific industry might reflect a trend toward capital or labor intensity for that industry (increased electrical consumption might also reflect better use of existing capital therefore, the significance of this comparison is limited). Percentage increases in millions of KWH of electricity consumed and workers employed from 1960 to 1966 for the following

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[6] "New Labor Law?" Business Latin America, April 22, 1970, p. 129.

[7] Ibid.

[8] "Industry in 1969," Review of the Economic Situation of Mexico, XLVI, No. 535 (June, 1970), p. 162.

industries were: auto construction, 140 per cent and 20 per cent respectively; Hydrolic cement, 87 per cent and 17 per cent respectively; glass and glass products, 57 per cent and 36 per cent respectively; pulp and paperboard, 84 per cent and 50 per cent respectively; and iron and steel, 59 per cent and 7 per cent respectively.[9] The implication of this industrial sample, if interpreted correctly, is that there is a trend toward greater capital intensity for those industries studied.

Assuming that Mexican industry and Latin American industry have become increasingly capital-intensive, how has this affected production costs? Besides the social costs created through market distortions resulting in an inefficient factor mix for industry (interms of national factor proportions), high private costs of production have been fostered by a poor use of capital by industry.

Capital usage

One element of the poor use of capital in Latin America and Mexico is found in inventory and marketing procedures in Mexico and Latin America. Inventories constitute a much larger proportion of total capital assets of industry in Mexico than in the United States.

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[9]Mexico, Secretario de Industria y Comercio, Departamento de Estadisticas Economicas Basicas, Estadistica Industrial Anual, 1966 (Mexico, D.F.: Talleres Graficos de la Nación, 1968, pp. 9-10, and; United Nations Department of Economic and Social Affairs, The Growth of World Industry, 1953-1965 (ST/STAT/SER/p/4), 1967, pp. 299-304.

This is due to the practice of overstocking raw materials and holding large inventories of finished goods because of a lack of marketing information. Mexico's 1960 industrial census showed fixed assets constituting only fifty-three per cent of capital. The ECLA has compared this fifty-three per cent share of fixed capital of total capital in Mexico to the United States' average share of seventy-eight per cent as evidence of the need for better inventory procedures in Mexico.[10]

The most significant aspect of poor capital usage is, however, the consistent underutilization of capacity by Mexican and Latin American industries. It is a paradox of planning that Mexican industry, with its high demand for capital underutilizes existing capacity to such a high degree. This paradox has been explained in several different ways. Albert O. Hirschman explains the paradox by stating that,

> It is this phase of import substitution the exuberant stage that gives rise to the often noted exuberance and boom atmosphere during which demand is easily overestimated. In any event, low duties or preferential exchange rates for machinery imports make for lavish hordes. As a result, the new industry is likely to find itself saddled with excess capacity. . . .[11]

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[10] U. N., The Process of Industrial Development, p. 70.

[11] Albert O. Hirschman, "The Political Economy of Import Substituting Industrialization in Latin America," in Latin America: Problems in Economic Development, ed. by Charles Nisbet (New York: The Free Press, 1969), p. 248.

To this explanation the ECLA adds the point that much sophisticated imported capital is designed for very high levels of production so that the Latin American firm in using such equipment creates a built-in undercapacity operation.[12] Henry J. Bruton, as noted earlier, claims that this phenomena emanates from the often monopolistic position of the Latin American industrialist which allows him to pass along high capital costs to the consumer, and provides no incentive for full utilization of capacity.

For perhaps all of the reasons stated above, much of Latin American industry does operate at undercapacity, and Mexico's industry is no exception (it should be pointed out, however, that Henry Bruton, as pointed out in the last chapter, attributes a large part of Mexico's accelerated GDP growth to a more effective utilization of capacity than was found in other Latin American countries studied).

According to an ECLA study of Latin American industries for the period 1961-1964, overall capacity usage for Latin American industry ranged from 40 per cent to 82 per cent. Metal working, motor vehicle, machinery, and electrical apparatus industries operated at an average 40 per cent to 45 per cent of capacity. Most heavy industry, according to this study operated at less than sixty per cent

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[12] U. N., "Industrial Development in Latin America," p. 14.

of their capacity.[13] An ECLA study of the seventeen integrated steel plants in Latin America in 1966 pointed out that output was an average forty-eight per cent of capacity for these plants.[14] ECLA studies for some specific Latin American countries in 1961 showed capital usage in Venezuela at approximately fifty per cent for most industries. Capital usage for Chile was approximately 55.3 per cent for major industry, and capital usage in Ecuador was 60 per cent for the factory sector.[15]

Sidney Dell has estimated that in 1962 most industrial establishments in Mexico were operating at something like fifty per cent of their capacity.[16] Whether or not this estimate is accurate, a substantial number of Mexican industries are operating with substantial excess capacity. A Comercio Exterior de Mexico editorial in 1963 estimated that at least fifty per cent of Mexican industry operated at less than normal capacity.[17]

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[13] U. N., The Process of Industrial Development in Latin America, p. 72.

[14] U. N., "Industrial Development in Latin America," p. 15.

[15] U. N., The Process of Industrial Development in Latin America, p. 73.

[16] Dell, A Latin American Common Market?, p. 19.

[17] "Editorial," Comercio Exterior de Mexico, X, No. 3 (March, 1963), p. 138.

With respect to some specific industries, Bela Ballassa cites that in 1962 iron foundries in Mexico worked at an average 50 per cent of their capacity, cigarette factories at an average 78 per cent of capacity, and textile plants at a 42 per cent of capacity, with railroad car, refrigerator, TV, and electrical appliance industries also operating at similar levels of capacity.[18]

The Mexican auto industry was estimated to be operating at 50 per cent of its capacity in 1969,[19] and the artificial fiber industry in 1969 was estimated to be operating at a little over fifty per cent of its capacity.[20] If these illustrations portray, to any significant degree, the state of capital utilization in Mexican industry, then underutilization of capacity is certainly one major factor responsible for high production costs in Mexico.

Profit margins

The lack of competition in industry fostered by protected markets has several major effects on the prices of industrial goods in a

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[18]Balassa, Economic Development and Integration, pp. 76-77.

[19]"The Automobile Market," Review of the Economic Situation of Mexico, XLVI, No. 533 (April, 1970), p. 96.

[20]"Industry in 1969," Review of the Economic Situation of Mexico, XLVI, No. 535 (June 1970), p. 162.

country such as Mexico. First, the incentive to efficiently use factors of production is often diminished as competition is diminished with the result that factor underutilization, such as previously discussed, emerges. Secondly, protected industries are usually able to achieve high profit margins because of their privileged national positions. As it will be demonstrated, these profit margins are a major contributor to high prices for Mexican products.

Using industrial census data reported by the Secretaria de Industria y Comercio for 1966, the average factory percentage mark-up over the total costs of production for thirty-seven reported industries was calculated, by the author, to be 41.32 per cent. Markup percentages for some specific industries were: meat processing, 19.52 per cent; milk processing, 57.97 per cent; beer, 62.20 per cent; artificial fabric, 44.24 per cent; cellulose and paper pastes, 45.60 per cent; auto motors, 72.88 per cent; tubes and posts of iron and steel, 60.40 per cent; and secondary iron and steel processing, 28.19 per cent.[21]

If profit margins for industry as a whole resemble those found in the above sample, then profit margins in Mexico certainly are one major factor responsible for high industrial prices in Mexico. It is

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[21]Calculated from; Mexico, Estadistica Industrial Anual, 1966, pp. 1-3.

argued that by exposing these industries to world competition or regional competition through the pursuit of "outward" industrialization, these profit margins would cease to be such a major component of price.

Economies of scale

The final determinant of high industrial costs and prices to be discussed is the role of economies of scale in determining industrial costs. It has been argued that the Latin American countries, because of their limited market sizes and "inward" orientation, should not develop many sophisticated capital goods and basic industries in that acceptable costs in these industries can only be attained through the achieving of economies of scale associated with unattainable high volumes of sales. Even in a country like Mexico with a population approaching fifty million people, many industries are not able to achieve internationally competitive costs because of the limitations in the markets of these industries. It should also be remembered that because of a high degree of income inequality in Mexico, as it will be shown, the market for manufactured goods is much less than fifty million people.[22]

[22]In fact, the ECLA has estimated that Mexico's consumption of manufactured goods in 1962 as a percentage of total private consumption (21.6 per cent in 1962) was the second lowest in Latin America; U.N., The Process of Industrial Development in Latin America, p. 121.

Bela Balassa in Economic Development and Integration discusses, in depth, the economies of scale to be gained through enlarged sales for various industries, and then estimates the ability of less developed countries to achieve these economies. In most cases discussed, the Latin American countries, including Mexico, fall short of the required industrial outputs for achieving these economies of scale.[23]

Prices of manufactured goods

The end result of the above factors interacting within a protected market is high industrial cost. Furthermore, these high industrial costs are compounded as intraindustry linkages serve to transmit pecuniary diseconomies in the form of high cost inputs through the various stages of production in Mexican industry.

It is argued by Bela Balassa that economic integration could serve to reduce industrial costs by eliminating, to a large degree, each of the above factors responsible for high costs within a protected market. By making the market more competitive and larger, factor price distortions, underutilization of capacity, high profit margins, and the inability of industry to generate economies of scale would cease to operate as high cost generators in industry.

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[23]Balassa, Economic Development and Integration, pp. 89-105.

The question of just how high are Mexican industrial prices is a difficult question to answer. Most everyone agrees that they are significantly higher than industrial prices in the United States or Western Europe but little evidence exists to, in general, substantiate these claims. One major problem in gathering such evidence on relative prices for manufactured products of Latin American countries involves the use of official exchange rates to develop comparable relative prices. The over-pricing or under-pricing of the various national currencies of Latin America can result in rather unexpected results in the comparison of relative prices of manufactured goods.[24]

The ECLA has conducted several studies of the prices of manufactured goods in Latin America which circumvent the problems imposed by exchange rate distortions. One study by the ECLA constructs an index of prices of manufactured goods based on a sample of expenditures on food products for each nation studied. Expenditures on these food samples were then considered to be equal for all countries, allowing for comparisons of relative prices of manufactured

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[24] This problem is discussed by the U. N. in The Process of Industrial Development in Latin America, p. 128. An example of the effects of exchange rate distortions on the prices of manufactured goods is found in the authors' attempt to develop a bench mark measure of the degree of trade creation and trade diversion resulting from Mexico's participation in LAFTA in Chapter V. In this example, the high degree of "trade creation" found must certainly be attributed largely to distortions in Latin American currency exchange rates.

goods between the various countries.[25] The second study derived unit prices of manufactured goods for the countries studied from both official exchange rates and estimated parity exchange rates, thus allowing a comparison of absolute prices among countries.[26] Both studies attempted to measure prices in 1962 for Argentina, Brazil, Colombia, Chile, Peru, Venezuela, Guatemala, Mexico, and the United States.

In general, the two Latin American countries displaying the lowest prices in both studies were Colombia and Guatemala. Latin American prices, however, were on the whole much higher then United States prices for manufactured goods. Price differences between Latin America and the United States were greater in the second study than the first study. In terms of absolute prices, the most serious distortions in prices for Latin American products were found in capital goods.

For Mexico, relative prices of investment goods were approximately 40 per cent higher than the relative prices of investment goods in the United States. Argentina, Brazil Chile, and Peru recorded even higher relative prices than Mexico. Relative prices for non-food consumer non-durable manufactured goods in Mexico were

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[25] U. N., The Process of Industrial Development in Latin America, pp. 130-134.

[26] Ibid., pp. 136-143.

approximately twenty-two per cent higher than relative prices for these goods in the United States. In this category of products, Argentina, Brazil, Chile, Peru, and Venezuela recorded higher relative prices than Mexico. It may be argued that if absolute prices of the sample food products were much lower in Latin America than in the United States, the significance of this study in terms of intra-country relative price comparisons might be overstated.

The second study, however, tends to substantiate the finding of the first study. For Mexico absolute per unit prices, calculated by the estimated parity exchange rate, were substantially higher than United States prices for all but a few of the products listed. Absolute per unit prices, calculated by official exchange rates were however, very comparable to United States prices. For example, the Mexican per unit price for adding machines, calculated by the parity exchange rate, was 73 per cent higher than the United States' price for adding machines. Calculated by the official exchange rate, the Mexican per unit price for adding machines was 7 per cent lower than the United States' price.[27]

Recognizing that official exchange rates significantly understate the prices of Mexican products, high comparative prices and costs are still found for many Mexican manufactured products using official conversion rates. For example, the cost of a light truck in

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[27] Ibid.

Mexico for 1967 was 58 per cent higher than the cost of a light truck produced in the United States.[28]

Concluding remarks

High costs and high prices of manufactured goods fostered by "inward" industrialization appear to be common to Latin America, as are the direct determinants of these high costs and prices. To what degree these undesirable by-products of "inward" industrialization will shape Mexico's continued preference for "inward" industrialization is difficult to determine. That such by-products constitute a serious problem for Mexico's development is, however, clearly evident. Moreover, the longer these conditions are allowed to exist, the more difficult will be the process of reorientation to "outward" policies. For Latin America as a whole, the fact that industrial costs are high and industrial performance, measured by the standards set in the last chapter, has been poor would seem to indicate that Latin America's preference for further "inward" industrialization should be relatively weak. Mexico's preference for "inward" industrialization is not so easily determined.

Assuming for the moment, however, that the aforementioned costs of industrialization are acceptable in view of the past benefits of

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[28]Jack Boranson, "Integrated Automobiles for Latin America?" Finance and Development, V, No. 4 (December, 1968), p. 27.

"inward" industrialization in Mexico, what other factors must go into a determination of Mexico's preference for "inward" industrialization?

As it was indicated at the beginning of chapter, Mexico's industrial coefficient has been declining since 1955, and one suggested cause for this decline was the existence of structural impediments or restraints to the expansion of the market for industrial goods. These restraints were identified as being a lack of further import substitution potential and a high degree of income inequality and regional dualism in Mexico. In that these factors act as restraints to the expansion of "inward" industrialization, they must also be considered in establishing a preference for "inward" industrialization.

Income Distribution and Regional Dualism in Mexico

The growth of Mexico's market for manufactured goods depends not only upon the growth of per capita income and population in Mexico. It also depends on the distribution of that income. Since "inward" industrialization requires a growing domestic market for manufactured goods, the successful use of "inward" instruments of industrialization is highly dependent on the national pattern of income distribution.

Raymond Vernon cites Mexico's poor distribution of income as one of the major bottlenecks to an expansion of industry through the domestic market;

> The nature of Mexico's income distribution is such that, instead of thinking of 35 or 40 million people as being the object of their sales campaigns, many businessmen are obliged to think of some small fraction as the target. For instance, the urban poor, the ejidal farmers, and the small landowners--making up perhaps two-thirds or three-fourths of the country--may have to be regarded as simply outside the market for many modern day products.[29]

Mexico's high level of income inequality is largely a function of regional dualism in Mexico--the North-South problem. Generally speaking, the Federal District, the northern tier of states, and the Gulf states can be thought of as the high income states while the central and southwest areas can be thought of as the low income regions. In part, regional disparities in income are the result of historical, geographic, and climatic forces in Mexico. The fact that the central and southwest areas of Mexico are generally mountainous, largely tropical and possess largely Indian populations is surely a major factor responsible for the relative low levels of development in these regions. At least to some extent, however, the plight of these regions has been accentuated by governmental development planning which has disproportionately promoted infrastructure development and industrialization in the already developed regions at the expense of the central and southern states.

To illustrate the impact of regional dualism on Mexico's distribution of income, it can be seen from Table 19 that the average

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[29]Vernon, The Dilemma of Mexico's Development, p. 183.

TABLE 19

DISTRIBUTION OF MONTHLY INCOME BY FAMILY FOR SELECTED STATES OF MEXICO
(Pesos)

State	Average monthly income for 1958	Percentage of families below the mean income
Baja California	2,066	11.7
Sonora	1,361	30.7
Chihuahua	1,365	54.3
Federal District	1,449	46.8
Hidalgo	847	58.6
Oaxaca	682	80.4
All Mexico	825	71.0

Source: William Friethaler, Mexico's Foreign Trade and Economic Development (New York: Frederick A. Praeger, 1968), Table 8, p. 22.

family monthly income, in 1958, for the northern state of Baja California was a little over three times greater than the average family monthly income of the southern state of Oaxaca. It can also be noted from Table 19 that the distribution of income within such central and southern states as Hidalgo and Oaxaca is very poor. In Oaxaca 80.4 per cent of the families had an average monthly income less the average 682 pesos. Such a distribution of income is comparable to the overall distribution of income for Mexico, with 71.0 per cent of the families of Mexico earning less than the national average monthly income of 825 pesos in 1958.

Mexican Presidents have periodically announced programs designed to equalize regional incomes in Mexico, such as the industrial decentralization program now in effect. Such programs, however, have apparently had little effect in narrowing disparities in regional incomes.

Referring to Table 20 it is evident that the disparity between per capita incomes in the Federal District and per capita incomes for the rest of the country has been widening since 1950.

Both the population and the GDP of the Federal District have grown at a faster rate than the population and GDP of Mexico as a whole. As a result of these different growth rates, the Federal District's share of national GDP and population have increased since 1950. The Federal District's share of GDP, however, has grown at a much faster rate than the Federal District's share of population: 22 per cent to 38 per cent versus 11.9 per cent to 15.3 per cent for the period 1950 to 1970. The result of this growth has been that per capita product has grown at a faster rate in the Federal District than for Mexico as a whole (1.78 times faster for the period 1950-1970). Whereas the average per capita product of the Federal District in 1950 was 1.88 times greater than the average national per capita product (6,161 pesos versus 3,273 pesos in 1960 prices), the average 1970 projected per capita product for the Federal District is 2.49 times greater than the average 1970 national projected per capita

TABLE 20

THE GROWTH OF PER CAPITA INCOMES FOR THE FEDERAL DISTRICT AND THE PROVINCES OF MEXICO
(Millions of Pesos, 1960 Prices)

Region/GDP	1950	1955	1960	1965	1970 (Projected)
Mexico	84,409	114,918	154,137	208,783	283,407
Federal District	18,791	29,939	46,312	74,856	108,285
Federal District GDP as a percentage of National GDP	22	26	30	36	38
Federal District population as a percentage of total population	11.9	13.4	13.9	14.6	15.3
Growth in GDP/Person, Index (1950=100)					
Mexico	100	118.3	130.6	149.4	170.9
Federal District	100	121.3	149.8	194.4	226.9

Source: "The Federal District and the Provinces," Review of the Economic Situation of Mexico, XLIV, No. 514 (September, 1968), pp. 12-14.

product (13, 979 pesos versus 5, 594 pesos in 1960 prices).[30] It would appear that despite governmental efforts to bring about a greater degree of income equality in Mexico, the disparity between per capita incomes in the Federal District and the remainder of Mexico has become worse. In view of the recent extensive border industrialization programs in the north of Mexico, the relationship between per capita incomes in the relatively wealthy northern states and per capita incomes in the southern states probably shows a similar trend toward greater inequality.

The severity of the income distribution problem in Mexico was clearly illustrated in an ECLA seven country study of income concentration for the period 1963-1964.[31] The countries studied included were Argentina, Brazil, Colombia, Costa Rica, El Salvador, Mexico, and Panama. The results of this study, as they pertain to Mexico are contained in Table 21.

Mexico, with 50 per cent of its population receiving only 15.4 per cent of personal income and 20 per cent of its population receiving 58.5 per cent of personal income, has one of the highest levels of income inequality in Latin America. Only El Salvador ranked

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[30] "The Federal District and the Provinces," Review of The Economic Situation of Mexico, XLIV, No. 514 (September, 1968), p. 12.

[31] U. N., "Income Distribution in Latin America," p. 40.

TABLE 21

MEXICO'S DISTRIBUTION OF INCOME
1963 - 1964

Percentages of families		Percentage of Mexico's personal income
Top	5.0	29.0
	15.0	29.5
	30.0	26.1
	30.0	11.8
Low	20.0	3.6

Source: United Nations, Economic Commission for Latin America, "Income Distribution in Latin America," Economic Bulletin for Latin America, XII, No. 2, 1968, p. 48.

ahead of Mexico in income concentration for the seven countries studied.[32]

The end result of such a pattern of income distribution is that effective demand for manufactured goods by the majority of the population is limited. An ECLA study in 1962 observed that 51.2 per cent of private consumption expenditures in Mexico were for food, the third highest percentage in Latin America. The same study showed that only 21.6 per cent of private consumption expenditures in Mexico were for manufactured goods, the second lowest per cent in Latin

[32] Ibid.

America.[33]

How will Mexico overcome this imbalance in income distribution? One element of any plan to bring about a greater equality of income distribution must certainly be a decentralization of industry. With approximately sixty per cent of the country's industrial economic activity centered in the Federal District area and most of the remainder of industrial economic activity centered in a few northern states, a movement toward income equality cannot begin until industry is infused into the economies of the central and southwestern states.[34] Certainly even greater efforts in agrarian reform and intrastructure modernization are needed in these areas, but the uplifting of these depressed regions will largely depend on Mexico's ability to decentralize industrial development.

While governmental programs designed to promote such a decentralization of industry are being developed and implemented, the process of income equalization will be very long and difficult. A report for the first half of 1969 showed that of the 26 billion pesos of industrial loans made by Mexico's private banks, 17 billion went to the Federal District, 5 billion went to Nuevo Leon and Jalisco (in the

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[33]U. N., The Process of Industrial Development in Latin America, p. 121.

[34]"Industrial Decentralization," Comercio Exterior de Mexico, XVI, No. 4 (April, 1970), pp. 19-20.

north), and only 4 billion went to the remainder of the country.[35] The President of the Nation Banking System referred to this as, ". . . further evidence of the industrial imbalance which obstructs the country's economic development."[36]

Yet this equalization is the goal of Mexico's government. To cite President Ordaz, "To raise the great mass of our people from their poverty is an imperative task to which we cannot, we may not respond by simply consolidating economic structures that do not benefit this important part of the Mexican family!"[37] The government has instituted such programs as the Program for Rural Development and The Office of Rural Industries to develop industries in the central states and the southwestern states, and they have met with some success. A 4.5 billion peso hydroelectric plant recently constructed in Malpaso is expected to attract forty billion pesos of industrial investment into the Mexican southwest within the next several years.[38]

Direct attempts to improve Mexico's distribution of income, such as President-Elect Echeverras' pledge to raise the minimum

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[35] Ibid.

[36] Ibid.

[37] "Economic Aspects of the President's State of the Union Address," Comercio Exterior de Mexico, XV, No. 10 (October, 1969), p. 24.

[38] "Regional Development," Comercio Exterior de Mexico, XIV, No. 8 (August, 1968), p. 13.

wage by twenty per cent, will probably meet with less success than industrial decentralization.[39] Raymond Vernon has pointed out that past reforms of this nature (minimum wages) have met with great hostility from the business community, which considers such reforms as being anti-business. Such planned reforms have, in the past, been dropped by the government because of this hostility.[40] As it was noted earlier, the proposed twenty per cent minimum wage increase has already encountered resistence in the form of industry's threats to automate their plants.

Summary conclusions

In summary, it may be said that Mexico's pattern of of income distribution and regional dualism pose serious restraints to the expansion of industry through the domestic market. Furthermore, it would appear that these restraints have intensified in recent years. Governmental programs to decentralize industry and raise the minimum wage have been instituted, but their effects may not be felt for many years. Mexico has been able to achieve rapid industrialization through the domestic market in the past, but in view of the high degree of income inequality evident in Mexico, serious doubts should be

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[39]"New Labor Law?" Business Latin America, April 23, 1970, p. 129.

[40]Vernon, The Dilemma of Mexico's Development, p. 184.

raised as to the ability of the domestic market to act as a dynamic stimulus to industrialization in the future.

The Import Substitution Process in Mexico

Import substitution has, until recent years, been the most successful and accepted means of promoting industrialization in Mexico and Latin America. The success and popularity of this "inward" instrument of industrialization was based on the two functions it supposidly performed for the development planner. First, import substitution, in that it involved a replacement of domestically produced goods for previously imported goods, was viewed as a partial solution to chronic balance of payment deficits that have plagued the Latin American countries. Second, import substitution, in that it worked by artificially creating a supply vacuum in a market for manufactured goods that was already easily measured, well developed, and clamoring for goods, resulted in a dynamic growth of domestic industry.

In more recent years, however, import substitution as a means of promoting industrial growth has declined in popularity. In countries such as Argentina, Chile, and Uruguay, industrial import coefficients $\frac{(\text{Imports of industrial goods})}{(\text{Total supply of industrial goods})}$ have become so low, as a result of past import substitution, that margins for future import substitution are nearly depleted. In countries such as Brazil, Mexico,

Peru, and Venezuela significant margins for further import substitution still exist, but these margins are largely for sophisticated manufactured goods, whose domestic production would entail high social and private costs. Moreover, Latin American development planners are increasingly becoming aware of the high costs generated by their past promotion of industry behind protective tariff walls, and these costs are not measured only in terms of immediate social costs. There is also the realization that continued use of IS makes the possible use of alternative instruments of industrialization, such as the export of manufactured goods, more difficult.

Import substitution industrialization in Mexico generally evolved through the various stages of the IS process described in Chapter I. During the late 1930's and during the period of World War II, IS was aimed at the import of non-durable consumer goods. This was a period of spontaneous import substitution with import restraints being caused by wartime shortages rather than government protectionalism. After 1945, however, continued growth in these industries was fostered by increasingly high protectionalist barriers. Many consumer durable goods were put under protection by 1948, and by 1954 intermediate products such as light chemicals, light basic metals, and glass were put under protection. Beginning in 1958 IS passed into a new phase--the promotion of basic industry (chemicals, petroleum, steel) and high technology industry (metal transformation, electronics,

machinery, and construction equipment).[41]

Mexico's pattern of industrial growth has essentially reflected the passage through these various stages of import substitution. Industrial growth during the late 1940's and the 1950's was largely promoted by the rapid growth of consumer durable and non-durable goods industries, whereas industrial growth during the past decade has been most marked in the basic industries and high technology industries.

The existence of stages in the IS process is a commonly observed phenomena in less-developed countries, in that IS is a highly sequential process. The substitution of domestically produced non-durable consumer goods for imported non-durable consumer goods is usually the first stage of the sequence because of the low technology and capital requirements of instituting such industries, and the high levels of imports of such goods at that stage of the country's development. The growth of domestic non-durable consumer goods industries creates, however, a new import demand--the demand for capital and intermediate products essential to the growth of these new non-durable consumer goods industries. With the institution of the second phase of the IS sequence, the substitution of domestic production of

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[41] A brief history of the IS process in Mexico, from which this discussion was derived, is contained in; Mexico, Secretario de Hacienda y Credito Publico, Investigacion Fiscal (Mexico, D. F.: Talleres Graficos de la Nación, August, 1967), pp. 98-105.

durable consumer goods for imports of such goods, import demand for capital goods and intermediate product reaches such a high level that domestic producers are now attracted to the IS production of such goods. Through backward linkages, the production of capital goods creates an additional demand for imports of intermediate products. In response to this import demand, IS production of intermediate products is promoted, creating an additional demand for imports of capital goods. Capital and intermediate products may, therefore, be thought of as disguised imports. When those products to which they are inputs are subjected to IS, their import demand is no longer disguised.

An example of this sequential IS process is found in Mexico's automotive industry. In 1960 there were approximately seventy lines of automobiles being produced in Mexico under protective import barriers. But, only 15 per cent of the parts used in the production of these autos were domestically produced. In response to the automotive industry's high import demand for capital and intermediate products, the government decreed in 1962 that automotive plants' inputs had to be at least 60 per cent Mexican produced. Another decree in 1964 prohibited the import of complete auto motors. As a result of these protective measures, investment in Mexican auto parts factories increased by 125 per cent during the period 1962-1964. By 1969 63. 9 per cent of the parts used in the automotive industry were

domestically produced.[42]

This sequential process can be more clearly seen by examining the composition of Mexico's imports for the period 1940-1967. Imports of consumer goods as a percentage of total imports, as seen in Table 22, declined from 23.9 per cent in 1940 to 11.1 per cent in 1967, that decline being fairly steady. Changes in the shares of capital goods and intermediate products, however, show a more complicated behavioral pattern.

The ECLA in a study of the import substitution process in Latin America has constructed a model, based on the behavior of Latin America imports, which comes close to explaining the behavior of imports of capital goods and intermediate products in Mexico. In their study they found that in the initial stage of IS, capital imports increased rapidly to facilitate the expansion of consumer non-durable and durable goods industries. During the second stage of the IS process, the development of simple metal transforming capital goods industries takes place, resulting in a decline in capitals share of total imports and an increase in intermediate products share of total imports. A third stage involves the rapid development of intermediate product industries, such as the chemical industry. This third stage increases the requirements for capital goods, resulting in an increase

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[42] "The Automobile Market," Review of the Economic Situation of Mexico, XLVI, No. 533 (April, 1970), p. 94.

TABLE 22

THE COMPOSITION OF MEXICO'S IMPORTS BY GROUPS OF PRODUCTS
1940-1967
(Group Imports as a Percentage of Total Imports)

Type of Import	Percentage of Total Imports									
	1940	1945	1950	1955	1960	1963	1964	1965	1966	1967
Total Imports	100	100	100	100	100	100	100	100	100	100
Consumer Goods	23.9	21.7	15.8	15.4	12.1	12.9	12.6	12.1	12.4	11.1
Non-durable	13.8	11.4	8.3	7.0	6.6	7.2	6.5	5.7	5.5	--
Durable	10.1	10.3	7.5	8.4	5.5	5.7	6.1	6.4	6.9	--
Raw Materials and Intermediate Products	44.6	41.0	43.5	45.1	48.5	54.9	45.9	45.8	45.1	42.3
Capital Goods	30.6	36.8	40.0	39.3	39.1	32.1	39.6	39.8	40.4	44.3
Others	0.8	1.5	0.7	0.3	0.3	0.1	1.9	2.3	2.1	2.3

Sources: Calculated from: William Freithaler, Mexico's Foreign Trade and Economic Development (New York: Frederick A. Praeger, 1968), p. 55; United Nations, Economic Commission for Latin America, Economic Survey of Latin America, 1967 (E/CN. 12/808/Rev. 1), 1969, p. 172.

in capitals' share of total imports and a decrease in intermediate products' share of total imports.[43]

Referring to Table 22, the first stage for Mexico would appear to correspond to the period 1940-1950. The second stage corresponds to the period 1955-1963 and the third stage corresponds to the period 1963-1967.

It would appear, from the above discussion, that IS industrialization in Mexico has been a highly sequential process with "import swallowing" starting with final demand linkages for consumer goods and working backwards through the various capital goods and intermediate goods industries supplying these consumer goods industries. This has also meant a verticle generation of high costs reflected by the high prices of the final product of this process.

Mexico's passage through each phase of this sequential IS process obviously reduces the potential for future aggregate IS, even though individual new IS areas are successively being created through the sequential process. It should also be pointed out that the new IS areas created by the sequential process usually involve a higher degree of sophistication and complexity of production techniques than the IS areas expended. The IS process, therefore, tends to slow down as successive stages of the process are reached. Also, each

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[43]U. N., The Process of Industrial Development in Latin America, pp. 28-33.

successive stage of the IS process tends to be more costly than the previous stage.

The two factors physically limiting the degree to which aggregate IS can be used in the future are the size of the import coefficient and the types of industries for which satisfactory import coefficients exist.

Import substitution in the past for Latin America was a major contributor to the industrial growth of the region. The past intensive use of import substitution, however, has resulted in little potential for future IS industrialization.

Imports as a percentage of GDP for the Latin American republics are among the lowest in the world. Whereas total imports were 20 to 25 per cent of the total domestic product of the region in 1929, by 1963 the ratio of regional imports to GDP was barely ten per cent.[44] For Mexico, the ratio of imports to GDP declined from 13.1 per cent in 1955 to 7.1 per cent in 1968.[45] With only a margin of 7.1 per cent of the domestic market, IS in Mexico can hardly be expected to be a dynamic force of industrialization in the future.

Mexico's industrial import coefficient has not dropped as low as either Argentina's or Brazil's industrial import coefficients,

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[44] Ibid., p. 21.

[45] Caculated from: International Monetary Fund, International Financial Statistics, XI, No. 10 (October, 1958), p. 178; International Monetary Fund, International Financial Statistics, XXIII, No. 7 (July, 1970), p. 200.

but the total effects of import substitution have still been rather minimal in Mexico in recent years. The ECLA estimates of industrial import coefficients for the major countries of Latin America in 1960 were: Argentina, 6.82 per cent; Brazil, 8.49 per cent; Colombia, 15.77 per cent; Chile, 16.41 per cent; Mexico, 16.62 per cent; Uruguay, 17.00 per cent; Peru, 18.30 per cent; and Venezuela, 45.09 per cent.[46]

Referring to Table 23 estimates of industrial import coefficients for Mexico were calcualted for the years 1966 and 1968 using the ECLA procedure used to derive the industrial import coefficients for 1960. The industrial import coefficients derived for these two years were 16.6 per cent and 15.3 per cent respectively.

Using the ECLA procedures used to estimate the amount of industrial growth attributable to import substitution for the period 1929-1960,[47] the increase in the total domestic supply of industrial goods attributable directly to IS has been estimated for the period 1966-1968.

Based on the assumption that the ratio $\frac{\text{1966 Imports of Manufactures}}{\text{1966 GIP-Exports of Manufactures}}$ should equal the ratio $\frac{\text{1968 Imports of Manufactures}}{\text{1968 GIP-Exports of Manufactures}}$ if the income elasticities of demand for imported manufactured

[46] U. N., The Process of Industrial Development in Latin America, p. 50.

[47] Ibid., p. 21.

goods and domestically produced goods are equal and their price ratios are constant, the following calculations were made:

$$\frac{\text{1966 Imports of Manufactures (17,239.3 million pesos)}}{\text{1966 GIP-Exports of Manufactures (86,083.8 million pesos)}} = 20\%;$$

20% X 1968 GIP-Exports of Manufactures (112,685.9 million pesos) = projected 1968 Imports of Manufactures (22,537.1 million pesos); projected 1968 Imports of Manufactures (22,537.1 million pesos) - actual 1968 Imports of Manufactures (20,367.9 million pesos) = IS effect (2,169.2 million pesos). So assuming that the income elasticities of demand for imports and domestically produced goods are equal, and the price ratios of these goods have not changed during the period, an IS effect of 2,169.2 million pesos for the period 1966-1968 is derived.

The total domestic supply of manufactured goods in Mexico increased by 30,266.3 million pesos from 1966 to 1968. That portion of increased supply attributable directly to IS amounted to only 2,169.2 million pesos, or 7.1 per cent of the total supply increase.

There are obviously many shortcomings in using a measure of IS such as derived above,[48] but the measure does provide a rough estimation of the role of import substitution in Mexico's industrialization, and that role appears to be rather weak overall.

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[48]Within each industry grouping considerable IS might have occurred for individual products. This would not show up, however, if another product in this grouping experienced a larger import growth than the IS effect.

TABLE 23

ESTIMATES OF MEXICAN IMPORT COEFFICIENTS FOR MANUFACTURING
(Current Pesos)

	Items	1966	1968
A.	Value of manufactured imports (Millions of pesos)		
	Milk products	118.8	79.4
	Food pastes	70.9	65.0
	Food, drinks, tobacco	335.8	217.7
	Mineral products	345.4	338.4
	Chemical products	2,587.4	2,718.5
	Plastics, resins, rubber	735.7	510.0
	Hides, leather	18.4	7.5
	Lumber, cork, wood	61.1	43.6
	Paper	640.4	676.0
	Textiles	198.2	133.0
	Hats, shoes	29.2	8.4
	Cement, glass	197.9	222.5
	Jewelry	14.9	9.3
	Metals	1,450.5	1,226.7
	Machines, electrical materials	6,521.5	8,448.5
	Transport equipment	3,091.1	4,581.6
	Optics, electronics	721.7	881.6
	Munitions	14.8	20.5
	Other manufactures	85.6	179.7
	Total	17,239.3	20,367.9
B.	Value of manufactured exports (Millions of pesos)	2,333.2	3,118.1
C.	Gross industrial product (Millions of pesos)	88,416.0	115,804.0
D.	Import Coefficient $\frac{A}{(A - B) + C}$	16.6 %	15.3 %

Sources: Calculated from: International Monetary Fund, International Financial Statistics, XXIII, No. 6 (June, 1970); Mexico, Secretaria de Industria y Comercio, Anuario Estadistico del Comercio Exterior de los Estados Unidos Mexicanos, 1968 (Mexico, D.F.: Talleres Gráficos de la Nación, 1969); Mexico, Secretaria de Industria y Comercio,

TABLE 23--Continued

Revista de Estadistico (Mexico, D.F.: Talleres Gráficos de la Nación, June, 1967); United Nations, Department of Economic and Social Affairs, Yearbook of National Account Statistics, 1968, I, 1969.

Referring again to Table 23, it is interesting to note that the strongest IS appears to have occurred in consumer non-durable goods for the period 1966-1968 with absolute declines in imports occurring from 1966-1968 for milk products, food pastes, food, drinks, tobacco, plastics, hides, textiles, and hats and shoes. The decline in metal imports was largely due to the fact that, whereas net imports constituted 31.3 per cent of the domestic supply of iron and steel in 1958, net imports constituted only 6.2 per cent of the domestic supply of iron and steel in 1968.[49] The three areas where IS appears to have the greatest potential application are chemicals, machines and electrical materials, and transport equipment. To some degree the import demand for these capital and intermediate goods must be thought of as irreducible. A high import demand for such sophisticated goods represents the last stages of the IS sequential process, and the production of many of these goods may require a larger market than that afforded by IS and potential growth in the domestic

[49]"Indices of the Iron and Steel Industry," Review of the Economic Situation of Mexico, XLVI, No. 530 (January, 1970), p. 15.

market.

A rather unique aspect of the import policy of Mexico, and one cause for the lack of growth in the IS in recent years, is found in the free import zone. Certain border areas in Baja California and Sonora have been classified as free import zones outside of the tariff and licensing umbrella, and therefore, outside of the IS process. In 1968 imports into these high income regions amount to a little over three billion pesos representing approximately twelve per cent of Mexico's total imports. Of these imports of three billion pesos, seventy-six per cent were classified as free imports.[50] That this region represents an extremely rich opportunity for import substitution is born out by the fact that in 1962 the imports of Tijuana and Mexicali, the two largest cities of the region, constituted fifty-two per cent of the total goods consumed in these two cities.[51] The government, unable to foster IS in the normal fashion, instituted in 1965 a subsidized border sales program to encourage sales in this rich region. Sales of Mexican products to the region in 1967 amounted to 1.7 billion pesos. The cost of the program's subsidization for 1967

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[50]Mexico, Secretaria de Industria y Comercio, Anuario Estadistico del Comercio Exterior de los Estados Unidos Mexicanos, 1968 (Mexico, D.F.: Talleres Gráficos de la Nación, 1969), pp. 729-730.

[51]Freithaler, Mexico's Foreign Trade and Economic Development, p. 128.

was was estimated to be 32.6 million pesos.[52] Comparing Mexican border sales of 1,727,000,000 pesos in 1967 to 1968 border imports of 3,117,573,000 pesos indicates the size of the IS market to be gained in this region.

Final remarks on IS in Mexico

The OAS and the ECLA in their evaluations of import substitution in Latin America have come to the conclusion that the IS phase of industrialization is over in Argentina, Chile, and Uruguay. In Brazil and Mexico they generally conclude that, although IS can still function as a tool of industrialization, its use will be extremely costly.[53]

While the limits to the IS process in Mexico were not established in this section, hopefully a better understanding of the IS process and its potential for stimulating industrial growth in Mexico has been achieved.

It has been established that industrial import substitution has, in recent years, lost much of the dynamism that marked its earlier use. According to ECLA calculations, IS directly promoted over thirty per cent of Mexico's industrial growth from 1929 to 1960.

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[52] "Conquest of the Border Market," Comercio Exterior de Mexico, XIV, No. 8 (August, 1968), p. 13.

[53] OAS, The Alliance for Progress and Latin American Development Prospects: A Five Year Review, 1961-1965, p. 33; U.N., The Process of Industrial Development in Latin America, p. 34.

Using the same ECLA estimating techniques, it was found that IS promoted only 7.1 per cent of total industrial growth for the period 1966 to 1968.

One might infer from the size of Mexico's ratio of imports to GDP (7.1 per cent in 1968) or from Mexico's industrial import coefficient (15.3 per cent in 1968) that the future use of import substitution in Mexico will be rather limited.

There is a concensus of opinion in Mexico that the IS process has passed the easy phases of its sequential development. Future IS must be used only sparingly and in a controllable fashion. The following statement by Antonio Armendaz, Director General of Mexico's Banco Nacional de Comercio Exterior, is representative of the Mexican development planners attitudes toward IS use in the 1970's:

> It is unthinkable that the experiences of the fifties and sixties, when the industrialization process was based on indiscriminate protectionism, should be repeated in the seventies with regard to intermediate and capital goods production. Protection in these cases can no longer be indiscriminate and permanent, but must be carefully programmed and scheduled to diminish progressively. [54]

The second function of IS, the balance of payment aspect, has been even less admirably performed than the industrial promotion

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[54] "Perspectives for the Decade of the Seventies," Comercio Exterior de Mexico, XVI, No. 4 (April, 1969), p. 14.

function in recent years. Mexico's import growth has, since 1963, regularly outstripped the growth of Mexico's capacity to import. The use of IS to reduce import needs has, because of the sequential process, merely transformed those needs rather than reducing them in many cases. The failure of IS to sufficiently control the growth of import demand has resulted in growing balance of payments pressures, the nature of which will be discussed in the next chapter.

Conclusions

The performance of Mexico's industrial sector in terms of absorbing a fast growing urban labor supply and stimulating the growth of GDP was established in Chapter II. In general it was concluded that Mexico's industrial growth has been satisfactory in terms of both of these criteria since 1963.

Mexico's development planners, however, should not base their preference for future "inward" industrialization solely on the accomplishments of "inward" industrialization during the past decade. These accomplishments were achieved at a high social cost.

Industry, operating in a protected market, generated high production costs and high prices in several ways. First, there is the tendency for industry to adopt western capital intensive techniques without regard to national factor proportions. There is also the tendency for industry to underutilize its capital for the various reasons discussed. Operating within a protected market, profit margins for

industry generally are high. Finally, because of limitations in the effective demand for manufactured goods of the protected market, economies of scale are beyond the reach of some key industries.

Even if the development planner finds that these costs are acceptable in view of the benefits associated with past "inward" industrialization, he should be aware of the bottlenecks to future "inward" industrialization.

The presence of a high degree of regional dualism and a high degree of income inequality in Mexico certainly makes the foundation of the Mexican domestic market rather tenuous. Import substitution, the most dynamic element of "inward" industrialization in the past, will not likely perform that role in the future. Import margins for consumer goods are nearly exhausted, and the overall industrial importcoefficient has dropped to a level so low as to make future import substitution most difficult.

To what degree these bottlenecks to the future use of "inward" industrialization will affect Mexico's preference for "inward" industrialization in the future is difficult to say. Their presence and the presence of the high costs of "inward" industrialization should, however, be of major concern to the development planner.

CHAPTER IV

THE CONTRIBUTION OF THE EXTERNAL SECTOR TO MEXICO'S DEVELOPMENT AND INDUSTRIALIZATION

The possession of a viable export sector is critically important to a developing nation such as Mexico. The export sector is a source of essential foreign exchange earnings needed to purchase producers' goods for national industrialization efforts and the export sector allows a nation's industries access to large external markets, which is especially important when domestic markets are small and poorly organized. It is the author's contention that Mexico's export sector has not performed adequately in terms of providing Mexico with a satisfactory capacity to import and in terms of providing a satisfactory stimulus to Mexico's development and industrialization. It is suggested that the solution to Mexico's export sector difficulties lies in an active persuance of "outward" industrialization. The official policy of the Mexican government with respect to the export sector has, in the past few years, increasingly reflected the above contention and suggested solution. Antonio Armendariz, Director General of the National Foreign Trade Bank of Mexico, observed in

1969 that,

> There seem to be few doubts that the main medium-range objective of Mexico's trade policy relative to exports should be that of ensuring a steady increase in export income while reducing export's structural dependency on primary products by so augmenting the participation of manufactured goods that they in time shall become the major component in total exports. The seventies represent an opportunity to approach this objective. [1]

Import Needs, "Outward" Industrialization, And Export Performance

As stated before, the export sector of a country such as Mexico has two important functions to perform. First, the "inward" industrialization of Mexico has created certain irreducible (at least in the near future) import needs that must be satisfied if industrial growth is to be maintained. Acquiring such imports requires adequate inflows of foreign exchange. Foreign exchange can be acquired through the export of goods and services, tourism, foreign investment earnings, unilateral transfers, direct foreign investment, long-term loans, short-term capital inflows, and from drawings on international reserves. Poor performance in any of these sources of foreign exchange, exports of goods and services being the largest source, can result in a balance of payments disequilibrium and eventual shortages of critical producer goods imports. In that such

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[1] Antonio Armendariz, "A LAFTA Pilot Sector," Comercio Exterior de Mexico, XVI, No. 4 (April, 1969), p. 14.

imports are essential to industrial growth, import shortages may result in a deceleration of industrial growth.

Second, the export sector is Mexico's window outward, the access to a far larger and wealthier market for agricultural and industrial products than afforded by the domestic market. Through participation in the export sector, manufacturers are exposed to the competition, production techniques, and technological innovations of the industries of more advanced countries; techniques and innovations which the firm might not adopt if its sole market was the protected domestic market. Through participation in the export sector the manufacturer might also achieve economies of scale and external economies previously unattainable within the limited domestic market. In other words, the export sector can be a dynamic tool of industrialization--"outward" industrialization. In view of the bottlenecks confronting further "inward" industrialization in Mexico, it would seem that a policy of "outward" industrialization should be actively pursued by Mexico. "Outward" industrialization can, however, be pursued in two different ways, through the promotion of manufactured exports to world markets in general, or through participation in an integration scheme such as LAFTA. The type of industrial exports generated through the use of each of these tools tends to be different, as are the restraints to the use of these tools. In pursuing "outward" industrialization some thought must, therefore, be given

to the type of industry desired as a determinant of the degree to which these two tools are to be employed.

The need for "outward" industrialization, as it will be discussed is partially a function of the performance of "inward" industrialization. The need for "outward" industrialization is also a function of the ability of the traditional export sector to generate sufficient export earnings to satisfy critical import needs. As stated before, a case can be made for Mexico's pursuance of "outward" industrialization on the basis of the prospective future performance of "inward" industrialization. A more conclusive case for the pursuance of "outward" industrialization can, however, be made on the basis of the export sectors' inability to generate foreign exchange sufficient to satisfy Mexico's import needs. For Latin America as a whole, the active pursuance of "outward" industrialization can be strongly justified on the basis of both of these needs.

Import needs and export performance

The sequential IS process, as discussed in Chapter III, has transformed Mexico's import bundle from one containing a high percentage of consumer goods and easily substituted capital goods to an import bundle predominantly consisting of what Jorge Sakamoto refers

to as critical imports.[2] Critical imports consist of highly complex capital goods and highly complex or exogenous intermediate goods and raw materials for which domestic substitution is exceedingly difficult, impractical, or impossible. The import of these goods is necessitated by and is essential to the growth of "inward" industrialization.

With these critical imports, referred to by Bela Balassa as irreducible import needs, representing an ever larger share of the import bundle, the indiscriminate use of IS protection becomes a somewhat risky means of promoting industrialization. If domestic production is not immediately instituted for a critical import subjected to IS protection, domestic industries to which this critical import is an input would be undesirably affected. This risk factor does not preclude future IS in Mexico for critical imports, the future use of IS must simply be more judicious.

With the growth in the demand for critical imports closely tied to the growth of Mexico's industrial output and with the IS effects of reducing import demand diminishing, one would logically expect that Mexico's propensity to import such critical goods should be increasing.

Bela Balassa in Trade Prospects for Developing Countries observed that while Latin America had the lowest ratio of imports to

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[2]Jorge Sakamoto, "Industrial Development in Integration of Underdeveloped Countries," Journal of Common Market Studies, VII (April, 1969), p. 293.

GDP among the less-developed regions of the world, nearly fifty per cent of Latin American imports consisted of chemicals, machinery, and transport equipment in 1961. Such critical imports constituted no more than one-third of total imports in any other less-developed region in 1961. Latin America's low ratio of imports to GDP and high ratio of critical imports to total imports was attributed to the past extensive use of IS in Latin America.[3] Referring back to Table 23 it can be seen that imports of chemicals, machinery, and transport equipment for Mexico in 1968 were 64.2 per cent of total imports.

Because of the extensive IS primarily for consumer goods and petroleum, Latin America's income elasticity of demand for imports $\left(\frac{\text{Percentage change in imports}}{\text{Percentage change in GDP}}\right)$ was relatively low for the period 1955 to 1961 (0.5 as calculated by Bela Balassa). But, because of the diminishing influence of IS in Latin America and the irreducibility of Latin America's critical imports, Bela Balassa forecasted a sharp rise in Latin America's income elasticity of demand for imports in the near future, from 0.5 to approximately 0.8. In the face of such a rapidly expanding demand for critical imports, Bela Balassa questioned the ability of Latin America to generate sufficient foreign exchange earnings to avoid a trade gap--an ever widening gap between

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[3]Bela Balassa, Trade Prospects for Developing Countries (Homewood, Illinois: Richard D. Irwin, Inc., 1964), p. 77.

Latin America's critical import needs and the ability to acquire enough foreign exchange to satisfy those needs. The result of this trade gap would be a slower rate of development for Latin America.[4]

Bela Balassa's forecast with respect to the growth of import demand in Latin America was essentially correct. Whereas the ratio of import growth to export growth for the period 1958-1963 for Latin America was $0.66\frac{(16\%)}{(24\%)}$, this same ratio was $1.64\frac{(41\%)}{(25\%)}$, for the period 1963 to 1968. As it can be seen, the change in this ratio between the two periods was entirely due to a rapid increase in imports for the region.[5]

In the cases of the three wealthiest countries of Latin America, Bela Balassa's forecast has been correct for Mexico and Argentina. Brazil has not experienced a significant change in its income elasticity of demand for imports. For Argentina and Mexico the income elasticity of demand for imports (as shown in Table 24) increased sharply from the period 1958-1963 to the period 1963-1968 (0.54 to 0.84 and 0.19 to 0.68 respectively). The ratio of imports to GDP, however, declined for both countries from 1958 to 1968, but the decline in this ratio was obviously slower during the period 1963-1968 than it was

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[4] Ibid., p. 78.

[5] Calculated from IMF, International Financial Statistics, XXIII, (July, 1970), No. 7, p. 220.

during the period 1958-1963. It is important to note that while the income elasticity of import demand for both Argentina and Mexico rose significantly between these time periods, each nation's propensity to export declined significantly between these time periods (2.70 to 0.73 and 0.84 to 0.24 respectively). It would appear that rising propensities to import in both Argentina and Mexico coincided with falling propensities to export. Such a situation strongly conforms to Bela Balassa's trade-gap hypothesis.

If Mexico's import needs continued to grow as they have in the past, then it would seem imperative that Mexico's export sector must rapidly accelerate its growth. As shown above, however, Mexico's export growth has decelerated in recent years. The seriousness of this trend is reflected by the fact that in 1968 the ratio of export earnings to import expenditures in Mexico was only 0.64, the lowest ratio among the LAFTA members.[6] Mexico has obviously expanded other sources of foreign exchange to finance these import expenditures. But an increasing reliance on sources of foreign exchange other than the export of goods and services often creates

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[6]This ratio was calculated from: IMF, International Financial Statistics, XXIII, No. 7 (July, 1970). Ratios of export earnings to import earnings for other LAFTA members, as calculated from this source, were: Argentina, 1.17; Bolivia, 0.96; Brazil, 0.88; Chile, 1.33; Colombia, 0.85; Ecuador, 0.93; Paraguay, 0.66; Peru, 1.37; Uruguay, 1.09; and Venezuela, 1.79.

TABLE 24

THE INCOME ELASTICITY OF DEMAND FOR IMPORTS AND THE PROPENSITY TO EXPORT OF ARGENTINA, BRAZIL, MEXICO
(Percentage changes are based on current dollars)

Country	$\frac{\text{Exports}}{\text{GDP}}$	$\frac{\text{Percentage Change in Imports}}{\text{Percentage Change in GDP}}$	
	1958 - 1968	1958 - 1963	1963 - 1968
Argentina[a]	7.4% 8.9%	$\frac{21\%}{39\%} = 0.54$	$\frac{161\%}{201\%} = 0.84$
Brazil[a]	4.9 4.5	$\frac{657}{812} = 0.81$	$\frac{449}{823} = 0.86$
Mexico[b]	7.2 4.6	$\frac{10}{51} = 0.19$	$\frac{58}{75} = 0.68$

[a]The last year reported is 1967 rather than 1968

[b]GNP rather than GDP is used.

SOURCES: Calculated from: International Monetary Fund, International Financial Statistics, XIX, No. 6 (June, 1969); International Monetary Fund, International Financial Statistics, XXIII, No. 7 (July, 1970).

TABLE 24--Continued

Percentage Change in Exports / Percentage Change in GDP				Imports / GDP	
1958 - 1963		1963 - 1968		1958	1960
105% / 39%	= 2.70	146% / 201%	= 0.73	9.1%	7.0%
762% / 812%	= 0.94	501% / 523%	= 0.96	7.9%	5.8%
43% / 51%	= 0.84	29% / 75%	= 0.39	11.0%	7.1%

undesirable long-run foreign exchange outflows which will, as it will be shown, further aggrevate an already aggrevated balance of payments position.

Mexico's export performance in recent years has also worsened relative to the performance of world exports. Mexico's share of world exports, as seen in Table 25, declined from 0.71 per cent in 1963 to 0.58 per cent in 1969. Similarly, Latin America's share of world exports has shown a steady decline from 6.74 per cent in 1963 to 5.43 per cent in 1969. The ratio of Mexican exports to Latin American exports remained fairly constant for the period 1963-1969, fluctuating between 10.00 per cent and 10.80 per cent.

Given the present composition of Latin America's exports, the ECLA has forecasted a Latin American balance of payments current account deficit of five billion dollars per annum by 1970.[7] Assuming that Mexico's current account deficit will grow for the next several years at its average annual growth rate for the period 1963-1968 (37.3 per cent) Mexico's current account deficit in 1970 would equal 1.42 billion dollars or 28.4 per cent of the forecasted Latin American current account deficit in 1970.[8]

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[7] U. N., The Process of Industrial Development in Latin America p. 239.

[8] Calculated from: IMF, International Financial Statistics, XXIII, No. 7 (July, 1970), p. 220.

TABLE 25

MEXICO'S DECLINING SHARE OF WORLD EXPORTS
(Exports, FOB, in millions of U.S. dollars)

Item	1963	1964	1965	1966	1967	1968	1969
World exports[a]	136,100	152,700	165,400	181,300	190,600	212,900	243,000
Latin America's[b] exports	9,180	9,860	10,380	11,040	11,030	11,570	. .
Mexico's exports	969	1,031	1,120	1,199	1,145	1,254	1,410[c]
Latin American Exports as a percentage of World Exports	6.74%	6.46	6.27	6.09	5.79	5.43	. .
Mexican exports as a percentage of World Exports	0.71%	0.68	0.68	0.66	0.60	0.59	0.58
Mexican exports as as a percentage of Latin American Exports	10.50%	10.00	10.70	10.80	10.30	10.80	. .

[a]Excludes the Soviet Bloc and Cuba.

[b]Excludes Cuba.

[c]IMF estimate.

Source: Calculated from: International Monetary Fund, International Financial Statistics, XXIII, No. 6 (June, 1970).

William Freithaler in his evaluation of Mexico's external sector in 1967 hypothesized that while Mexico had a rather large trade deficit, this posed no serious limitation on Mexico's present or future capacity to import.[9] In his opinion, Mexico was an example of a country that had escaped the implications of the trade gap hypothesis. His observations were based on three factors. First, the active use of IS during the period 1958-1963 had resulted in a virtual standstill in import growth (the value of imports increased by only ten per cent for the period).[10] Second, an active program of diversifying Mexico's largely agricultural exports had generated a respectable forty-three per cent growth in the value of Mexico's exports of goods for the period 1958-1963; a total percentage growth over four times greater than the growth of imports for the period.[11] As a result of these two trends, Mexico's trade deficit declined from 420 million dollars in 1957 to 263 million dollars in 1963.[12] Finally, and most importantly to William Freithaler, the rapid growth of alternative autonomous sources of foreign exchange, i.e., tourism, border trade, direct foreign investment, and long-term capital loan inflows, precluded the possibility

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[9]Freithaler, Mexico's Foreign Trade and Economic Development, p. 122.

[10]Table 24.

[11]Ibid.

[12]Calculated from: IMF, International Financial Statistics, XIX, No. 6 (June, 1966), p. 204; IMF, International Financial Statistics, XXIII, No. 7 (July, 1970), p. 220.

of future limitations in Mexico's capacity to import.

With respect to export and import growth trends, William Freithaler's hypothesis has obviously been incorrect. His observations concerning the growth of alternative autonomous sources of foreign exchange, however, bear further investigation. If the growth of alternative autonomous sources of foreign exchange has more than compensated for the growth of Mexico's trade deficit, then perhaps the need for a restructuring of the export sector has been overstated.

Trends in Mexico's balance of payments

Mexico's principle means of compensating for its trade deficit has been through the growth of travel balance surpluses and long-term capital surpluses in Mexico's balance of payments. Largely because of Mexico's proximity to the United States, travel balances are a very important item in Mexico's balance of payments current account. Travel balances include both net tourist trade income and net border trade income. The importance of travel balances in Mexico's balance of payments is illustrated by the fact that Mexico's gross tourist trade income and border trade income in 1968 (1,137 billion dollars) was 96.5 per cent as large as the total value of merchandise exports for that year. Moreover, Mexico's travel balance surplus in 1968 of 6.2 billion pesos (Table 26) compensated for

70.2 per cent of Mexico's trade deficit of 8.9 billion pesos for that year.

The growth rates of tourist trade and border trade have in recent years been more rapid than both the growth rates of exports of goods and imports of goods. For the period 1966 to 1969, gross tourist income increased from 328.4 million dollars to 465.0 million dollars, an increase of 41.5 per cent for the period.[13] Gross border trade income for the period 1966-1969 increased from 546.6 million dollars[14] to 744.0 million dollars, an increase of 32.0 per cent for the period.[15] In comparison, the growth of merchandise exports for the period 1966-1969 was 21.1 per cent and the growth of merchandise imports for this period was 29.0 per cent (Table 26).

The contribution of this rapid growth of gross travel income to Mexico's capacity to import has, however, been restrained

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[13] "The External Sector of Mexico's Economy, 1969," Comercio Exterior de Mexico, XVI, No. 4 (April, 1970), p. 3.

[14] Ibid.

[15] The growth of tourist income and border trade income for this period was highly influenced by the 1968 Olympics and "Operation Intercept" in 1969. In 1968 gross tourist income and gross border income both increased by 19.0 per cent reflecting the effects of the 1968 Olympics in Mexico. In 1969 gross tourist income and gross border trade income increased by 7.6 per cent, and 4.3 per cent respectively, reflecting the effects of "Operation Intercept." Calculated from: "The External Sector of Mexico's Economy, 1969," Comercio Exterior de Mexico, XVI, No. 4 (April, 1970), p. 3.

TABLE 26

MEXICO'S BALANCES OF PAYMENTS, 1963-1969
(Millions of Pesos, Current Prices)

	1963	1964	1965
Goods and Services			
Exports (FOB)	12,114	12,883	14,005
Imports (CIF)	15,496	18,662	19,495
Trade balance	- 3,288	- 5,562	- 5,388
Travel balance	3,838	4,088	4,000
Net investment income	- 3,325	- 4,050	- 4,238
Other current account items	262	375	138
Current account balance	- 2,513	- 5,149	- 4,888
Net transfers	-- 212	- 138	- 75
Net long-term capital	3,625	6,788	2,038
Net short-term capital	- 112	1,112	- 188
Net variation in official international reserves	- 1,562	- 575	725
Net errors and ommissions	775	- 2,038	2,388
Current account balance + net long-term capital	1,112	1,639	- 2,850

Notes:

The accounts may not balance because of rounding.

Sources: International Monetary Fund, International Financial Statistics, XXIII, No. 6 (June, 1970), pp. 223-224; "The External Sector of Mexico's Economy, 1969," Comercio Exterior de Mexico, XVI, No. 4 (April, 1970), p. 3.

TABLE 26--Continued

1966	1967	1968	1969	Total percentage change 1963-1968
14,985	14,314	15,674	18,135	29.4
20,065	21,823	24,501	26,005	58.1
- 4,888	- 7,688	- 8,875	. .	169.9
4,775	5,400	6,238	6,188	61.2
- 4,662	- 5,862	- 6,888	. .	107.2
250	138	138	. .	-47.3
- 4,525	- 8,012	- 9,387	. .	273.5
- 88	- 38	162	, ,	, ,
4,850	7,675	6,062	. .	67.2
1,775	88	- 2,588	. .	. .
262	- 962	- 1,000	. .	. .
2,275	1,250	6,750	. .	. .
325	- 337	- 3,325	. .	. .

by an even more rapidly growing gross outflow of travel expenditures. Whereas gross travel income increased by 38.2 per cent from 1966-1969, the gross outflow of Mexican travel expenditures increased by 49.1 per cent for the period: from 478.8 million dollars in 1966 to 714.0 million dollars in 1969 (tourist outflow and border trade outflows increased for the period by 72.0 per cent and 40.0 per cent respectively and totaled 234 million dollars and 480 million dollars respectively in 1969).[16]

An editorial in Comercio Exterior de Mexico has attributed much of the rapid rise in Mexico's outflow of tourist expenditures to Mexico's distribution of income, and has forecasted a doubling of travel expenditure outflows every three years. In 1969 only one-half of one per cent of Mexico's population traveled abroad. These Mexican tourists numbered only ten per cent of the foreign tourists visiting the interior of Mexico, yet they spent fifty per cent as much as the total tourist expenditure inflow. In other words, the average Mexican tourist in 1969 spent five times more money travelling abroad than the average tourist visiting the interior of Mexico. The Comercio Exterior de Mexico editorial concluded that, "It became increasingly evident in 1969 that outflow is growing far more quickly than income, with an ensuing decline in the services account surplus."[17]

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[16] Ibid.

[17] Ibid., p. 4.

As it can be seen from Table 26, the travel balance did in fact decline in 1969 by 0.8 per cent (from 6,238 million pesos in 1968 to 6,188 million pesos in 1969.

It would appear that the ability of travel balance surpluses to keep pace with trade balance deficits is diminishing. While the travel balance surplus of 1963 more than compensated for the trade balance deficit for that year (Table 26) the subsequent growth of the trade balance deficit (169.9 per cent for the period 1963-1968) has been much more rapid than the subsequent growth of the travel balance surplus (62.5 per cent for the period 1963-1968). The results of these trends have obviously contributed to Mexico's growing current account deficit.

Long-term capital inflows (primarily long-term loans and direct foreign investment) in Mexico constitute the remaining major autonomous source of foreign exchange for Mexico. It has, however, become increasingly apparent to Mexico and to Latin America as a whole that while inflows of long-term capital have contributed to their capacity to import through inflows of foreign exchange, inflows of long-term capital have also created a rapidly growing and rather irreducible outflow item in the form of foreign remittances of profits and interest on foreign investments and loans.

The ECLA observed in 1968 that Latin America's financial services for amortization, profits, and interest on foreign investments

and loans increased far more than Latin America's export earnings for the period 1960 to 1966. The latter increased by 35 per cent while remittances of profits and interest rose by 67 per cent, and amortization payments on autonomous loans increased by 41 per cent. The ECLA concluded that, "In short, these financial services in 1966 absorbed a third of the total value of income from exports of goods. For this reason imports have been unable to grow at the same pace as export earnings."[18]

Referring to Table 26 it is apparent Mexico's experience has been similar to that of Latin America, with the net outflow of investment income (interest, profits, and dividends) for 1968 (6,888 million pesos) absorbing 43.8 per cent of Mexico's total income from the export of goods for 1968 (15,674 million pesos). If the amortization payments on long-term loans for 1968 (6,464 millions of pesos)[19] are added to the net outflow of investment income for that year, it is found that the total financial service payment of 13,352 million pesos absorbed 85.2 per cent of the total income from exports of goods.

Comparing financial services outflows to the earnings from the export of goods, however, is rather misleading. Certainly

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[18] U. N., Economic Survey of Latin America, 1967, p. 93.

[19] Mexico, Anuario Estadistico del Comercio Exterior de los Estados Unidos Mexicanos, 1968, p. 720.

outflows from financial services have compounded Mexico's current account deficit, but these financial services have resulted from substantial inflows of foreign currency in the form of direct foreign investment and long-term loans. It would therefore be more logical to compare these outflows from financial services to the inflows of foreign exchange from direct foreign investment and other long-term capital inflows.

The total net inflow of long-term capital (discounted by amortization payments) for Latin America during the period 1961 to 1968 was 11,493 million dollars as seen in Table 27. The remittance of profits and interest on long-term foreign capital for this period, however, totaled 14,741 millions of dollars. The net result of these transactions for this period was, therefore, 3,256 million dollar outflow. It is significant to note the instability of the growth of the long-term capital balance during the period 1961-1968, and the fact that net long-term capital and investment income balances were negative in seven of the eight years examined.

Comparisons of long-term capital inflows and investment income outflow, such as those above, have been the focus of a great deal of concern in Latin America. Long-term capital inflows, while being a major credit in Latin America's balance of payments, are also the initiating sources of investment income outflows. In past years, the investment income outflows have been greater than new

TABLE 27

LATIN AMERICA'S LONG-TERM CAPITAL INFLOWS AND INVESTMENT INCOME OUTFLOWS FOR THE PERIOD 1961-1968
(Millions of Dollars, Current Prices)

Year	Long-term Capital Balance (Amortization deducted)	Investment Income Balance	Net Balance (Col. 2-Col. 3)
1961	1,036	- 1414	- 378
1962	921	- 1521	- 600
1963	870	- 1479	- 621
1964	1,595	- 1730	- 135
1965	1,018	- 1851	- 833
1966	1,740	- 2111	- 371
1967	1,658	- 2294	- 636
1968	2,655	- 2337	318
Total	11,493	-14,741	- 3,256

Source: Banco Interamericano de Desarrollo, "Contribucion Financiero de Europa al Desarrollo y la Integracion de America Latina," Boletin de la Integracion, V, No. 52 (April, 1970), p. 198

long-term capital inflows and some Latin America economists feel that this problem will be even more serious in the future. Jorge Marshall, the Director of Studies for the Central Bank of Chile, has forecasted a total net balance deficit (long-term capital balance-investment income balance) for Latin America for the period 1969-1973 of 3,565 million dollars.[20]

[20]Jorge Marshall, "El Model de Las Dos Brechas Como Medio de Cuantificar Los Requerimientos de Recursos Externos de America

This growing gap between long-term capital inflows and investment income outflows has prompted some Latin American economists to question the contribution of long-term capital flows to Latin America in that such flows have created a large and rather irreducible liability which serves to reduce Latin America's over all capacity to import. Such evaluations, however, are in error. Flows of investment income come from stocks of long-term capital, not the annual inflows of long-term capital. Also, the productive aspect of these long-term capital flows is ignored, attention being concentrated only on their contribution of foreign exchange to Latin America's capacity to import. A determination of the total contribution of long-term capital inflows to Latin America's development would, therefore, have to consider the total productive effects of the long-term capital stock.

Net long-term capital inflows for Mexico have, in recent years, been greater than net investment income outflows but by a very small margin. The total outflow of net investment income for Mexico during the period 1963-1968 was 29, 025 million pesos, while the total net inflow of long-term capital was 31, 038 million pesos; leaving a net contribution to Mexico's capacity to import of 2, 013 million pesos for the period (Table 26). This surplus item of 2, 013 million pesos

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Latin" Revista de la Integracion, No. 6 (May, 1970), p. 62.

represented only 5.6 per cent of Mexico's trade balance deficit for the period 1963-1969. As in the case of Latin America, Mexico's long-term capital surplus has shown a rather sporadic growth, while the investment income deficit has experienced a very steady growth (averaging 13.8 per cent per year). The result has been a large fluctuation from year to year in the net contribution of these two accounts to Mexico's capacity to import, a factor not conducive to a steady pattern of national growth.

Direct foreign investment in Mexico, as seen in Table 28, experienced a very sporadic growth after 1961. Moreover, remittances from direct foreign investment in the form of remitted profits and dividends were greater than new flows of direct foreign investment for the period 1960-1968 by 2,070 millions of pesos.

To some degree the inability of Mexico's current account and private long-term capital inflows to generate sufficient foreign exchange to satisfy Mexico's import needs can be compensated for by Mexico's aquisition of long-term loans. A Comercio Exterior de Mexico editorial in 1969 pointed out, however, that:

> The continued uneasiness of the international monetary system, exemplified by--among other things--the persistence of high interest rate levels, may in the near future, seriously diminish Mexico's capacity to obtain capital in the international market. It therefore becomes increasingly imperative to adopt adequate measures regarding current transactions in order to ensure a rapidly expanding export volume of merchandise and services which would permit

Mexico to finance its legitimate import needs. . . .[21]

It would seem reasonable to conclude that Mexico will not be able to further rely on either travel balances or net investment income long-term capital balances to offset a growing trade balance

TABLE 28

DIRECT FOREIGN INVESTMENT AND REMITTANCES IN MEXICO
(Millions of Pesos, Current Prices)

Year	Direct Foreign Investment	Total Remittances	Total Direct Foreign Investment Minus Remittances
1950	758.3	603.8	- 154.5
1960	980.3	1,637.5	- 657.2
1961	1,490.7	1,536.1	- 45.4
1962	1,581.1	1,539.4	41.2
1963	1,468.5	1,871.1	- 402.6
1964	2,024.3	2,385.8	- 361.5
1965	2,673.5	2,286.2	387.5
1966	2,316.1	2,256.8	59.3
1967	1,652.0	2,036.1	- 411.1
1968	2,837.5	3,517.9	- 680.4

Note:
Foreign direct investment includes intercompany accounts and reinvestment.

Sources: Calculated from: International Monetary Fund, Balance of Payments Yearbook, 1964-1968, XXI (November, 1969); International Monetary Fund, International Financial Statistics, XXIII, No. 6 (June, 1970).

[21] "The External Sector of Mexico's Economic Economy in 1968," Comercio Exterior de Mexico, XVI, No. 4 (April, 1969), p. 3.

deficit. Assuming that Mexico's import needs will continue to grow as they have in the past few years the main thrust in providing a satisfactory capacity to import must come from growth in Mexico's exports of merchandise. That growth, in recent years, has not been satisfactory.

Determinants of the performance of Mexico's export sector

It may be concluded from the above discussion that Mexico's export sector in recent years has performed poorly in terms of keeping pace with import growth, in terms of maintaining its share of world exports, and in terms of absolute growth. Moreover, it was shown that the performance of exports for Latin America in general has also been unsatisfactory.

One major determinant of the unsatisfactory performance of both Latin America's exports and Mexico's exports has been the composition of those exports. In 1968, approximately 85 per cent of Latin America's exports and 75 per cent of Mexico's exports consisted of foodstuffs and raw materials. These high concentrations of primary exports are both a product of the structure of the Latin American economies previous to 1940 and subsequent industrialization efforts on the part of the Latin American countries. In general, the economies of the Latin American nations before 1940 were close approximations of the idealized types of economies one might expect

to evolve from an international division of labor. The Latin American nations generally specialized to a high degree in the production of primary products for export while satisfying their demand for manufactured goods through imports from the industrialized nations. As it was pointed out in Chapter III, slightly over twenty-five per cent of the goods consumed in Latin America in 1928 were imported.

Because of shortages of foreign exchange during the world depression of the 1930's and the unavailability of manufactured imports during World War II the Latin American nations were forced to develop internal industries to satisfy their domestic demand for manufactured goods. In subsequent years industrialization efforts intensified though an active persuance of IS with the result that the Latin American countries now possess large manufacturing sectors producing a wide range of consumer and producer goods. The export sectors of the Latin American countries have not, however, changed significantly since 1930. Faced with the competition of the industrialized nations, the traditions attached to the export of primary products, a governmental industrialization program characterized by "inward" incentives, and the high industrial costs generated by such a program, few Latin American manufacturers ventured into the high-risk export sector. Most of the Latin American countries viewed their export sectors as simply a source of foreign exchange by which essential capital imports might be obtained. As long as primary product exports

could provide an adequate flow of foreign exchange and as long as "inward" industrialization was successful, there was little clamor for a restructuring of their exports.

In addition to being largely primary products, Latin America's exports also have little diversification. For seven of the eleven LAFTA members, one commodity export accounted for over forty per cent of their total export earnings in 1969 (Table 29). In the aggregate, four of the commodities listed in Table 29 (petroleum, coffee, cotton, and copper) accounted for 50.3 per cent (5.2 billion dollars) of the total LAFTA members exports in 1968 (10.3 billion dollars). Of all the LAFTA members listed in Table 29 only one country, Mexico, did not have three principal commodity exports generating over fifty per cent of total export earnings in 1968.

All of the Latin American countries are attempting to diversify their export base and to a limited degree some of the Latin American countries have been successful in their attempts at diversification. The country that has had the greatest success in diversifying its primary product exports has been Mexico. As seen in Table 29, Mexico's seven largest commodity exports in 1968 constituted only 37.7 per cent of the total value of Mexico's exports in 1968. A Committee for Economic Development (CED) index of export diversification of less-developed countries for 1964-1965 showed that Mexico had the greatest degree of export diversification in Latin

TABLE 29

PRINCIPAL COMMODITY EXPORTS FOR SELECTED LATIN AMERICAN COUNTRIES FOR 1968
(Millions of Dollars, Current Prices)

	EXPORTS		
Country	Type	Value	Percentage of Total
Argentina	Meat	335.0	24.5
	Cereals	276.9	20.2
	Wool	105.8	7.7
	Hides	72.0	5.3
	Total	1,367.9	. .
Bolivia	Tin	92.5	52.6
	Total	175.7	. .
Brazil	Coffee	744.1	41.1
	Cotton	131.0	7.0
	Cacao	46.0	2.4
	Total	1,881.0	. .
Chile	Copper	684.0	76.6
	Nitrates	14.6	1.6
	Total	892.9	. .
Colombia	Coffee	351.4	62.9
	Petroleum	36.3	6.5
	Total	588.3	. .
Ecuador	Bananas	104.8	52.1
	Coffee	39.8	19.8
	Cacao	24.9	12.4
	Total	201.0	. .

TABLE 29--Continued

Country	Type	EXPORTS Value	Percentage of Total
Mexico	Cotton	170.5	13.6
	Coffee	77.5	6.2
	Lead	22.7	1.8
	Copper	7.2	0.6
	Zinc	47.4	3.8
	Sugar	96.0	7.7
	Shrimp	49.6	4.0
	Total	1,254.9	. .
Paraguay	Meat	13.5	28.4
	Wood	8.0	16.8
	Tobacco	4.5	9.5
	Total	47.6	. .
Peru	Copper	234.0	27.1
	Fishmeal	156.5	18.1
	Cotton	55.8	6.5
	Silver	68.0	7.9
	Sugar	62.3	7.2
	Total	865.0	. .
Uruguay	Wool	78.0	43.6
	Meat	60.3	33.7
	Total	179.1	. .
Venezuela	Petroleum	2,652.5	93.0
	Total	2,854.7	. .

Sources: Calculated from: International Monetary Fund, International Financial Statistics, XXIII, No. 6 (June, 1970).

America.[22] As it will be shown, however, Mexico's program of export diversification has largely focused on the development of "minor" agricultural exports such as shrimp, tomatoes, meat products, and other assorted foodstuffs, rather than manufactured goods.

One final characteristic of Latin America's exports should be analyzed--their market. In 1968, 66.4 per cent of Latin America's highly concentrated primary product exports went to the United States, the European Free Trade Association (EFTA) and the five members of the European Economic Community (EEC).[23] The market for Mexican exports in 1968 showed an even higher concentration as seen in Table 30. In 1968, 79.5 per cent of Mexico's exports went to the United States, the EFTA, and the EEC. The United States alone absorbed 68.2 per cent of Mexico's exports in 1968. Moreover, Mexico's exports to the United States in 1968 were largely foodstuffs (52 per cent of exports) and raw materials (12 per cent of exports).[24]

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[22] Committee for Economic Development, Trade Policy Towards Low Income Countries (New York: Committee for Economic Development, 1967), p. 39.

[23] Calculated from: International Monetary Fund, Direction of Trade Annual, 1964-1968, VI (1970).

[24] "Mexico's Trade with the U.S.," Review of the Economic Situation of Mexico, XLVI, No. 529 (December, 1969), p. 6.

TABLE 30

THE DIRECTION OF MEXICO'S TRADE IN 1968
(Millions of Pesos)

	Exports		Imports	
	Value	Percentage of total	Value	Percentage of total
Total	15,674.0	100.00	24,501.0	100.00
American, excluding Latin America	9,046.6	69.79	15,899.1	64.89
United States	8,840.7	68.20	13,416.8	63.00
LAFTA	778.0	6.00	535.7	2.18
CACM	227.6	1.76	25.4	0.12
Rest of Latin America	254.4	1.96	85.0	0.35
Eastern Europe	43.4	0.34	70.2	0.29
EEC	759.4	5.86	4,024.2	16.42
EFTA	717.2	5.53	2,108.2	8.60
Rest of Western Europe	96.5	0.74	409.7	1.67
Asia, excluding the Middle East	975.9	7.53	1,095.7	4.50
Middle East	4.3	0.03	6.7	0.03
Africa	23.0	0.18	12.5	0.05
Oceania	36.3	0.28	228.9	0.93

Notes: The data given may not total correctly and it may not completely agree with other data in this paper because of rounding and because this data has not been re-valuated by Mexico.

Source: Calculated from: Mexico, Secretaria de Industria y Comercio, Anuario Estadistico del Comercio Exterior de los Estados Unidos Mexicanos, 1968 (Mexico, D.F.: Talleres Gráficos de la Nación, 1969).

It should also be pointed out that Mexico, like Latin America in general, has incurred heavy trade deficits with its major trading partners. Mexico's trade deficit with the United States, the EFTA, and the EEC in 1968 amounted to 9,231.9 million pesos, a deficit equal to 105 per cent of Mexico's total trade deficit for that year.

In conclusion, it can therefore be said that Latin America's exports consist largely of primary product. Moreover, most of the Latin American countries rely on only a few primary product exports for the most of their export earnings, and they sell most of these exports to the industrialized countries of the Atlantic community, (the United States, the EFTA, and the EEC). While Mexico has achieved a greater degree of export diversification than other Latin America countries, Mexico's export sector still exhibits most of the characteristics of the exports of Latin America as a whole. Mexico's exports are predominately primary products, and these exports are largely sold to the industrialized countries of the Atlantic community, primarily to the United States.

The characteristics of Latin America's exports, as discussed above, have been the basis of a general theory attempting to explain the poor performance of Latin America's exports--the structuralist theory. The structuralist theory attempts to demonstrate that the poor performance of Latin America's exports in terms of growth and stability has been largely due to the structure of those exports and the

structure of world trade. The structuralist generally holds to the premise that an international division of labor, such as that approximated by the primary product exports of the less-developed countries and the manufactured exports of the industrialized countries, brings forth structural forces that create a situation where benefits of trade are not distributed alike over the whole community, but tend to flow from the less-developed countries to the industrialized countries. The explanation of this phenomena is generally contained in what has been called the Prebish Thesis.[25]

The Prebish Thesis and other structuralist theses hypothesize that structure obstacles to the performance of the exports of less-developed countries manefest themselves in three ways. First, the

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[25]The Prebish Thesis has had its basic derivation from Raul Prebish's work with the ECLA and through his writings, such as, "Commercial Policy in the Underdeveloped Countries," American Economic Review; Papers and Proceedings, XLIX, No. 2 (May, 1959), pp. 251-273. While the Prebish Thesis specifically refers to the declining term of trade of less-developed countries, it has, however, been expanded and clarified by other economists so that the Prebish Thesis is now associated with a whole host of hypotheses concerning structural obstacles to the development of less-developed countries created through their interaction with developed countries. Different aspects of the generalized Prebish Thesis can be found in the following writings: Hans. W. Singer, "The Distribution of Gains Between Investing and Borrowing Countries," American Economic Review; Papers and Proceedings, XL, No. 2 (May, 1950), pp. 473-485; Gunnar Myrdal, Rich Lands and Poor (New York: Harper and Brothers, 1957): and Louis J. Zimmerman, Poor Lands, Rich Lands: The Widening Gap (New York: Random House, 1965). Therefore, when the Prebish Thesis is referred to in this paper, it may not be with strict reference to Raul Prebish's original formulation.

presence of these structural obstacles has resulted in a high degree of fluctuation in commodity prices. Such instability in export commodity prices for less-developed countries causes serious fluctuations in the foreign exchange earnings of such countries which adversely influences economic and social development plans. Second, the presence of these structural obstacles has seriously retarded the ability of less-developed countries to expand their exports of primary products. Finally, the presence of these obstacles has resulted in a reduced per unit purchasing power of primary product exports through a declining commodity terms of trade $\frac{\text{(average price of exports)}}{\text{(average price of imports)}}$. In some cases, where the commodity terms of trade have decreased at a faster rate than the rates of increase in the volume of primary product exports, the income terms of trade $\frac{\text{(average price of exports}}{\text{(average price of imports}}$ X volume of exports) have also declined for less-developed countries. Such a decline in the income terms of trade is equated with an absolute decline in a country's capacity to import from exports.

The structural obstacles referred to above and the effects that they have had on Latin American and Mexican export performance can be best examined by discussing each of the three manefestations of these structural obstacles.

Fluctuations in commodity prices

The causes for fluctuations in commodity prices can be

grouped into supply and demand factors.[26] The primary supply factors are: (1) climate variations affecting the volume of production and prices of primary products according to their price elasticity of demand; (2) the existence of production cycles for some primary products spanning several years; (3) a low elasticity of production due to production cycles and a lack of willingness by primary product producers to reduce production in the face of unfavorable supply trends; and (4) the protection of domestic primary product prices in developed countries in the face of market gluts, which places the entire weight of adjustment on the exports of such products from the less-developed countries.

The primary demand factors responsible for fluctuations in commodity prices are: (1) the price in elasticity of demand for many primary products which serves to intensify price changes resulting from supply shifts; (2) the effects of wars on the demand for primary products; (3) the inventory policies of industries in industrialized countries that tend to intensify price movements resulting from other causes, i. e., stocks of primary products are increased when primary product prices go up, and inventories are reduced when primary product prices fall; and (4) the business cycles of the industrialized

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[26] Romulo A. Ferrero, "The International Trade of Latin America," Regional Integration and the Trade of Latin America, Translation of a study by the Inter-American Council for Commerce and Production (New York: Committee for Economic Development, 1968), p. 52.

countries which have a multiplier effect on their demand for primary product inventories.

The degree to which the above supply and demand factors affect any countries commodity export prices will depend, of course, on the types of commodities that country exports and the degree of diversification of those exports. Romulo A. Ferrero has observed that:

> Which cause of price unstability has greater or lesser importance will vary with the circumstances and products involved. The elasticity of supply and demand depends on the product. As a rule, elasticity of supply is greater for agricultural products with an annual production cycle than for those with a longer cycle. Elasticity of demand is higher for raw materials than for foodstuffs. Supply fluctuations tend to produce price changes in a compensatory manner: If supply increases, prices fall, and vice versa. Fluctuations in demand, however, tend to create price changes in a different manner: If demand decreases so do prices.[27]

The degree to which those forces discussed by Romulo Ferrero have affected Mexico's export prices in recent years can best be analyzed by first examining the price stability of Mexico's major exports, and then by examining the overall stability of Mexico's export prices in comparison with the export price stability of several industrialized nations and other Latin American countries.

The values of Mexico's major commodity exports, as seen in Table 31, have in most cases shown a high degree of instability in

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[27] Ibid., p. 54.

TABLE 31

THE PRICE STABILITY OF MAJOR MEXICAN COMMODITY EXPORTS
(1963 = 100)

Commodity	1963	1964	1965	1966	1967	1968
Cotton						
Value	100	86	108	113	73	87
Volume	100	86	111	116	73	85
Price	100	100	97	97	100	102
U.S. import price (15 markets)	100	96	90	79	68	77
Coffee						
Value	100	190	148	170	122	157
Volume	100	151	117	139	112	143
Price	100	126	126	122	110	110
U.S. import price (Brazil)	100	139	131	120	111	110
Lead						
Value	100	85	101	100	86	82
Volume	100	77	78	83	70	70
Price	100	110	129	120	123	117
U.S. import price (World)	100	159	180	146	129	130

TABLE 31--Continued

Commodity	1963	1964	1965	1966	1967	1968
Zinc						
Value	100	142	143	150	148	158
Volume	100	91	86	90	85	90
Price	100	156	166	167	174	176
U.S. import Price (World)	100	110	118	118	113	110
Sugar						
Value	100	130	106	96	110	130
Volume	100	130	132	138	144	157
Price	100	100	80	81	76	83
U.S. import Price (Carribean)	100	86	84	86	90	91
Shrimp						
Value	100	78	76	91	102	86
Volume	100	93	78	86	93	73
Price	100	84	97	106	110	118

Source: Calculated from: International Monetary Fund, International Financial Statistics, XXIII, No. 7 (July, 1970).

recent years. In the case of cotton, the export value index (1963 = 100) for the period 1963-1968 showed wide fluctuations: decreasing from 100 in 1963 to 86 in 1964, increasing to 113 in 1966, falling to 73 in 1967, and increasing to 87 in 1968. Most of the variation in the value of cotton exports was due, however, to highly unstable cotton export volumes due to climatic factors. The prices of Mexico's cotton exports remained remarkably stable for this period in view of the high instability of world cotton export prices (derived from the 15 market United States' import price). In the case of Mexico's coffee exports, fluctuations in the value of exports can be attributed to both fluctuations in export volumes and export prices for the period 1963-1968. In general, however, price movements were neither compensatory or reinforcing to changes in the volume of exports, which were much more eratic than price movements. Following the same general trend as the United States' import prices for Brazilian coffee, Mexico's coffee prices rose from 100 (using an index where 1963 prices equal 100) in 1963 to 126 in 1964-1965, and then fell to 110 in 1968.

In the case of Mexico's lead exports, fluctuations in export prices tended to be compensatory to fluctuations in export volumes until 1968. The degree of price compensation was not great enough, however, to prevent a high degree of instability in the value of lead exports. In general, fluctuations in the price of Mexico's lead

exports were not as great as those of the United States lead import prices. In the case of zinc, Mexico's export prices tended to be compensatory to changes in the volume of zinc exports with the result that the value of zinc exports increased rapidly for the period 1963-1968.

In the case of sugar, Mexico's export prices were also compensatory to changes in the volume of sugar exports. While the volume of sugar exports increased by 57 per cent for the period 1963-1968, the price of sugar decreased from an index value of 100 in 1963 to 83 in 1968. Despite the compensatory movement of export prices, the value of sugar exports still displayed a high degree of instability: increasing from an index value of 100 in 1963 to 130 in 1964, falling to 96 in 1966, and rising to 130 in 1968. As in the case of coffee export prices movements in Mexico's shrimp export prices were rather independent from changes in the volume of shrimp exports for the period 1963-1968. Both shrimp export prices and export volumes fluctuated widely for the period with the result that the value of shrimp exports displayed a highly unstable pattern of growth for the period.

It might be concluded from the above discussion that except for cotton prices and zinc prices, the prices of Mexico's major commodity exports exhibited a rather high degree of instability during the period 1963 to 1968. In the case of zinc and sugar, price movements

were largely compensatory. For the other commodities discussed, no such relationship between prices and volumes of exports is apparent.

The greater the degree to which a country relies on the export earnings of just a few commodities, the greater becomes the chance that overall export performance will be marked by instability in export prices, volumes, and values. To minimize the effects of the instability of commodity export prices and values on a country's total export earnings, it is advisable that a country diversify its export base, and as it was stated before, Mexico has the most diversified export base in Latin America.

The price fluctuations of Mexico's total exports for the period 1958-1966 as well as the price fluctuations of the exports of the developed countries, the less-developed countries, Latin America, the United States, and some of the larger Latin American countries can be observed in Table 32. It should first be noted that the stability of export prices is partially a function of the size of the economic unit discussed. Obviously, in an economic unit such as "the developed countries" a very high degree of export diversification is implicit, yielding probably a greater degree of export price stability than the majority of the individual developed countries would possess. It is, therefore, unwise to compare export price stability for such a large economic unit to export price stability for any one country.

TABLE 32

THE COMPARATIVE PRICE STABILITY OF MEXICO'S EXPORTS (1958 = 100)

Country or region	1958	1959	1960	1961	1962
Developed countries	100	95	98	101	98
Less-developed countries	100	97	99	96	94
Latin America	100	93	94	93	91
United Kingdom	100	99	101	101	102
United States	100	100	101	103	102
France	100	93	96	96	96
Germany	100	99	101	106	107
Mexico	100	95	98	101	98
Argentina	100	103	108	107	99
Brazil	100	85	83	85	80
Chile	100	111	115	108	110
Colombia	100	87	87	84	80
Peru	100	102	103	100	103

Sources: Calculated from: International Monetary Fund, International Financial Statistics, XXI, No. 6 (June, 1968); United Nations, Economic Commission for Latin America, Economic Survey of Latin America, 1967 (E/CN. 12/808/Rev. 1), 1969.

TABLE 32--Continued

1963	1964	1965	1966	Mean value	Average deviation
106	112	108	110	102	2.0
96	100	102	103	99	2.4
93	101	102	105	97	4.6
105	107	109	113	104	3.9
102	103	106	107	103	1.9
96	98	101	102	98	2.4
106	107	109	111	105	3.1
106	112	108	110	103	5.1
108	119	119	154	113	11.8
83	95	100	100	90	7.7
110	117	127	. .	112	5.5
78	92	91	87	87	4.7
107	121	122	138	111	11.0

In comparing the developed countries to the less-developed countries (Table 32) it can be observed that there was no significant difference between the export price stability of the former countries and the latter countries as measured by the average derivation of export prices from the mean for the period 1958-1966 (2.0 versus 2.4 respectively). It should be noted, however, that the mean value of export prices for the developed countries for the period was 103 (1958 = 100) as opposed to a mean value of export prices for the less-developed countries of 99. This illustrates the often neglected point that a high degree of export price fluctuation around an upward moving mean export price may certainly be more desirable than a low degree of export price fluctuation around a diminishing mean export price.

Fluctuations in the prices of Latin American exports appear to have been much greater (4.6) than export price fluctuations for both the developed and less-developed countries for the period 1958-1966. It should also be noted that Latin America's mean export price for the period was only 97. Export price stability for the larger Latin American countries varied considerably for the period 1958-1966. While Colombia's export price average derivation was relatively low (4.7), Colombia's mean export prices was also low (87). It would therefore be unwarranted to say that Colombia achieved a more satisfactory export performance than, for example, Argentina. While Argentina had a high degree of export price instability for the period

(11.8), Argentina also experienced a sharp rise in export prices with a mean export prices for the period of 113.

In comparison to the other Latin American countries listed in Table 32, Mexico's export prices were relatively stable (5.1) for the period 1958-1963. Moreover, this stability occurred around an upward moving mean export price (103). In comparison to the export price stability of the United States (1.9), the United Kingdom (3.9), France (2.4), and Germany (3.1), the stability of Mexico's export prices, however, shows much room for improvement.

The degree to which export price fluctuations affect a country's development efforts is a subject for conjecture. That such fluctuations are harmful can, however, be verified by the efforts of less-developed countries to establish commodity agreements (such agreements exist for coffee, sugar, tin, and wheat) and to diversify their export bases.

Mexico has been relatively successful in diversifying its export base. The effects of this diversification can be seen in the relative stability of Mexico's export prices by Latin American standards. By Western European and United States standards, however, greater progress in export price stabilization can still be made in Mexico.

The structuralist argument, however, goes far beyond the hypothesis that structural forces exist which give rise to fluctuations

in commodity export prices. As stated before, the structuralist also argue that the presence of structural obstacles has seriously retarded the ability of less-developed countries to expand their exports of primary products. It is this argument that we will now examine.

Obstacles to the expansion of Latin America's and Mexico's exports

The apparent inability of Latin America's export earnings and Mexico's export earnings to keep pace with the growth of world export earnings has been primarily attributed, by the structuralists, to the existence of structural demand obstacles which have served to retard the growth of primary product exports. Foremost among these obstacles is the often cited low income elasticity of demand of the industrialized nations for food product and raw material exports of less-developed countries.

According to Raul Prebisch, for every one per cent of per capita increase of income in the United States, imports of primary goods tend to increase by only 0.6 per cent, while imports of manufactured goods tend to increase by over one per cent.[28] If this is true, then it is understandable why Latin America's share and Mexico's share of world trade have been declining. It is also important to note that as a country becomes wealthier, its income elasticity of demand

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[28]As cited in: Zimmerman, Poor Lands, Rich Lands: The Widening Gap, p. 160.

for primary products in general appears to decline while its income elasticity of demand for manufactured goods appears to remain stable or to even to increase during the earlier stages of development. This would seem to indicate that, ceteris paribus, the rate of the decline in Latin America's share and Mexico's share of world exports will probably increase as the world income increases. As seen in Table 31, there appears to be a strong inverse relationship between a country's income elasticity of demand for food products and raw materials and that country's per capita income, i. e., the higher the country's per capita income, the lower becomes that country's income elasticity of demand for primary products. It can be observed from Table 33 that in such high per capita income countries as the United States, the principal market for Mexico's exports increased growth in per capita income will result in virtually no increase in the demand for many primary products. Increases in the demand for such primary products in the United States will therefore be largely limited to the population growth rate.

Those factors most often cited as contributing to the low income elasticity of demand for primary products are: (1) the effects of Engel's Law on the demand for agricultural foodstuffs; (2) the substitution of synthetics for natural raw materials in various production processes; (3) the minimization of raw material inputs per unit of product output by industry through technology; and (4) the shift toward

TABLE 33

PROJECTED 1970 INCOME ELASTICITIES OF DEMAND FOR SELECTED PRIMARY PRODUCTS

Country or Region	Product				
	Sugar	Coffee	Cacao	Fibers	Calories
Southeast Asia	1.3	1.5	0.8	1.1	0.6
Japan	0.8	1.5	0.7	0.9	0.2
Mediterranean countries	0.8	1.0	0.5	0.8	0.2
E.E.C. Countries	0.5	0.6	0.3	0.5	0.1
United States	0.0	0.3	0.1	0.0	- 0.03

Source: Louis J. Zimmerman, Poor Lands, Rich Lands: The Widening Gap (New York: Random House, 1965), p. 160.

less material-intensive products in manufacturing.

With respect to the effects of Engel's Law on the demand for agricultural foodstuffs, it has been often observed that the per capita consumption of such agricultural products as meats (other than beef), wheat and other grains, sugar coffee, and cocoa has tended to remain constant or decrease over long period of time in the highly industrialized nations. For example, the per capita annual consumption of sugar in the United States in 1930 was 110 pounds, while the per capita annual consumption of sugar in 1964 in the united States was

only 96 pounds. Similar changes in the United States' per capita annual consumption occurred for the following products: meats (other than beef), 80 pounds in 1930 to 73 pounds in 1964; wheat, 174 pounds in 1930 to 119 pounds in 1964; and other grains, 67 pounds in 1930 to 44 pounds in 1964.[29]

Changes in industrial raw material requirements in industrialized nations have also retarded their demand for primary products. Bela Balassa largely attributed the poor performance of agricultural raw material exports from 1955 to 1961 (the value of such exports declined by five per cent during that period) to the effects of synthetic substitution for raw materials on the demand for agricultural raw materials by the developed countries. Bela Balassa observed that whereas synthetic rubber production was negligable in 1938, by 1955 the share of natural rubber in rubber consumption fell to 42 per cent in the United States. During the same period of time the share of cotton and wool in the fiber consumption of the United States and Western Europe fell from ninety per cent to seventy-two per cent.[30] The OAS has reported that while the overall consumption of fibers in

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[29] OAS, The Alliance for Progress and Latin American Development Prospects: A Five Year Review, 1961-1965, p. 68.

[30] Balassa, Trade Prospects for Developing Countries, p. 6.

the United States increased at the annual rate of four per cent between 1959 and 1964, the overall consumption of cotton and wool nearly remained stationary between 1959 and 1964. Almost the entire increase in the United States' textile fiber consumption for this period was accounted for by synthetic fibers.[31]

The degree to which any of the above mentioned four factors has contributed to low income elasticities of demand for primary products in the developed countries is conjectural. That the income elasticity of demand for primary products in developed countries is low, however, is an accepted fact.

The growth of world demand for primary product exports from Latin America and Mexico faces, however, greater obstacles than the low income elasticity of demand for primary products. Another major obstacle to the growth of demand for Latin American and Mexican primary product exports is to be found in the protectionalist commodity policies of the developed nations. The industrialized countries employ a whole series of highly protectionist commodity measures--high import duties, customs preferences, quantitative restrictions, subsidies to domestic production and export, and export sales of agricultural surpluses on very favorable terms. While some of these measures serve to directly exclude Latin American and

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[31]OAS, The Alliance for Progress and Latin American Development Prospects: A Five Year Review, 1961-1965, p. 68.

Mexican exports from domestic markets, other measures, such as the promotion of domestic commodity production and export, and the granting of exclusive trade preferences, serve to indirectly reduce the market potential of Latin American and Mexican exports.

Latin American economists have focused a great deal of world attention on the high import duties that some industrialized nations impose on the primary product exports of less-developed countries. Romulo A. Ferrero, using data supplied by a 1961 Congressional Committee study of trade restraints in industrialized nations, has calculated the average ad valorem tariffs on selected agricultural products and industrial goods for the following countries: Japan, 54 per cent and 19 per cent respectively;[32] Austria, 42 per cent and 19 per cent respectively; Italy, 29 per cent and 16 per cent respectively; Germany, 23 per cent and 9 per cent respectively; France, 22 per cent and 15 per cent respectively; the United Kingdom, 10 per cent and 17 per cent respectively; and the United States, 8 per cent and 11 per cent respectively.[33] Changes have, however, taken place in primary product import tariffs in more recent years, but not all of

[32]Restrictionsof agricultural commodities vary greatly depending on the nature of those commodities. Bela Balassa in Trade Prospects for Developing Countries cites the rather low level of protection in the case of tropical and temperate products, and the high levels of protection for competing primary products.

[33]Ferrero, "The International Trade of Latin America," p. 37.

these changes have benefited Latin America and the less-developed countries. The ECLA in evaluating the results of UNCTAD II in New Delhi in 1968 and the progress of GATT negotiations has observed that while, " . . . tariff concessions or reductions were negotiated for some of the products of the developing countries, nothing was done to remove the basic obstacles that prevent these products from gaining access to the developed countries' markets on satisfactory terms."[34] The supposed world movement towards trade liberalization, in the view of the ECLA, has resulted in a substantial reduction of import tariffs and quantitative restrictions for manufactured goods, thus promoting the trade of the industrialized nations. The gains of the less-developed nations, however, have been marginal.[35]

In the case of the EEC, protectionalist tariff policies might even become more restrictive in the future than they have been in the past. At the end of 1967 almost half of the EEC'S agricultural production was subject to the European Agricultural Guidance and Guarantee Fund (EAGGF). Products already subject to the EAGGF include cereals, pork, rice, oilseeds, and beef. The two major functions of the EAGGF are the establishment of a single price for agricultural products exchanged in the community, the adjustment of the prices of

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[34]United Nations, Industrial Development Organization, "Latin America and the Second Session of UNCTAD," Economic Bulletin for Latin America, XXIII, No. 1, 1968, p. 5.

[35]Ibid.

third country imports to the single price of the community, and the subsidization of community producers. The EAGGF has not only further stiffened an already rigid pattern of agricultural protection in EAGGF, but because a high proportion--about 50 per cent--of the EAGGF resources comes from the price adjustment duties on third country imports, the EAGGF has created a situation where the less-developed countries will be directly subsidizing the production of competing agricultural products in the EEC.[36]

Serious as direct tariff restraints are, however, they probably represent only a fraction of the restraints imposed by the developed nations on the primary product exports of the less-developed countries. While these restraints of trade are too numerous to discuss in depth, some of the most significant restraints will be singled out for comment.

As it was noted above, the United States' average ad valorem tariff on agricultural products is very low in comparison to such tariffs in Japan and the ECC countries. In that the United States is Mexico's prime market for agricultural products, one might be led to believe that the aforementioned restraints to trade might apply less to Mexico than to other less-developed countries. In reality, however, Mexican and Latin American exports to the United States

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[36] Ibid., pp. 10-11.

have been increasingly encountering protectionalist restraints in the United States in the form of quantitative restraints.

As a founding member of the Organization of American States (OAS), the United States has been, at least on paper, dedicated to the elimination of restraints to inter-American trade. Towards this end, the United States in 1966 abolished import quotas on lead and zinc ores and concentrates, which had first been imposed in 1958. In that same year, the United States reduced import controls and duties on some oilseeds and various ores, and eliminated the two per cent duty on soluble coffee. Also, the voluntary 30 per cent reduction of the United States in the cotton acreage planted for the 1966-1967 crop year[37] improved the competitive position of Latin American and Mexican exports of cotton.[38]

These favorable developments were, however, offset by increased protectionism in other areas. In 1965 an amendment to the 1948 Sugar Act was passed (to be in force until 1971), reducing the relative share of foreign producers in the domestic market by 20.4 per cent (from 2.84 to 2.26 million tons). In that Latin America's

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[37] Ibid., p. 14.

[38] It should be pointed out that while the United States did reduce its cotton crop considerably in 1966-1967, Mexico at the request of the United States also reduced its cotton output, from 2.5 million bales in 1965-1966 to 2.0 million bales in 1967-1968. The gain to Mexico by the United States' action has, therefore, probably been overstated.

share of the United States' sugar market had already declined from 36.3 per cent in 1948 to 21.0 per cent in 1965, this additional restriction was viewed with apprehension by major Latin American sugar producers such as Mexico.[39] Congressional Act 88-442 in effect since 1967 makes meat imports subject to quotas restricting their volume to the 1959-1963 levels. This act also includes provisions for the extension of quotas to meat products not covered by the act.[40] Argentina's and Uruguay's meat exports to the United States will not, however, be affected by this act in that their meat exports to the United States have already been severely restricted by sanitary controls.[41] Since 1967 the United States Senate has considered a wide variety of bills designed to increase quotas on agricultural products and processed agricultural products. Needless to say, such bills have created a great deal of consternation in Latin America. One action that has been particularly offensive to Mexico has been the tomato import restrictions. At the request of the Florida Committee of Tomato Growers, the United States Department of Agriculture has progressively adopted restrictive measures directed at the importation of Mexican tomatoes into the United States--the major market for Mexican tomatoes. On May 8, 1968 the United States

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[39] U. N., "Latin America and the Second Session of UNCTAD," p. 15.

[40] Ibid.

[41] Ibid.

Department of Agriculture announced that tomatoes less than 6.35 centimeters in diameter could not be imported into the United States. On April 27, 1970 this restriction was extended to tomatoes less than 7.25 centimeters in diameter.[42] The United States' tomato growers pointed out that this action was necessary to maintain the prices of tomatoes in the United States' market. The president of Mexico's National Union of Vegetable Growers, Alfredo Careaga Cedreros, contested this argument by pointing out that current tomato prices are higher than they have ever been before. He contended that these restrictions only benefited a small group of Florida growers. Alfredo Careaga Cedreros also forecasted a 40 per cent decline in the value of Mexico's tomato exports over the next several years as a result of these actions. Furthermore, the 1968 restriction announcement came only twenty days before the Mexican harvest, a factor which contributed greatly to the indignation of the Mexican producers.[43]

This action on the part of the United States has been viewed with considerable alarm in Mexico for several reasons. First, the export of tomatoes has been a key part of Mexico's attempts to diversify its export base. Mexico's exports of tomatoes rose from

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[42] "Foreign Trade," Comercio Exterior de Mexico, XVI, no. 6 (June, 1970), p. 10.

[43] "Foreign Trade," Comercio Exterior de Mexico, XV, No. 7 (July, 1969), p. 14.

307 million pesos in 1963 to 788 million pesos in 1967. While Mexico's total export earnings increased by 18.2 per cent for the period 1963-1967, the value of Mexico's tomato exports increased by 156.7 per cent for the period with the result that tomato exports represented 5.5 per cent of the value of Mexico's exports in 1967. The value of tomato exports in 1968, however, fell to 251 million pesos and in 1969 the value of tomato exports was only 303 million pesos.[44] The United States' restrictions have, therefore, had a rather disastrous effect on this aspect of Mexico's program of export diversification. The United States' tomato restrictions have also touched off a re-evaluation of the whole Mexican export diversification program. The ability of Mexico to maintain the rapid growth of shrimp, melon, and strawberry exports in the face of a growing fear of United States protectionism must be questioned. With respect to the tomato restrictions, the United States Senate Farm Committee Chairman, Allen J. Ellender, declared that the Mexican tomato would have no problem reaching the United States market provided it complies with the specifications established by the federal authorities.[45] The logic of Senator Ellander's observation must certainly add fuel to Mexico's fears.

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[44]"The Performance of Mexico's Exports," Comercio Exterior de Mexico, XVI, No. 6 (June, 1970), p. 6.

[45]Ibid.

While the possibility of increased quantitative import restrictions in the United States has been a growing source of concern to Mexico and Latin America, so has been the prospect of increased import discrimination in the EEC. Latin American concern has so far focused mainly on the EEC's granting of preferences to its associated African states for imports of coffee, cocoa, and bananas.[46] Whereas Latin American exports of these products to the EEC are subject to ad valorem tariff rates of 9.6 per cent, 5.0 per cent, and 20.0 per cent respectively, associated states' exports of these products can enter the EEC duty free.[47] This discrimination has not thus far preceptively prejudiced Latin American exports of these products, a point often made by the EEC to allay the fears of Latin America. The point, however, is that EEC associate state membership is being expanded. In 1966 associate membership was extended to Nigeria, a country that has not been linked traditionally to continental Europe. The EEC has also negotiated conditions of membership with Kenya, Uganda, Tanzania, Algeria, Tunisia, and Morocco in recent years. With the possibility of associate membership encompassing much of Africa (Latin America's major primary product competition among

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[46]U. N., "Latin America and the Second Session of UNCTAD," p. 11.

[47]Ferrero, "The International Trade of Latin America," p. 39.

the less-developed regions), and with the possibility of British membership in the EEC existing, Latin America and Mexico face the prospect of a shrunken market for their primary product exports. The ECLA has observed that, "This policy (the extension of preferences) suggests that, over the short or medium term, this type of special relationship between the community and Africa will probably be progressively extended, to the detriment of the position of the other developing regions in the EEC market."[48]

Almost all of the protective measures that the developed countries have applied to the primary exports of the less-developed countries have been directed towards one end--the promotion of domestic production of primary products. Towards this end the developed countries have met with a great deal of success. While the EEC has historically relied upon large imports of beef, wheat, sugar, and cereals to satisfy domestic demand, the EEC now (1968) has a high degree of self-sufficiency in these products: beef, 85 per cent; wheat, 110 per cent; cereals, 66 per cent; and sugar, 97 per cent. Bela Balassa has observed that foodstuffs imports (wheat, maize, rice, butter, sugar, and meat) fell by 18 per cent in Western Europe between 1938 and 1956 while Western European consumption of these

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[48] U. N., "Latin America and the Second Session of UNCTAD," p. 11.

products increased by 14 per cent.[49] It is quite probable that such agricultural promotion in industrialized countries, either through protection or subsidy, has been the greatest obstacle to the expansion of Latin American exports.

The United States, like the EEC, has also actively pursued agricultural self-sufficiency through price supports, protection, and subsidies. While the United States, for example, has liberalized direct restrictions on cotton imports, the United States' cotton subsidies equal up to 40 per cent of the export price of cotton. It is, therefore, difficult to measure the net effect of such diverse actions on the exports of less-developed countries.[50] In the case of sugar, import quotas, price supports, and subsidies have all been used to promote self-sufficiency in sugar production in the United States. The result has been that while the United States was only 28.5 per cent self-sufficient in sugar production in 1948, the United States was 42.5 per cent self-sufficient in 1965.[51] Mexico, as a large exporter of sugar to the United States, has officially lodged protests with the

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[49]Balassa, Trade Prospects for Developing Countries, p. 6.

[50]Ferrero, "The International Trade of Latin America," p. 38.

[51]U. N., "Latin America and the Second Session of UNCTAD," p. 15.

United States over the subsidization of beet sugar production in the United States which they feel might in time displace sugar exports to the United States' market from Mexico and other developing countries.

Subsidies and other promotional measures are not only used by the industrialized nations to promote agricultural self-sufficiency they are also used to promote agricultural exports. The result of this export promotion has been that Latin America's share of world commodity exports as well as Latin America's share of world exports has declined in recent years. The ability of the United States, for example, to export wheat, cotton, and other commodities with payment to be made over twenty years in the local currency of the importing country (United States Public Law 480, Sect. 1) makes the United States a very attractive exporter of commodities.

The industrialized nations are major commodity exporters. In 1963 the industrialized countries exported approximately 48 per cent of the total world value of commodity exports.[52] In general, the commodity exports of the developed countries have also been growing at a faster rate than the commodity exports of the less-developed countries. From 1955 to 1963 the commodity exports of the industrialized countries increased from 20.8 billion dollars to 31.2 billion

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[52] Pincus, Trade, Aid, and Development, p. 225.

dollars, an increase of 50 per cent. In comparison, the commodity exports of the less-developed countries increased from 20.5 billion dollars in 1955 to 26.5 billion dollars in 1963, an increase of 29 per cent. The poor performance of the less-developed countries' commodity exports relative to the performance of the industrialized countries' commodity exports was exceeded, however by the poor performance of Latin America's commodity exports which increased from 7.2 billion dollars in 1955 to 8.8 billion dollars in 1963, an increase of only 22 per cent.[53] The effects of this growing competition of the industrialized nations is best seen in its effects on Latin American primary product exports to the United States in recent years. Latin American exports to the United States during the period 1955-1968 increased by only 16 per cent while the total United States' imports during that period approximately tripled.[54] As a result of these trends, Latin America's share of the United States' imports has declined considerably (27.8 per cent in 1958 to 12.4 per cent in 1968.[55]

One often cited reason for this decline in Latin America's share of the United States' imports has been that the composition of

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[53] Ibid.

[54] IMF, International Financial Statistics, XXIII, No. 6 (June, 1970), p. 220.

[55] "Progress Under the Alliance," Business Latin America, (July 24, 1969), pp. 236-237.

the United States' imports changed during this period. Because of increased self-sufficiency, changes in tastes, and the very nature of the demand for primary products, primary product imports as a per cent of total imports declined from 63 per cent in 1955 to 37 per cent in 1967. While this changing composition of the United States' imports has been a major factor accounting for Latin America's declining share of the United States' imports, the increased competition of the industrial countries in primary product exports was also a major factor accounting for this decline. Whereas Latin America's share of the United States' foodstuff imports in 1955 was 62 per cent, it was only 39 per cent in 1967. During this same period of time, Western Europe's share of the United States' foodstuff imports increased from 12 per cent to 21 per cent, and the Australia--New Zealand share increased from 0.6 per cent to 7.4 per cent.[56]

Although the effects of the above obstacles to the growth of Mexico's and Latin America's exports have not, and probably cannot, be measured with any precision, there is reason to believe that these obstacles have posed and will continue to pose formidable barriers to the growth of Mexico's and Latin America's export earnings. The reason for such belief is found in the actual performance of Mexico's and Latin America's exports--that performance being poor in both relative and absolute terms.

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[56] Ibid.

As states before, Mexico's share and Latin America's share of world trade have diminished considerably in recent years. That decrease has been, moreover, rather uniform with respect to their major export markets. From 1963 to 1968, the following declines in Latin America's share of major export markets took place: the United States, 20.4 per cent to 12.4 per cent; the EEC, 5.3 per cent to 4.0 per cent; and the EFTA, 4.3 per cent to 3.2 per cent.[57] For Mexico market shares of major export markets in 1963 and in 1968 were: the United States, 3.5 per cent and 2.0 per cent; the EEC, 0.14 per cent and 0.10 per cent; and Japan, 1.1 per cent and 0.6 per cent.[58] In almost every market area, the influence of both Latin America and Mexico has been diminishing.

Those obstacles to the expansion of Mexican and Latin American exports discussed in this section were demand obstacles. There do exist supply obstacles to the expansion of such exports. Such supply obstacles might include the slow productivity growth of Latin American primary products due to a fixity of resources, i. e. x.. the ability of Mexico to increase sugar output depends heavily upon the amount of arable land available for such production. While such

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[57] United Nations, Department of Economic and Social Affairs, Statistical Yearbook, 1968, 1969, pp. 376-377.

[58] IMF, Direction of Trade Annual, 1964-1968, pp. 1-30.

supply limitations have generally been ignored by the structuralists, they have, no doubt, contributed to Latin America's export dilemma.

Despite the inventory of obstacles to the expansion of exports described in the preceeding pages, some economists feel that countries such as Mexico can achieve satisfactory export growths if the proper measures are taken. Before discussing these measures, however, the last of the structuralist arguments will be examined.

The terms of trade

A great deal of discussion in recent years has centered around the question of whether the gains from trade are biased in favor of the advanced industrial countries such that trade yields greater international inequality. A large part of this discussion has focused on the terms of trade movements of less-developed countries. The hypothesis has been advanced, by among others Raul Prebish, that over the long run the commodity terms of trade $\frac{(\text{average price of exports})}{(\text{average price of imports})}$ of less-developed nations have shown a tendency to decline, and they will continue to decline in the future unless the composition of the exports of less-developed countries changes. The significance of this hypothesis, simply stated, is that over the long-run each given unit volume of export of a less-developed country will exchange for less and less volume of imports, thus potentially weakening that country's capacity to import.

The general idea of a long-run tendency for the commodity terms of trade to turn against the less-developed countries is primarily drawn from the United Nations Department of Economic Affairs study, "Postwar Price Relations in Trade Between Underdeveloped and Industrialized Countries," which was released in 1949.[59]

The major finding of this report was that the index of the ratio of prices of primary products to manufactured goods showed a declining trend from 100 for the period 1876-1880 to 62.0 for the period 1931-1935. The index then rose during World War II to 68.7 (1946-1947). According to the structuralists, however the long-run deterioration appeared again in the 1950's.

To Raul Prebish, the declining commodity terms of trade of commodity exporting less-developed countries are caused by disparate forces shaping international demand and supply. The result of this decline is viewed not only as an obstacle to the development of less-developed countries by curtailing foreign exchange earnings and making capital imports relatively more expensive over the long-run. This decline is also viewed as representing a transfer from the less-developed countries to the developed countries of a greater part of the

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[59]Werner Baer, "The Economics of Prebisch and ECLA," in Latin America: Problems in Economic Development, ed. by Charles T. Nisbet (New York: The Free Press, 1969), p. 212.

fruits of their increased productivity.[60]

To Raul Prebish, the inevitable secular deterioration of the commodity terms of trade of the less-developed country can in part be explained by the low income elasticity and price inelasticity of demand for the primary product exports of less- developed countries. As the supply of these primary product exports increases through increased productivity, there is a tendency for the prices of such exports to decrease because of the nature of the demand for such exports. The demand for the manufactured exports of the developed country is, however, highly income and price elastic with the result that export prices tend to remain stable or rise as the supply of these exports increases through productivity increases. Raul Prebish also argues that supply forces serve to reinforce the resultant declining commodity terms of trade of the less-developed country. Productivity increases in the industrialized countries have not resulted in lower prices for their exports. Instead, the fruits of productivity increases in the industrialized countries have largely been retained by the industrialized countries in the form of wage and profit increases which have, in general, exceeded productivity increases. The relatively smaller productivity increases in the primary product producing

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[60]Prebish, "Commercial Policy in the 'Underdeveloped Countries'," p. 256.

less-developed countries have, however, resulted in lower export prices because of the weakness of unions in the less-developed country, the greater degree of competition in the less-developed country, and the nature of the business cycle.[61] The interaction of these forces results in both a declining terms of trade and a transfer of the larger part of the benefits of technological change from the less-developed countries to the developed countries.[62]

Both the logic of Raul Prebish's hypothesis and the evidence which supposedly supports his hypothesis have been the subject of a great deal of analysis.[63] While the various critiques of the Prebish

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[61]It is argued that during the upswing of the business cycle, with the demand for consumer goods exceeding the supply of consumer goods, profits and prices tend to rise rapidly in the industrialized countries. During the upswing of the business cycle profits are also transferred from the industrialized countries to the primary product producers in the less-developed countries with the result that prices also rise rapidly in the less-developed countries. During the downswing of the cycle, however, prices in the industrialized countries do not fall to their former level because part of the profits of the upswing were transferred into higher wages. Pressure is therefore placed on the less-developed country during the downswing to absorb the brunt of the adjustment with the result that price declines are much greater than price declines in the developed countries. Over a series of cycles, the commodity terms of trade of the less-developed countries tend to fall.

[62]Prebish, "Commercial Policy in the Underdeveloped Countries," pp. 256-260.

[63]The reader can refer to Gerald M. Meier, Leading Issues in Development Economics (New York: Oxford University Press, 1964), pp. 338-413 for a general presentation of the views of Raul Prebish, Gunnar Myrdal, Professor Haberler, A. K. Cairncross,

Thesis are too numerous and complex to be presented here, several comments of a general nature will be offered to the reader.

The validity of the findings of the previously mentioned 1949 U. N. study of export price movements, which has been used as a basis for the terms of trade argument, has been challenged on four grounds. First, the study was based on British export prices (as representative of manufactured exports) which cannot be presumed to be representative of world manufactured product export prices. Second, the base year of 1876 was a year when primary product prices were unusually high. Third, the study ignores changes in the quality of manufactured products which would naturally alter prices. Finally, the study used British export FOB prices as representative of the prices of manufactured goods, and British import CIF prices as representative of the prices of primary products. In view of the fact that freight charges were lowered considerably during the period studied, it is natural that import CIF prices also declined relative to export FOB prices. It has been argued that if these freight charges

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Professor Hicks, and Professor Nurkse with respect to the benefits of trade, with particular reference to the terms of trade argument. An in-depth discussion of the terms of trade argument can be found in Werner Baer, "The Economics of Prebish and ECLA" in Latin America: Problems in Economic Development, ed. by Charles T. Nisbet, (New York: The Free Press, 1969), pp. 203-218, and Gerald M. Meier, The International Economics of Development (New York: Harper and Row, 1968), pp. 41-66.

were taken in to consideration, the ratio of primary product prices to manufactured product prices might not, in fact, show any decline at all. There does, therefore, exist a strong case for doubting the validity of the evidence that was the initial basis for the Prebish Thesis.

Raul Prebish's thesis has, however, been based as much on movements in the terms of trade of Latin America and other less-developed regions since 1950 as it has been based on the U. N. study. Structuralists are fond of pointing out that the commodity terms of trade of the less-developed countries (based on the index 1951 = 100) declined from 113 in 1951 to 84 in 1962.[64] This trend is often used to support their claim of a continuing secular deterioration of the terms of trade of less-developed countries. With respect to this claim, several words of caution are in order in interpreting commodity terms of trade indexes.

First, the use of a composite import or export price index involves several major difficulties. The reliability of such price indexes should first be considered. Gross price indexes, as calculated by the IMF or the U. N., are at best rough estimates of price movements. The commodity terms of trade of Argentina, for example, as calculated by the IMF index are very different from Argentina's commodity terms of trade as calculated by the U. N. s' index for the

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[64] Pincus, Trade, Aid, and Development, p. 233.

period 1960-1965 (Table 34).

TABLE 34

THE RELIABILITY OF TERMS OF TRADE INDICES--ARGENTINA
(1958 = 100)

Commodity terms of trade index	Year						
	1958	1960	1961	1962	1963	1964	1965
United Nations	100	112	113	100	119	126	121
International Monetary Fund	100	111	108	101	101	111	109

Sources: United Nations, Economic Commission for Latin America, Statistical Bulletin for Latin America, V, No. 1, 1969, p. 4; International Monetary Fund, International Financial Statistics, XX, No. 6 (June, 1968), pp. 30-31.

As it can be seen in Table 34 the commodity terms of trade as calculated by the United Nations are not only different than the commodity terms of trade as calculated by the IMF, but they are also moving in opposite directions for the periods 1960-1961 and 1962-1963. The conclusion to be drawn is that relatively small changes in a country's commodity terms of trade cannot be accorded significance. Moreover, the use of such a gross measurement as the commodity terms of trade of Western Europe, the less-developed countries, or Latin America serves to smooth out wide variations in terms of trade movements of the individual countries that comprise

the region, thus limiting the significance of the measure. This is best seen by comparing the commodity terms of trade of Latin America for the period 1958-1966 (Table 35) to the commodity terms of trade of Mexico, Argentina, Brazil, and Chile for the same period (Table 36).

A distinction should also be made between short-term and long-term variations or trends in a country's commodity terms of trade. The use of the early 1950's as a base for constructing Latin America's commodity terms of trade is very misleading, as is ending the index in 1962. The period 1950-1955 was a very favorable period for Latin American export prices because of the Korean War just as the period 1955-1962 was a very unfavorable period for Latin American export prices because of the presence of large stockpiles of commodities in the industrialized nations and the recurrent recessions during this period. The observed decline in the commodity terms of trade of Latin America and the less-developed countries during the period 1950-1962 could therefore be more logically interpreted as a short-run phenomena than as a long-run trend. In any event, no valid conclusion about the secular movement of the terms of trade can be reached in a period as short as twelve years.

Finally, the reader should be cautioned that a declining commodity terms of trade does not necessarily represent either a lessened capacity to import or a welfare loss. It is certainly possible for a

TABLE 35

REGIONAL COMMODITY TERMS OF TRADE (TOT) AND INCOME TERMS OF TRADE (TOT)
(Base 1963 = 100)

Item	1948	1955	1956	1958	1959	1960	1961	1962	1963	1964	1965	1966
World												
Commodity TOT	94	97	96	97	98	100	99	100	100	100	100	100
Income TOT	37	61	66	69	74	84	87	93	100	110	118	127
North America												
Commodity TOT	101	92	94	97	99	99	100	100	100	99	101	101
Income TOT	54	66	78	76	76	86	89	92	100	113	116	128
Western Europe												
Commodity TOT	92	90	91	95	95	97	98	100	100	100	101	100
Income TOT	25	52	56	64	71	81	86	93	100	109	121	129
Latin America												
Commodity TOT	100	110	108	100	97	97	96	92	100	104	101	102
Income TOT	65	80	85	81	85	86	90	91	100	106	107	113
Value of Imports	71	87	92	99	91	96	99	101	100	110	112	122

Notes:

Commodity TOT are calculated by dividing the prices of exports by the price of imports. Income TOT equals commodity TOT times volume of exports.

Source: United Nations, Department of Economic and Social Affairs, Yearbook of International Trade Statistics, 1966 (ST/STAT/SER.G/17), 1968, pp. 32-33.

TABLE 36

THE COMMODITY TERMS OF TRADE AND INCOME TERMS OF TRADE FOR MEXICO AND SELECTED LATIN AMERICAN COUNTRIES
(1958 = 100)

Items	1958	1959	1960	1961	1962	1963	1964	1965	1966
Mexico									
Commodity TOT	100	98	92	97	92	104	103	98	101
Income TOT	100	106	98	109	119	131	132	142	147
Value of Imports	100	89	105	102	102	110	132	138	142
Argentina									
Commodity TOT	100	105	112	113	100	119	126	121	110
Income TOT	100	107	114	104	128	152	158	164	167
Value of Imports	100	80	101	119	110	80	87	97	91
Brazil									
Commodity TOT	100	85	85	84	77	78	85	81	75
Income TOT	100	109	106	116	99	116	112	122	127
Value of Imports	100	102	108	108	109	110	93	81	105
Chile									
Commodity TOT	100	107	123	125	118	118	119	140	160
Income TOT	100	123	132	148	142	144	158	182	222
Value of Imports	100	100	121	142	123	134	147	146	170

Sources: Calculated from: International Monetary Fund, International Financial Statistics, XXI, No. 6 (June, 1968); United Nations, Department of Economic and Social Affairs, Yearbook of International Trade Statistics, 1966 (ST/STAT/SER.G/17), 1968; United Nations, Economic Commission for Latin America, Statistical Bulletin for Latin America, V, No. 1, 1969.

country to have a declining commodity terms of trade concurrent with an improved capacity to import and a welfare gain. Assuming consumer preferences to be constant, welfare gains or losses from trade are better measured by the single-factored terms of trade ($S = \frac{P_x}{P_m} \cdot Z_x$) where $\frac{P_x}{P_m}$ = commodity terms of trade and Z_x = an export productivity index). A rise in S is a favorable movement in the sense that a greater quantity of imports can be obtained per unit of factor-input in the production of exports.[65] It is noted that if Z_x is rising faster than $\frac{P_x}{P_m}$ is falling, a country's welfare is improving. A country's capacity to import based on exports is measured by a country's income terms of trade ($I = \frac{P_x}{P_m} Q_x$, where Q_x = an index of export volumes). Again, if Q_x is rising faster than $\frac{P_x}{P_m}$ is falling, a country's capacity to import based on exports is improving.[66] It is important, therefore, for a writer to specify what terms of trade measurement he is using when discussing the supposed effects of such terms of trade movement.

With the above words of caution in mind, a few observations on Latin America's and Mexico's commodity terms of trade can be offered. Referring to Table 35 it can be seen that from 1955 to 1962,

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[65] The Meier, The International Economics of Development, pp. 44-45.

[66] Ibid., pp. 43-44.

the commodity terms of trade of Latin America declined by 16.3 per cent, while during the same period of time the commodity terms of trade of Western Europe and North America increased by 11.0 per cent and 8.6 per cent respectively. While Latin America was able to increase its income terms of trade by 14 per cent during this period, this was a rather small increment in comparison to a 39 per cent increase in North America's income terms of trade and a 78 per cent increase in Western Europe's income terms of trade during this period. These trends were viewed by the structuralists as evidence of the long-run deterioration of Latin American trade.

While Mexican export and import price indexes were not regularly compiled during the 1950's, there is strong evidence to suggest that Mexico's commodity and income terms of trade both declined during this period of time. According to calculations made by William Freithaler, Mexico's commodity terms of trade declined by 24 per cent between 1950 and 1958.[67] As it can be seen from Table 34, this decline continued until 1962. Raymond Vernon has further estimated that Mexico's income terms of trade declined by 13.3 per cent during the period 1955-1960.[68] By adjusting Raymond Vernon's data to

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[67]Freithaler, Mexico's Foreign Trade and Economic Development, p. 80.

[68]Raymond Vernon, Public Policy and Private Enterprise in Mexico (Cambridge: Harvard University Press, 1964), p. 262.

reflect the period 1955-1962 (for comparison with Latin America) it is found that Mexico's income terms of trade did increase by 7.1 per cent. This increase was, however, still less than that recorded by Latin America for this period (14.0 per cent). It would, therefore, appear that in Latin America in general and Mexico in particular, the Prebish Thesis was born out during the 1950's and up to 1962.

The commodity terms of trade of Latin America and Mexico appear, however, to have stabilized since 1963, as have the commodity terms of trade of North America and Western Europe as seen in Table 35 and Table 36. The stability of Latin America's terms of trade has, moreover, continued in more recent years with the commodity terms of trade in 1967 = 103, 1968 = 103, and 1969 = 102.[69] Some Latin American countries such as Argentina and Chile have, moreover, improved their commodity terms of trade considerably since 1958 (Table 36). Brazil is the only major Latin American country that has continued to incur a declining commodity terms of trade during the 1960's. It might be concluded, therefore, that Raul Prebish's thesis has not been born out by either the Latin America or Mexican experience since 1963.

While the performance of Latin American and Mexican commodity terms of trade has improved in recent years, their income

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[69] IMF, International Financial Statistics, XXIII, No. 6 (June, 1970), pp. 30-32.

terms of trade have not shown significant improvement. Latin America's income terms of trade increased by only 13 per cent during the period 1963-1966, as compared to increases in the income terms of trade of North America and Western Europe of 28 per cent and 29 per cent respectively (Table 35). Mexico's income terms of trade increased by only 12 per cent during the period 1963-1966, a considerable slowdown considering the 37 per cent increase in Mexico's income terms of trade for the period 1960-1963 (Table 36). This slowdown in the growth of Mexico's income terms of trade has come at a very unfortunate time for Mexico in that the growth rate of Mexico's imports is accelerating. Whereas the value of Mexico's imports grew by only 5 per cent for the period 1960-1963, the growth of Mexico's imports for the period 1963-1966 was 29 per cent (Table 36). As in the case of Latin America as a whole, Mexico's imports are therefore growing at a faster rate than Mexico's capacity to import from exports.

Conclusions

The structuralists have advanced the hypothesis that the poor performance of the exports of less-developed countries such as those of Latin America is largely due to the fact that those exports predominantly consist of primary products. According to the structuralists, there exist certain obstacles to the expansion of primary product exports and the stability of the earnings of these exports. These

obstacles have been the subject of discussion in this section.

With respect to these obstacles, it was found that in the case of Mexico and Latin America as a whole, the declining commodity terms of trade argument has not provided an adequate explanation for the poor performance of exports in recent years (Brazil being the exception). While there has not been an observable long-run tendency for Mexico's or Latin America's commodity terms of trade to decline, there has been a considerable degree of short-run fluctuation in their export prices and earnings. It was found that while Mexico's export price fluctuations were greater than those experienced by the industrialized nations, they were generally less than those experienced by other major Latin American countries, a factor which is often attributed to Mexico's relatively high degree of export diversification by Latin American standards.

Mexico's program of export diversification has not, however, contributed significantly to Mexico's ability to expand its volume of exports and its capacity to import from exports. It has been suggested that the relatively slow rate of primary product export expansion evident in Mexico and Latin America has been largely due to the low income elasticity of demand for such products in the industrialized countries (the principle markets for such goods), and the protectionalist policies of the industrialized countries. Because of the limitations that such demand obstacles impose on the exports of less-

developed countries, economists such as Raul Prebisch have suggested that the less-developed countries should change the composition of their exports from primary products to manufactured goods that would not be subject to the aforementioned obstacles to expansion. While the export of manufactured goods would probably involve a high initial degree of subsidization costs, the benefits to be derived from such manufactured exports in terms of generating a more viable export sector and a more rational domestic industrialization effort would, it is argued, more than compensate for these costs.

Some economists have argued, however, that countries such as Mexico can achieve adequate export growth rate with the present composition of exports. William Freithaler has argued that Mexico has been able to adequately expand several primary product exports because of productivity increases and cost reductions achieved in the production of these goods. An example of this is found in Mexico's coffee exports. For the period 1963-1968, Mexico's exports of coffee increased by 57.0 per cent as compared to a decrease of 0.3 per cent in the value of Brazil's coffee exports and a 29 per cent increase in the total value of Mexico's exports for that period.[70] It has, therefore, been argued that despite a low income elasticity of demand for primary products Mexico, as a low cost producer, can rapidly expand

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[70] Ibid., pp. 78, 79, 220.

her exports of many major and minor primary products.

The structuralists, however, are not urging the complete transformation of the export sector of a country such as Mexico. They are only urging that countries such as Mexico increase their exports of manufactured goods, not only to rejuvenate the growth of their exports but also to bring about a more rational policy of national industrialization. It would appear from our previous observations on "inward" industrialization and the performance of Mexico's and Latin America's export sectors that such a policy of promoting manufactured exports should be a most desirable policy in Mexico and in Latin America as a whole. Romulo A. Ferrero has summarized the structuralist sentiment in his observation that,

> A study of the problems of Latin American foreign trade, as they bear on the development process, indicates that while it is essential to do everything possible to increase commodity exports, it is also vitally important to increase the export of manufactures and semi-manufactures, now in its early stages. The latter would serve to reduce the fluctuations in export earnings that result from the sharp variation in international commodity prices. Diversification of exports would provide greater purchasing power and greater stability.[71]

"Outward" Industrialization: The Promotion of Manufactured Exports in Mexico

The supposed benefits that a country such as Mexico can accrue from the persuance of an outward policy of industrialization were

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[71]Ferrero, "The International Trade of Latin America," p. 67.

adequately discussed in the first chapter. In summary, it was found that the major advantages that "outward" industrialization offers over "inward" industrialization are: (1) the fostering of industry under conditions of international competition rather than within a narrow, protected market tends to reduce the high costs and inefficiency associated with industrialization in less-developed countries; (2) the larger market available to industries through "outward" industrialization allows such industries to achieve economies of scale and external economies they could not acquire through exclusive reliance on a narrow, unbalanced domestic market; (3) "outward" industrialization, according to D. B. Keesing, provides a country with a "window to the West" through which technology, better production techniques, and other learning effects might enter; and (4) "outward" industrialization is not subject to those restraints to domestic industrialization (maldistribution of income, regional dualism, and the diminishing of the IS coefficient) which have served to diminish the stimulus of industrialization to development in many Latin American countries. Perhaps the most convincing reason for a less-developed country to promote a policy of "outward" industrialization is that "inward" industrialization in much of Latin America is no longer adequate in terms of absorbing a growing urban population and stimulating development growth.

Also, we have found that "inward" industrialization creates rather irreducible capital import needs which are increasingly not being satisfied by the expansion of traditional exports. The Latin American countries have tried to reduce pressures on their external sectors by reducing import needs through the use of "inward" IS industrialization rather than through improving the earnings performance of exports by changing the composition of those exports. The use of IS to reduce imports, however, creates additional needs for more sophisticated imports through the staged sequential IS process. In the face of growing current account deficits, alternative means of acquiring foreign exchange have in many cases, proved ineffective in maintaining adequate capacities to import for countries such as Mexico.

The pursuance of an "outward" policy of industrialization, however, works to transform the traditional export sector, to increase the stability of export earnings, and to increase the rate of growth of a country's capacity to import. To the countries of Latin America, the validity of this hypothesis has an a priori historical proof, i. e., the successes of those countries whose exports primarily consist of manufactured goods and the failures of those countries whose exports primarily consist of primary products, as interpreted by the structuralists.

The above observations have been of a general nature. The degree to which an "outward" policy of industrialization should be

pursued in any one country obviously depends upon forces peculiar to that country. It is quite probable that Mexico's need to actively pursue a policy of "outward" industrialization is less than the need of Latin American as a whole to pursue such a policy. Mexico's "inward" industrialization, unlike the "inward" industrialization of Latin America as a whole, has provided an adequate stimulus to development in terms of industrial growth rates and labor absorption. Nevertheless, "inward" industrialization in Mexico has been marked by the high costs and inefficiency of production associated with "inward" industrialization in other Latin American countries, and it is also apparent that Mexico also faces those restraints to "inward" industrialization (maldistribution of income, regional dualism, and a low import coefficient) that have signaled the end of "inward" industrialization in countries such as Argentina or Chile. Moreover, the need to accelerate the growth of export earnings in Mexico is just as great as the need in Latin America as a whole. For these reasons, the active promotion of manufactured exports in Mexico has become more pronounced in recent years.

Some of the more important aspects of "outward" industrialization in Mexico and Latin America will be the subjects of discussion in the remainder of this chapter. The first aspect of "outward" industrialization to be discussed will be the contribution of manufactured exports to the industrial development and export performance

of Mexico and Latin America as a whole. Second, consideration will be given to the types of manufactured products that are being exported from Mexico and Latin America. As it will be pointed out, the composition of manufactured exports can be an important determinant of the performance of manufactured exports. Third, the two mechanisms of "outward" industrialization, world trade in general and participation in LAFTA, will be examined with respect to the advantages and disadvantages that each mechanism offers to the development planner. Finally, the reader should remember that "outward" industrialization carries a high risk, a point often ignored by the structuralists. "Outward" industrialization, if improperly used, can be potentially harmful to domestic industries that have been cultivated under protectionism. "outward" industrialization will also require a high initial cost in terms of the subsidization of high cost domestic manufacturers. The United Nations Industrial Development Organization has, however, put these risks into proper perspective in their observation that, "The high degree of specialization implied in a pronounced export orientation of industrial development undoubtedly carries a considerable risk, for the economy as a whole and even more for individual producers. The real alternative, however, is not a similar degree of industrial development with less risk but a slower rate of

industrialization."[72] Given Latin America's preference for industrialization, the latter alternative will be unacceptable.

The performance of the manufactured exports of Mexico and Latin America

Latin America has not, until recent years, actively pursued a policy of promoting manufactured exports, a factor which partially explains the poor performance of Latin American exports. Despite the absence of a policy of active manufactured export promotion, the growth of Latin America's manufactured exports has been significantly greater than the growth of Latin America's traditional exports since 1955. In comparison to the growth of manufactured exports from other less-developed regions and the world, however, Latin America's expansion of manufactured exports has shown much room for improvement. Latin America's exports of manufactured products increased by 43 per cent for the period 1955-1963, as compared to a 22 per cent increase in the value of Latin America's commodity exports for this period. During the same period of time, however, the manufactured exports of all less-developed countries increased by 60 per cent and the manufactured exports of the world increased by 90 per cent.[73]

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[72] U. N., "The Need for an Export Oriented Pattern of Industrialization," p. 29.

[73] Pincus, Trade, Aid, and Development, pp. 180, 243.

Although the growth of manufactured exports was nearly twice as great as the growth of commodity exports in Latin America for the period 1955-1963, the total growth of Latin American exports (25 per cent) was only slightly greater than the growth of commodity exports for the period (22 per cent). The minimal influence of the growth of manufactured exports on Latin America's total export performance for this period can be explained by the fact that while 55 per cent of world trade consisted of trade in manufactured goods in 1963, only ten per cent of Latin America's total exports were classified as manufactured goods in 1963.[74]

As of 1963, it could have been concluded that Latin America was not as competitive as other less-developed countries in promoting manufactured exports. While Latin America accounted for 40 per cent of the industrial production of the less-developed nations, its exports of manufactured goods represented only 20 per cent of the less-developed nation's total exports of these goods. While manufactured exports as a percentage of total exports in 1962 amounted to only 10 per cent in Latin America, they were 23 per cent in Central Africa, 35 per cent in the sterling area of Asia, and 17 per cent for all less-developed countries.[75] By 1960, however, Latin America's

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[74] Ibid., p. 64.

[75] Ferrero, "The International Trade of Latin America," pp. 68-69.

preoccupation with "inward" industrialization was over, as was Latin America's reliance on traditional exports to satisfy her growing import needs. By 1960, nearly every Latin American country had formulated a plan for the active promotion of manufactured exports. That these various plans have been relatively effective is evident by the fact that for the period 1960-1967, Latin America's manufactured exports increased by 106 per cent.[76] The average annual rate of increase of manufactured exports during this period of 10 per cent was more than twice as great as the annual rate of increase of total exports (4.4 per cent) and it was nearly twice as great as the annual rate of increase of total gross industrial product (5.4 per cent) for the period. Although the advances in the promotion of manufactured exports have been most encouraging in recent years, their contribution to industrialization and export performance must still be viewed as marginal. In 1967 Latin America's manufactured exports were only valued at 1.73 billion dollars. This value represented only 15 per cent of total Latin America exports and less than two per cent of the regions industrial product.[77] The importance of manufactured exports is, however, growing.

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[76] "Progress Under the Alliance," Business Latin America, July 24, 1969, p. 236.

[77] Ibid., p. 237.

As in the case of Latin America as a whole, the active promotion of manufactured exports in Mexico has been a relatively recent phenomena, but it has been a phenomena of growing importance to Mexico's industrial development and export performance. Whereas manufactured exports constituted only seven per cent of Mexico's exports in 1950, they were 17 per cent of Mexico's exports in 1964, and 24 per cent of exports in 1969 (Table 37).

Philippe C. Schmitter and Ernst B. Haas have suggested that Mexico's attitudes toward the export of manufactures underwent a major change in 1960, a change which was to result in the formulation of a program of active promotion of manufactured exports.[78] Mexico in 1960 was struggling to solve what Raymond Vernon has referred to as the dilemma of Mexico's development. Mexico's external sector was performing poorly and it was felt by many that "inward" industrialization had reached the limits of its growth, and was now slowing down. It was felt that one way out of this dilemma was through the expansion of manufactured exports. Domestic manufacturers, however, were hesitant to enter the export sector. They felt that because of their high cost, fostered by years of protectionism, they could not be competitive in world markets. These domestic manufacturers

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[78]Schmitter and Haas, Mexico and Latin American Economic Integration, p. 16.

TABLE 37

MANUFACTURED GOODS IN MEXICO'S WORLD TRADE
(Thousands of Pesos)

	World		Latin America[a]	
	Total Exports	Manufactured exports	Total Exports	Manufactured Exports
1966	14,985,000	2,457,540	1,282,560	611,558
1967	14,314,000	2,333,319	1,127,864	669,539
1968	15,674,000	3,118,100	1,368,100	709,601
1969	18,135,000	4,271,797	1,509,887[b]	1,060,515[b]
Percentage change over the period	21.0	73.0	17.7	73.0
Manufactured exports as a percentage of total exports in 1969	. .	23.5	. .	70.0

Notes:

[a]Mexico's exports of manufactures to Latin America for 1968 and 1969 consist of exports to LAFTA and exports to the CACM and Panama which were 81 per cent of Mexico's non-LAFTA, Latin American exports in 1968. Total exports for 1968 and 1969 were based on the whole region.

[b]Estimated from the first nine months of 1969.

[c]LAFTA trade for 1966 and 1967 does not include Venezuela and Bolivia.

Because of the limitations of the above data as expressed by the above notes, and because of the constant revising of data by the Mexican government, this table should be used with caution. The

TABLE 37--Continued

LAFTA[c]		Rest of Latin America[a]	
Total exports	Manufactured Exports	Total Exports	Manufactured Exports
708,287	421,430	574,273	190,128
595,613	440,138	532,251	229,401
778,000	470,653	590,227	238,948
1,076,887	753,814	433,000[b]	306,701[b]
52.0	78.0	- 24.0	61.0
. . .	69.9	. .	70.0

above foreign trade statistics, like all Latin American statistics, may contain a high degree of error.

Sources: Calculated from: Asociacion Latinoamericana de Libre Comercio, Comite Ejecutivo Permanente, El Comercio Exterior de la ALALC (CEP/Repartido 1161), Montevideo, June 17, 1969; "The External Sector of Mexico's Economy in 1967," Comercio Exterior de Mexico, XIV, No. 4 (April, 1968), pp. 2-4; "The External Sector of Mexico's Economy in 1969," Comercio Exterior de Mexico, XVI, No. 4 (April, 1970), pp. 2-3; "Mexico's Latin American Trade," Review of the Economic Situation of Mexico, XXV, No. 531 (February, 1970), p. 32; Mexico, Secretaria de Industria y Comercio, Anuario Estadistico del Comercio Exterior de los Estados Unidos Mexicanos, 1968 (Mexico, D.F.: Talleres Gráficos de la Nación, 1969); Mexico, Secretaria de Industria y Comercio, Direcion General de Integracion Economica Latinoamericano, Integracion Latinoamericana, No. 18, (February, 1970).

felt that they could only enter into the external sector if the government would in some way guarantee their operations against risk. The government responded by formulating two general plans for promoting manufactured exports.

The first of these plans involved Mexico's participation in LAFTA. The second of these plans involved the establishment of a general system of subsidies, tax exemptions, and credit extensions to stimulate the export of manufactured goods to world markets in general. Firms that manufactured goods for export could receive exemptions from export taxes, permanent subsidies, reductions on taxes for imported raw materials and capital, tax exemptions, and up to fifty per cent rebates on rail freight to points of export. In addition, the Fund for the Promotion of Manufactured Exports (FOMEX) was established in 1963. FOMEX, which is sponsored by the Banco de Mexico, S. A., offers financial backing for credit sales of manufactured exports and export-oriented production. FOMEX, through its credit guarantees to exporters, has enabled Mexican exporters of manufactured goods to approach international markets under stronger competive conditions than those prevailing before FOMEX was established. The acceptance of FOMEX by Mexican manufacturers has been encouraging, as indicated by the fact that while only six per cent of Mexico's manufactured exports were financed by FOMEX in 1965,

22 per cent of such exports were financed by FOMEX in 1968.[79]

This active Mexican promotion of manufactured exports has paid high dividends in recent years. Mexico's manufactured exports increased by 90.9 per cent for the period 1964-1969, from 2.24 billion pesos in 1964 to 4.27 billion pesos in 1969.[80] This increase in the value of manufactured exports partially offset the poor performance of commodity exports which increased by only 26.9 per cent for this period. The increase in the value of total exports for the period, was 37.7 per cent.[81]

Since 1966, the disparity between the growth rates of manufactured and non-manufactured Mexican exports has been even more evident (Table 37). For the period 1966-1969 the total growth of non-manufactured exports was only 11 per cent as compared to a 73 per cent increase in the value of manufactured exports. The importance of Mexico's manufactured exports can be seen by the fact that their growth accounted for 57.6 per cent of the growth of total exports for the period 1966-1969 (total exports increased by 3,150 million pesos while manufactured exports increased by 1,814 million pesos).

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[79] "Resume of the FOMEX Operational Report," Comercio Exterior de Mexico, XVI, No. 4 (April, 1970), pp. 15-17.

[80] United Nations, Department of Economic and Social Affairs, Yearbook of International Trade Statistics, 1966 (ST/STAT/SER.G/17), 1968, pp. 541-547; Table 35.

[81] Ibid.

The contribution of manufactured exports to the performance of Mexico's export sector has been far from marginal in recent years. Manufactured exports represent a rapidly growing share of Mexico's total exports, and manufactured exports have been by far the most dynamic elements of Mexico's export sector during the past decade. The contribution of manufactured exports to Mexico's industrial development, however, must still be considered marginal. In 1968 only 2.7 per cent of Mexico's GIP was exported. While this export share is small, it has been growing. In 1964 only 1.7 per cent of Mexico's GIP was exported. Moreover, the growth of manufactured exports during the past two years (33.6 per cent in 1968 and 37.0 per cent in 1969) was over three times greater than the growth of GIP during those years.

The composition of manufactured exports

As it was pointed out in the first chapter, the composition of a less-developed country's manufactured exports can be an important determinant of the performance of those exports in terms of stimulating industrial development and in terms of promoting export expansion. A country's choice of what manufactured exports to promote can, therefore, have an important effect on the short-term and long-term development prospects of that country.

Two arguments concerning the composition of the manufactured exports of less-developed countries have emerged in recent years. One argument, as put forth by Hal B. Lary, suggest that less-developed countries should primarily promote those manufactured exports for which they possess a comparative advantage in world trade--labor-intensive goods.[82] Hal B. Lary reasons that the rate at which manufactured exports can expand depends on their competitive position, the growth of world demand for such exports, and the tariff policies of the developed countries. On the basis of all of these limitations, Hal B. Lary concludes that exports of such goods as textiles, clothing, footwear, glasswear, prepared foods, optical goods, and small appliances have the greatest growth potential from the less-developed countries.[83] Hal B. Lary also concludes that the promotion of such exports will yield substantial benefits to the industrial development of the less-developed country. One of the most serious problems facing industrialization in less-developed countries has been the inability of industries to adequately absorb labor. Through the active promotion of labor-intensive manufactured exports, this problem can be alleviated.

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[82] Lary, Imports of Manufactures from Less-Developed Countries, p. 14.

[83] Ibid., p. 89.

The LAIESP contends, however, that while the expansion of labor-intensive manufactured goods is desirable, the main impetus of export promotion should be directed at durable consumer and capital goods.[84] Their argument is based on the supposed advantages that such exports would have over labor-intensive exports in stimulating industrial development and export expansion.

With respect to the stimulus of manufactured exports to industrial development, the LAIESP has observed that in textile and food production economies of scale are insignificant. In the promotion of durable consumer and capital goods, however, economies of scale are very significant. Moreover, the initial scale requirements for producing capital and durable consumer goods are much higher than those required for producing non-durable consumer goods. The impact of an expanded market on domestic production would, therefore, be greatest in the case of durable consumer and capital goods exports. It is pointed out that while the expansion of labor-intensive manufactured exports will serve to rationalize the domestic production of such goods, it will also serve to increase the share of such products in domestic production, a share which is at present excessively high.

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[84] United Nations, Industrial Development Organization, The Latin American Institute for Economic and Social Planning, "Industrial Development Strategy in Latin America," Industrialization and Productivity, No. 13, 1969, p. 37.

The LAIESP argues that, ". . . over the long term, light industries tend to have a less dynamic effect on the rest of the economy, as a result, inter alia, of the fact that their technical content is smaller and the chain of technological interrelationships shorter."[85] A balanced industrial development requires the promotion of capital and durable consumer goods industries. Such a promotion can not realistically take place exclusively within the confines of the small and poorly organized domestic markets of the less-developed countries. While less-developed countries have viewed their manufactured exports as spillovers from domestic production, the opposite must to some degree hold true in the case of the development of capital and durable consumer goods industries.

With respect to the contribution of labor-intensive industries to the absorption of a rapidly growing urban labor force, the LAIESP correctly observes that labor absorption does not depend solely on the size of an industry's labor-out-put ratio, it also depends upon the growth of that industry's output and the multiplier effects of that industry on output and employment in other industries.

The LAIESP contends that exports of capital and durable consumer goods have a greater growth potential than do the labor-intensive manufactured exports of less-developed countries. The LAIESP has

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[85] Ibid., p. 43.

observed that, "The products of the metal-working and metal transforming industries account for over 60 per cent, and these plus chemical products for more than 70 per cent of world exports of manufactured goods . It is in respect to these items too, that the volume of industrial exports shows the greatest increase."[86]

The LAIESP has pointed out that at least one reason for the poor performance of Latin America's manufactured exports relative to the performance of world exports of manufactured goods during the period 1953-1963 can be found in the composition of those exports. In 1964 only 4.8 per cent of the manufactured exports of Latin America consisted of machinery and transport equipment (SITC section seven). The largest part of manufactured exports (81.0 per cent) consisted of manufacturers classified by materials (textile, etc., SITC section six) and miscellaneous manufacturers (footwear, clothing, etc., SITC section eight). World exports of manufactures, however, contained a very large share (41.8 per cent) of machinery and transport equipment exports. The importance of these contrasting compositions of manufactured exports to the growth rates of Latin American and world exports of manufactures can be seen by the fact that world exports of machinery and transport equipment grew at an average annual rate of 10.5 per cent for the period 1953-1963 while world

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[86] Ibid., p. 41.

exports of manufactures classified by materials and miscellaneous manufactures grew at an average annual rate of only 6.9 per cent for this period.[87]

It is reasonable that world exports of consumer durable and capital goods should be growing at a faster rate than exports of labor-intensive consumer non-durable goods. First, the income elasticity of world demand is greater for consumer durable and capital goods than it is for labor-intensive consumer non-durable goods. The U. N.'s calculation of the elasticities of world output (which corresponds roughly to the income elasticity of demand) for various consumer non-durable and producer goods tends to verify this hypothesis. The income elasticities of output for various goods classified as either non-durable consumer or producer goods were found to be as follows: leather products, 0.89; food, beverages, and tobacco, 0.98; textiles, 1.21; clothing and footwear, 1.36; chemicals and petroleum products, 1.55; metal products, 1.98; and basic metal transformation products, 1.99.[88]

The protectionist policies of the developed countries are other factors which have contributed to the relative faster growth of

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[87] Ibid., p. 49.

[88] United Nations, Conference on Trade and Development, Trade in Manufactures and Semi-Manufactures: Proceedings of the United Nations Conference on Trade and Development (E/Conf. 46/114/Vol. IV), 1964, p. 45.

consumer durable and capital good exports. A comparison of the tariffs on different classes of manufacturers shows that exporters of labor-intensive consumer goods encounter higher tariff barriers than do exports of consumer durable and capital goods. Bela Balassa has observed that tariffs and quantitative restrictions tend to rise according to the degree of fabrication of consumer non-durable goods and basic metals (manufactures classified by material) until they reach very high levels in the cases of finished non-durable consumer goods. But, according to Bela Balassa,

> The graduation of tariffs from raw materials to semiprocessed and processed goods does not continue as we move to more sophisticated products, however. While tariff rates rise from iron ore to pig iron and to steel ingots and finished articles of steel, duties again become lower on much of machinery and transport equipment. [89]

In 1963 the United States imposed the following average ad valorem tariffs on imports of the following classes of manufactures: miscellaneous manufactures, 24 per cent; manufactured goods classified by material, 21 per cent; chemicals, 17 per cent; and machinery and transport equipment, 12 per cent. The average ad valorem tariffs on these goods for the United States, the United Kingdom, Japan, Italy, Canada, France, Benelux, and West Germany as a whole in 1963 were: miscellaneous manufactures, 20 per cent; manufactured

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[89] Balassa, Trade Prospects for Developing Countries, p. 116.

goods classified by material, 16 per cent; chemicals, 11 per cent; and machinery and transport equipment, 13 per cent.[90] The LAIESP contention that the protectionist policies of the developed countries tend to concentrate on those manufactured goods exported by the less-developed countries is certainly given weight by the above findings.

Unfortunately for the less-developed countries, the disparity between protectionist restrictions on labor-intensive manufactured good exports and protectionist restrictions on durable consumer and capital goods exports is growing. Bela Balassa has observed that,

> Lower tariffs on highly sophisticated products as compared to the relatively simple manufactures exported by developing countries can be explained by reference to the process of negotiations on tariff reductions among industrial countries in the framework of GATT which takes the form of trading concessions for concessions.[91]

In that the largest part of the trade of the developed countries consists of sophisticated manufactured goods, it is logical that the force of trade liberalization has been directed primarily at these products. This tendency was observed by the ECLA during the Second Session of UNCTAD in 1968. The ECLA stated that,

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[90] U. N., Trade in Manufactures and Semi-Manufactures, p. 10.

[91] Balassa, Trade Prospects for Developing Countries, p. 116.

> In the case of manufactures . . . the negotiations were conducted mainly among the "major negotiators"--i. e., among the developed countries themselves--, so that the liberalization measures benefited chiefly those manufactures and semi-manufactures which constitute a substantial proportion of trade among the countries in question, while many products of particular interest to the developing countries were left on one side. The tariff reductions negotiated related mainly to lines of production characterized by advanced technology or high degrees of capital intensity, i. e., products that the great majority of the developing countries are not in a position to export. . . . In the last analysis, all this is liable to accelerate the expansion of the developed countries' reciprocal trade, without giving the developing countries any real share in the increase achieved. . . .[92]

As it was stated previously, the composition of manufactured exports can be an important determinant of the performance of those exports in terms of stimulating industrial development and in terms of promoting export expansion. It would appear, from the above discussion, that manufactured exports of consumer durable and capital goods will potentially contribute more to a countries industrial development than will exports of labor-intensive non-durable consumer goods. The less-developed country's choice of what manufactured exports to promote must, however, also be based on the rate at which such exports can be expected to expand.

Hal B. Lary has stated that the rate at which manufactured exports can expand depends on their competitive position, the growth

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[92]U. N., "Latin America and the Second Session of UNCTAD," p. 36.

of world demand for such exports, and the tariff policies of the developed countries. Given these criteria, Hal B. Lary contends that less-developed countries should direct their efforts to the promotion of labor-intensive manufactured exports. The LAIESP, however, contends that while the expansion of labor-intensive manufactured exports is certainly desirable, the main impetus of export promotion should be directed towards expanding durable consumer and capital goods exports. While these two views may appear to be in conflict, they are essentially complementary. Hal B. Lary's position is primarily based on the short-run ability of the less-developed country to expand manufactured exports, while the position of the LAIESP is primarily based on the long-run potential of the less-developed country to expand manufactured exports. While the growth of world demand and the tariff policies of the developed countries favor the expansion of durable consumer and capital goods exports in the long run, most of the less-developed countries do not possess the short-run ability necessary to competitively export these products to world markets. Instead, their comparative advantage is found in the produtions and export of labor-intensive manufactures.

Rather than advocating either one type of promotion or another, the proper policy objective of the less-developed country should be to maximize the short-run gains that it can accrue from the export of those labor-intensive goods for which it possess a comparative

advantage, while at the same time establishing those pre-conditions necessary for the active expansion of durable consumer and capital goods exports. Several of the less-developed countries have gone a long way towards successfully establishing these preconditions. Among the less-developed countries Mexico has, perhaps progressed the furthest towards the establishment of these preconditions.

The composition of Mexico's manufactured exports was essentially the same as the composition of Latin America's manufactured exports in 1964. Only 5.9 per cent of Mexico's manufactured exports consisted of machinery and transportation equipment (SITC section seven) in 1964, while chemical products (SITC section five) accounted for 17.5 per cent of manufactured exports. As in the case of Latin America as a whole, the larger share of Mexico's manufactured exports (76.6 per cent) consisted of manufactures classified by material and miscellaneous manufactured goods.[93] By 1966, however, it was clear that Mexico's manufactured exports were undergoing a transformation. In 1966 the composition of Mexico's manufactured exports was as follows: machinery and transportation equipment, 7.4 per cent; chemicals, 22.0 per cent; and manufactures classified by materials and miscellaneous manufactures, 70.1 per

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[93] U. N., Yearbook of International Trade Statistics, 1966, pp. 541-547.

cent.[94] Based on the first nine months of 1969, the composition of Mexico's manufactured exports was as follows: machinery and transportation equipment, 26.0 per cent; chemicals, 23.7 per cent; and manufactures classified by material and miscellaneous manufactures, 50.3 per cent.[95]

Machinery, tools electrical equipment, and transport equipment have emerged as the most dynamic elements of Mexico's trade in manufactures. Based on the first ten months of 1968 over the first ten months of 1967, these exports increased by 47.8 per cent (from 273 million pesos to 402.7 million pesos). The value of these exports for the first nine months of 1969 (734 million pesos) was 105.0 per cent greater than the value of these exports for the same period in 1968.[96]

In view of the needs for less-developed countries to improve the earnings of their exports and to rationalize their protected industries, it is important to analyze Mexico's success in promoting exports of consumer durable and capital goods.

LAFTA as a tool for promoting exports of manufactures

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[94] Ibid.

[95] "Mexico's Latin American Trade," Review of the Economic Situation of Mexico, XLV, No. 531 (February 1970), p. 32.

[96] Ibid.

While Mexico's success in promoting exports of consumer durable and capital goods has been the result of many factors, it is the hypothesis of this paper that the single factor most responsible for Mexico's success in promoting these exports has been Mexico's participation in LAFTA. LAFTA has emerged as a tool of "outward" industrialization distinct from the promotion of exports of manufactures to the world in general. LAFTA trade is unique from the standpoint of the type of manufactures exported, the rate of expansion of those exports, and the mechanisms by which trade is promoted.

The importance of LAFTA to Mexico's efforts to promote manufactured exports can be seen in Table 38. While the export data in Table 38 refers to Latin America as a whole, the largest part of Mexico's exports went to LAFTA. In Table 38 Mexico's manufactured exports for 1967 have been listed by class of manufacture, with the percentage share of the total value of each class of manufacture being listed for Latin American exports and exports to the rest of the world.[97] It is seen that for those manufactures normally classed as labor

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[97] The NABALAC coding of exports used in Table 38 allows a more comprehensive classing of manufactures than the SITC coding used by the United Nations. SITC codes 1-4 refers to primary commodities, yet many manufactured food, beverage, and tobacco products are contained in these categories. Since the NABALAC coding defines manufactures by stages of production (two stages are required for a good to be classed as a manufactured good), these products are represented as manufactures.

TABLE 38

VALUE OF EXPORTED MANUFACTURED PRODUCTS IN 1967 BY NABALAC SECTION AND BY PERCENTAGES OF TOTAL TRADE FOR LATIN AMERICA AND THE REST OF THE WORLD

NABALAC Section	Items	Total Value $ U. S.	Sub-items Whose Value Exceeds $100.00 (U.S.) Percentage of exports going to Latin America	Percentage of exports going to the Rest of the World	Percentage of Total Value of Sub-items whose Value was less Than $100.000 (U.S.)
I	Live Animals and Their Products	3,060	. .	. .	100.00
II	Vegetable Products	. .	. .	. .	. .
III	Animal and Vegetable Greases and Oils	5,551	. .	. .	100.00
IV	Foods Industry, Drinks, Alcoholic Beverages, Tobacco	17,045,293	4.75	90.01	5.24
V	Mineral Profucts	15,485,624	0.73	98.20	1.07
VI	Chemical Products	57,562,773	37.67	59.55	2.78
VII	Plastics, Resins, Rubber	1,690,397	45.80	37.80	16.40
VIII	Hides and Leather	1,157,495	. .	80.09	19.91
IX	Lumber, Cork, Wood Products	5,761,863	. .	96.27	3.73

TABLE 38--Continued

NABALAC Section	Items	Total Value $ U. S.	Sub-items Whose Value Exceeds $100.00 (U.S.) Percentage of exports going to Latin America	Percentage of exports going to the Rest of the World	Percentage of Total Value of Sub-items whose Value was less Than $100.000 (U.S.)
X	Material Used in Paper Production and Paper Products	13,699,286	74.63	20.17	5.20
XI	Textiles	33,064,561	2.65	92.95	4.40
XII	Shoes, Hats, Artificial Fruits and Flowers	1,908,595	. .	84.33	15.67
XIII	Cement,Glass, Ceramics	9,038,155	12.67	80.27	7.06
XIV	Jewelry	2,091,787	5.81	87.38	6.81
XV	Metals and Metal Products	27,676,374	29.57	65.01	5.42
XVI	Machines and Electrical Materials	18,452,108	42.53	45.57	11.89
XVII	Transportation Materials	4,077,649	26.32	62.42	11.26
XVIII	Optical, Photographic, Electronic, and Musical Equipment	2,195,552	22.66	38.51	38.83
XIX	Arms and Munitions	440,736	. .	88.06	11.94
XX	Other Manufactures	3,353,425	. .	85.50	14.50
Total Manufactures		214,710,284	24.85	69.48	5.67

Source: Calculated from: Instituto para la Integracion de America Latina, Mexico: Exportaciones de Manufacturas a America Latina, 1966-1967, Series Estudios No. 1 (Buenos Aires: Instituto para la Integracion de America Latina, 1969).

intensive manufactures (NABALAC codes I-V, VIII, IX, XI, XII, and XIII), Latin American trade is a very small percentage of world trade. Mexico's exports of manufactures to Latin America are most heavily concentrated in capital-intensive manufactures, goods which require large scales of production. For example, NABALAC codes VI, VII, X, XV, XVI, and XVII, which include chemical products, plastics, paper products, metal products, machines, electrical materials, and transportation materials, accounted for 57.4 per cent of the total value of Mexico's exports of manufactures in 1967. Exports of these goods to Latin America totaled 49.8 million dollars in 1967, or 40.4 per cent of the total world exports of these goods in 1967. While only 7.9 per cent of Mexico's world exports went to Latin America in 1967 (Table 37), 24.9 per cent of Mexico's world exports of manufactures went to Latin America and 40.4 per cent of those manufactured exports normally requiring the highest degrees of sophistication in production went to Latin America in 1967. Mexico's total Latin American exports may be a minor share of total world exports, but in the area of trade in manufactures Latin American trade is of vital importance to Mexico.

While Mexico's LAFTA trade in manufactures will continue to grow in importance, Mexico will also continue to actively pursue world trade in manufactures, especially in the areas of consumer durable and capital goods. The experience that Mexican manufacturers

gain from LAFTA trade will certainly promote the latter objective. Baring a breakthrough in the policies of the developed countries with respect to preferential treatments for manufactured exports of less-developed countries, however, the expansion of exports of the more sophisticated manufactures to world markets will be less dynamic than the expansion of such exports to LAFTA.[98]

Final Remarks

In this paper we have shown first, the existence of two industrialization paths or theories--"inward" industrialization and "outward" industrialization. The significance of the latter of the two has been seen in the light of some of the short-comings of the former as well as some of the successes of the former in Mexico and in Latin America as a whole. Secondly, a case study of these instruments as they apply to Mexico and Latin America has been made to illuminate the present states of industrialization and export performance in

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[98]There has been a perceptable change in the attitudes of the developed countries towards the question of general preferences for the manufactured exports of the less developed countries in recent years. The OECD, for example, announced in May, 1970 that a general system of preferences for the manufactured exports of less-developed countries to be extended by all of the members of the OECD would begin in mid-1971. Such promises have, however, been made in the past. The OECD also proposed such a system of preferences at the Second Meeting of UNCTAD in 1968. In that case, the system was discarded during negotiations with the less-developed countries.

Mexico and in Latin America as a whole. The findings of this case study indicate that there exists a growing need for Mexico and Latin America to expand their exports of manufactured goods. To some degree, they have gained success in their efforts to expand such exports.

According to the findings of this case study, one category of manufactures, which occupies the larger share in total manufactured exports from Mexico finds its main export market in developed countries, while the other category of manufactured exports whose importance is clearly increasing, is largely directed to LAFTA and Latin America. The former category of manufactures consist largely of labor-intensive consumer non-durable goods. The latter category of manufactures consist largely of capital-intensive consumer durable and capital goods.

This case study has attempted to illuminate some of the factors influencing Mexico's preference for industrialization through participation in LAFTA. It would appear that the most important factors are Mexico's need to accelerate the growth of export earnings, the need to rational industrial production, and the need to expand the market for Mexico's industrial products. Mexico's participation in LAFTA has as its objectives the fulfilling of such needs.

Mexico's ability to reach these objectives will largely depend upon Mexico's ability to mold LAFTA into an instrument conducive to

the attainment of these objectives. LAFTA is now in a period of redefinition. The type of market which emerges from this period of redefinition will certainly have a great influence on Mexico's ability to attain its objectives in LAFTA, and it will, therefore, influence Mexico's preference for continued participation in LAFTA.

CHAPTER V

LAFTA AS A TOOL OF NATIONAL INDUSTRIALIZATION: THE MEXICAN EXPERIENCE

Mexico, after a history of little economic interaction with its Latin American neighbors, entered the decade of the 1960's possessing a new development tool--a membership in a free trade association of Latin American nations--LAFTA. It has been suggested that Mexico's decision to join LAFTA in 1960 was largely conditioned by Mexico's expectations of using LAFTA as vehicle for expanding manufactured exports.

The founding of LAFTA by the Treaty of Montevideo in 1960, however, offered little promise of a high level of intra-regional trade in manufactured goods. One major instrument of trade liberalization in LAFTA was to be the Common List. The Common List was to be augmented every three years by items constituting twenty-five per cent of the total value of existing regional trade. Items once placed on the Common List were to be permanently free from tariffs and quantitative restriction within the region. It was hoped, therefore,

that by 1973 all of the region's trade would be substantially free from tariffs and quantitative restrictions. Such a program of trade liberalization, however, offered little incentive to regional trade in manufactured goods, much less to trade in capital and consumer durable goods, in that intra-regional trade in 1960 consisted almost wholly of primary products (eighty percent).[1] The Common List, since it was only designed to stimulate trade in those goods already traded in the region, could obviously not be a meaningful tool for the promotion of trade in manufactures.

The other major instrument of trade liberalization created by the Treaty of Montevideo was the National List. Every LAFTA participant was to annually construct a national schedule specifying tariff concessions to be granted to other members of LAFTA. The national schedule was to be constructed in such a way that each member country would commit itself to granting to other LAFTA participants annual tariff reductions equivalent to eight per cent of the weighted average of tariffs applicable to third countries. While the National Lists could include manufactured items currently not traded in the region, and could thus potentially serve to stimulate inter-regional trade in such items, the National List had an important drawback.

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[1] Wionczek, Economic Cooperation in Latin America, Africa, and Asia: A Handbook of Documents, p. 37.

Tariff concessions placed on the National List could be withdrawn by the granting country if such concessions, " . . . have, or are liable to have, serious repercussions on specific activities of vital importance to the national economy."[2] In view of the costs involved in promoting manufactured exports, the National List escape clauses were viewed with apprehension. It is significant to note that the National List negotiations of 1961 produced very few concessions on manufactured goods.[3]

It might therefore be concluded, as it was by Philippe C. Schmitter and Ernst B. Haas,[4] that LAFTA offered little promise for a high level of trade in manufactured goods when Mexico began participating in LAFTA in 1961. In fact, 81.4 per cent of Mexico's exports to LAFTA in 1961 were foodstuffs and primary products.[5] It was widely felt that LAFTA trade would continue to center around traditional exports throughout most of the period of trade liberalization (until 1973). Trade in manufactures was viewed as a long-run goal, given the initial framework of LAFTA. Mexico's participation in

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[2]Ibid., p. 284.

[3]Schmitter and Haas, Mexico and Latin American Economic Integration, p. 25.

[4]Ibid., p. 24.

[5]Francisco Borza, "Mexico: Sistema de Comercio Exterior," Derecho de la Integracion, No. 4 (April, 1970), p. 181.

LAFTA, as viewed by Philippe C. Schmitter and Ernst B. Haas, was, therefore, based on the expectations of changing the structure of LAFTA to make it more responsive to the immediate needs of the relatively more industrial members of LAFTA.[6] Romulo A. Ferrero observed in 1966 that,

> . . . the development of the regional Latin American market is geared to the future, for the most important products to be traded are not those exchanged today but these to be sent to the market tomorrow, especially in the industrial field. This applies not only to industries already established in the countries, which must compete among themselves, but also to new industries--particularly those producing intermediate goods and durable consumer goods, as well as capital goods having greater and greater importance for regional industrial production.[7]

As it was pointed out before, the structure of LAFTA, has in recent years, changed in such a way as to promote a high level of intra-regional trade in manufactured goods. Whereas 81.4 per cent of Mexico's exports to LAFTA in 1961 consisted of foodstuffs and primary products, 69.9 per cent of Mexico's exports to LAFTA in 1969 were manufactured goods. The internal forces which have produced this fundamental change in the structure of LAFTA trade have been well received by Mexico, for they have changed LAFTA into an

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[6]Schmitter and Haas, Mexico and Latin American Economic Integration, p. 30.

[7]Ferrero, "The International Trade of Latin America," p. 81.

instrument that is much more responsive to Mexico's immediate development needs. The internal forces which have transformed LAFTA into an instrument for the promotion of trade in manufactured goods have, however, generated countervailing forces which threaten to sharply reduce the growth of Mexico's exports of manufactures to some members of LAFTA. Those internal forces which have served to promote expanded intra-regional trade in manufactured goods have been generated by the emergence of the sectoral meeting and the complementation agreement as the major instruments of trade liberalization in LAFTA. The countervailing forces referred to above have emanated from the unbalanced nature of the expanding intra-regional trade in manufactured goods and the resultant attempts by some participants to gain a larger share of the trade in manufactured goods through the formation of subregional groupings within the general framework of LAFTA.

It is the purpose of this chapter to further identify the benefits and the costs that Mexico has accrued from its participation in LAFTA, as well as to analyze the changes which have taken place in LAFTA's framework over the past ten years. Then, on the basis of our knowledge of the external forces and the internal forces shaping Mexico's participation in LAFTA, the author will offer several statements on the probable course of Mexico's future participation in LAFTA.

Mexico and Latin American Integration: The Benefits and Costs of Participation

The benefits that Mexico might gain from participating in LAFTA can be grouped into two categories. One category, which might be termed the dynamic benefits of participation, would include those benefits associated with the expansion of regional manufactured exports. Such benefits include: the economies of scale derived from the expansion of industrial output; the rationalization of industry (the lowering of industrial cost) which might occur through the exposing of domestic industries to regional competition; the development of capital and consumer durable industries that could not develop within the constraints of Mexico's domestic market; and the expansion of the market for industrial goods whose domestic market is limited by structural bottlenecks such as the pattern of income distribution. Such dynamic benefits of LAFTA participation could allow Mexico to accelerate its industrial growth rate, a factor of major importance in view of the declining stimulus of import substitution to industrial growth. Such dynamic benefits should also generate a more balanced pattern of industrialization. Other dynamic benefits associated with the expansion of regional trade in manufactures include the development of manufactured exports able to compete in world markets, thus serving to transform the traditional export sector, and the attraction of foreign

investment in manufacturing because of the access of Mexican industries to a regional market. Finally, a country such as Mexico can acquire certain "learning effects" from participation in a regional integration scheme which could enable Mexico to more effectively compete in world trade markets.

A second category of benefits that Mexico might gain from participating in LAFTA could be termed the short-run benefits of participation. Such a short-run benefit might include the contribution of regional trade surpluses to Mexico's overall trade balance and the strengthening of Mexico's bargaining position in world trade, in that the immediate effect of a trade union is to increase the elasticity of the reciprocal demand curve of the union for a third country's products while reducing the elasticity of the third country's reciprocal demand curve for the union's products.

Some of the dynamic benefits of participation in LAFTA referred to above are difficult to measure directly. Their magnitudes can only be indirectly implied by the rate of growth and composition of Mexico's regional exports of manufactured goods. This would be true in the case of the external economies and rationalization of industry associated with expanded regional exports of manufactured goods. Most of the dynamic benefits of participation and short-run benefits of integration can, however, be directly measured by examining the rate of growth and composition of Mexico's regional exports.

The growth and composition of LAFTA regional trade

Several aspects of the growth and composition of LAFTA regional trade were discussed in Chapter I and Chapter IV of this paper. In Chapter I it was pointed out that LAFTA regional trade has been growing at a much faster rate than LAFTA's trade with the rest of the world. The former increased by 144 per cent while the latter increased by 27 per cent during the period 1961-1968 (Table 1). Although LAFTA regional trade only represented 11.1 per cent of LAFTA's world trade in 1968, increases in LAFTA regional trade for the period 1961-1968 accounted for 25.4 per cent of the total increase in LAFTA's world trade for the same period. It was also pointed out that intra-regional trade has exhibited a higher degree of diversification, especially in the areas of semi-manufactured and manufactured exports, than has LAFTA's world trade. For the period 1962-1967 forty-six per cent of regional trade consisted of semi-manufactured and manufactured exports.

Regional exports of manufactured goods, however, have largely been the domain of the commercialists (Argentina, Brazil, and Mexico). In 1966, 68.3 per cent of all LAFTA exports of manufactured goods were attributable to the commercialists. In the area of highly sophisticated manufactured exports, the dominance of regional trade by the commercialists has been even greater. In 1966 the commercialists

exported 79. 8 per cent of the intra-regional exports of chemical products and 93. 1 per cent of the intra-regional exports of machinery and transportation equipment. The domination of the intra-regional trade in sophisticated manufactures by the commercialists is, as it was pointed out, of great importance to the future development of LAFTA. In 1967 trade in such sophisticated manufactures as precision instruments, transportation equipment, machinery, pulp and paper, plastics, and chemical products represented 63. 2 per cent of intra-regional trade in manufactures. Moreover, trade in these products has been the fastest growing element of trade in manufactures. From 1962 to 1966, intra-regional exports of machinery and transportation equipment alone increased from 1. 3 million dollars to 29. 0 million dollars--an increase of 2, 130 per cent for the period.[8]

In Chapter IV it was pointed out that Mexico's exports of manufactured goods have been growing at a much more rapid rate than Mexico's traditional exports in recent years. From 1966 to 1969, Mexico's total world exports increased by 21 per cent while Mexico's world exports of manufactured goods increased by 73 per cent during the same period (Table 37). The most dynamic element of this growth in manufactured exports was found to be in the growth of consumer durable and capital goods exports such as machinery, tools, electrical

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[8]U. N., "Industrial Development in Latin America," p. 24.

equipment and transport equipment.

While only 7. 9 per cent of Mexico's world exports went to Latin America in 1967, it was pointed out that 24. 9 per cent of Mexico's world exports of manufactures went to Latin America in that year, and 40. 4 per cent of Mexico's exports of chemical products, plastics, paper products, metal products, machinery, electrical materials, and transportation equipment went to Latin America in 1967, (Table 38). The largest part of those Latin American manufactured imports were absorbed by LAFTA (65. 7 per cent of Mexico's total Latin American manufactured exports went to LAFTA in 1967). It was therefore concluded that while Mexico's Latin American and LAFTA trade may represent a relatively minor share of Mexico's total world trade, Mexico's exports of manufactures to Latin America and LAFTA are very important elements of Mexico's total world exports of manufactures.

Mexico's ability to promote manufactured exports to LAFTA has compared favorably to the ability of other LAFTA participants to promote regional manufactured exports. LAFTA trade in negotiated products (negotiated trade was approximately 89 per cent of total trade in 1965) for the period 1962-1967 had the following composition: primary products, 54 per cent; semi-finished manufactures, 29. 1 per cent; and finished manufactures, 16. 9 per cent (Table 39).

TABLE 39

THE COMPOSITION OF LAFTA TRADE IN NEGOTIATED PRODUCTS BY COUNTRY FOR THE PERIOD 1962-1967
(Thousands of Dollars)

Country	Value of exports	Value of imports	Percentage of imports			Percentage of exports		
			Primary	Semi-finished manufactures	Finished manufactures	Primary	Semi-finished manufactures	Finished manufactures
Argentina	1,321,128.5	884,877.2	54.5	41.8	13.7	70.0	12.5	16.5
Brazil	762,578.5	928,535.9	65.7	27.0	8.3	42.8	40.1	17.1
Colombia	64,425.6	168,248.1	50.5	32.9	16.6	41.5	22.5	36.0
Chile	318,935.2	601,306.3	58.2	21.5	20.3	21.4	61.1	17.5
Ecuador	75,912.9	25,849.4	21.0	32.3	46.7	84.8	6.7	8.5
Mexico	237,415.4	113,076.8	13.0	27.3	59.7	33.2	45.6	21.2
Paraguay	100,970.0	18,235.5	28.1	24.3	47.6	68.2	23.5	8.3
Peru	284,798.5	354,395.3	66.7	8.8	24.5	44.9	40.0	15.1
Uruguay	92,372.5	164,012.3	41.1	41.3	17.3	66.3	17.5	16.1
Total	3,258,536.6	. .	. .	. .	. .	54.0	29.1	16.9

Source: Asociacion Latinoamericana de Libre Comercio, Comite Ejecutivo Permanente, El Comercio Exterior de la ALALC (CEP/Repartido 1161), Montevideo, June 17, 1969, p. 21.

Referring to Table 39 it can be seen that Mexico's regional exports of primary products as a percentage share of Mexico's total regional exports for the period 1962-1967 (33.2 per cent) were significantly smaller than the share of primary products in LAFTA's total trade in negotiated products (54.0 per cent). In fact, the percentage share of primary products of total regional exports for Mexico was the second smallest percentage share of all LAFTA participants (Chile had the smallest primary product content of exports--21.4 per cent). While Argentina's exports accounted for 40.5 per cent of total LAFTA exports for the period, it is significant to note that 70.0 per cent of Argentina's exports were primary products. Although Mexico's total exports to LAFTA were considerably less than either Argentina's or Brazil's total exports to LAFTA, Mexico's exports to LAFTA had a higher percentage content of both semi-finished and finished manufactures than the exports of either Argentina or Brazil for the period 1962-1967.

Several recurrent sources of conflict in LAFTA can be seen by examining the data presented in Table 39. First, the composition of the exports and imports of the relatively less-developed members of LAFTA (Paraguay, and Ecuador) for the period 1962-1967 tends to substantiate the claims of these countries that the structure of LAFTA has not allowed them to develop their domestic industries to the degree that LAFTA has served as a stimulus to industrialization for the more developed member of LAFTA. Because LAFTA does not provide for a

planned regional allocation of industry, but rather relies upon the free workings of regional trade to allocate industry within the region, it is the contention of the less-developed members of LAFTA that their role in LAFTA is essentially one of being a potential dumping ground for the high priced industrial products of the more developed members of LAFTA while being themselves relegated to largely exporting primary products to the region. Only 8. 3 per cent of Paraguay's LAFTA exports of negotiated products and 8. 5 per cent of Ecuador's exports of negotiated products to LAFTA consisted of finished manufactures for the period 1962-1967. During the same period 46. 7 per cent of Ecuador's imports from LAFTA and 47. 6 per cent of Paraguay's imports from LAFTA consited of finished manufactures. The less-developed members of LAFTA have, therefore, argued that LAFTA should reorient itself to be an instrument of programmed regional integration rather than an instrument solely for the promotion of regional trade.

While the relatively less-developed members of LAFTA had a high percentage content of manufactures in their LAFTA imports for the period 1962-1967, Argentina's and Brazil's LAFTA imports for this period had a low percentage content of manufactured goods, especially in finished manufactured goods where they had the lowest percentage import contents of such goods of all LAFTA participants (13. 7 per cent and 8. 3 per cent respectively). To a large extent, this was due to the superior competitive positions of these countries in the trade of

manufactured products, but to some degree the low percentage content of manufactured goods in their total LAFTA imports was due to the national protectionist policies of these countries. Such protectionist policies have been the object of criticism by other LAFTA participants who feel that these large, relatively developed countries could be more responsive to efforts of the less-developed members to expand their industrial exports. Mexico, on the other hand, had the highest percentage content of manufactured goods in its imports from LAFTA of all LAFTA members for the period 1962-1967. It might be argued that Mexico's willingness to purchase manufactures from other LAFTA members during this period might have been a factor contributing to the high content of manufactures in Mexico's export to LAFTA.

A final source of conflict in LAFTA is found in the lack of reciprocity in LAFTA trade. It can be seen from Table 39 that while Argentina and Mexico accumulated large trade surpluses from LAFTA trade during the period 1962-1967, the majority of the LAFTA countries incurred large trade deficits during the period (the trade surpluses of Paraguay and Ecuador were largely fostered by their status as less-developed members in LAFTA). In the case of Chile and Uruguay trade deficits in regional trade preceded the formation of LAFTA, but in the case of Brazil, Colombia, and Peru chronic trade deficits in regional trade have occurred only since the formation of LAFTA. Such intra-regional trade deficits, when they serve to compound the seriousness

of a country's world trade deficits, often result in that country's criticism of LAFTA for its lack of mechanisms which would guarantee reciprocity in intra-regional trade. Such criticisms have been frequently made during the ten year history of LAFTA.

While Mexico ranked only fifth among LAFTA members in the value of its regional exports for the period 1962-1967, it was pointed out from Table 39 that Mexico's exports had a high content of semi-finished and finished manufactures. Because of the composition of Mexico's LAFTA exports, Mexico has been able to favorably compete with the other large commercial powers of the region, Argentina and Brazil, in the export of manufactures. Although Mexico's exports to LAFTA for the period 1962-1967 were only 11.4 per cent of the combined value of Argentina's and Brazil's regional exports, Mexico's regional exports of manufactures were 19.3 per cent of the value of the combined manufactured exports of Argentina and Brazil for the period 1962-1967.

Moreover, the growth of Mexico's regional exports was much more rapid than the growth of either Argentina's or Brazil's regional exports during the period 1961-1967. While Argentina's regional exports increased by 171.4 per cent (100.0 million dollars to 271.4 million dollars) and Brazil's regional exports increased by 61.9 per cent (95.2 million dollars to 154.2 million dollars), Mexico's regional exports increased by 503.0 per cent (7.9 million dollars to 47.6 million dollars)

during the period 1961-1967.[9] As a result of the very rapid growth of Mexico's regional exports and the high content of manufactures in those exports, Mexico was able to annually increase its share of both regional trade and regional trade in manufactures during the period 1961-1967.

In view of the recent founding of the Andean Common Market, the relationship between the commercialists and the Andean countries (Bolivia, Chile, Colombia, Ecuador, and Peru) in the trade of manufactured goods is an interesting relationship to investigate. As pointed out before, one reason for the founding of the Andean Group was the domination of LAFTA trade in manufactures by the commercialists. In 1967, for example, 73 per cent of LAFTA manufactured exports excluding Venezuelan oil products came from the commercialists. Only 21.7 per cent of LAFTA manufactured exports came from the five Andean Group members in 1967. Yet, the Andean Group members absorbed 35.6 per cent of the total LAFTA exports of manufactured goods in that same year (Table 40).

One major reason for the lack of reciprocity in the Andean Group's trade in manufactures is found in the trade relationship of Argentina with the Andean Group. In 1967 the Andean Group absorbed 48.1 per cent of Argentina's regional exports of manufactures. Only

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[9]Asociacion Latinoamericana de Libre Comercio, El Comercio Exterior de la ALALC, p. 7.

TABLE 40

LAFTA TRADE IN MANUFACTURED PRODUCTS - 1967
(Thousands of U.S. Dollars)

Importer	Exporter					
	Bolivia	Chile	Colombia	Ecuador	Peru	Argentina
Bolivia	. .	720	136	94	352	3,717
Chile	1	. .	798	22	616	17,309
Colombia	1	966	. .	1,190	369	1,645
Ecuador	. .	1,297	4,278	. .	3	646
Peru	51	3,156	2,456	29	. .	10,239
Argentina	. .	8,369	2,258	34	13	. .
Brazil	81	2,238	87	129	917	20,255
Mexico	. .	4,836	224	649	5,678	4,494
Paraguay	13	146	59	33	6	4,576
Uruguay	. .	2,582	6	. .	12	5,411
Venezuela	. .	3,593	2,699	22	2,731	1,698
Total	148	27,903	13,001	2,200	10,697	69,711

Note:

Totals include only those products with export values exceeding $100. INTAL classifications of manufactures, while based on NABALAC coding appear to differ slightly from ALALC classifications of manufactures.

Source: Calculated from: Instituto para la Integracion de America Latina, Mexico: Exportaciones de Manufacturas a America Latina, 1966-1967, Series Estudios No. 1, (Buenos Aires: Instituto para la Integracion de America Latina, 1969).

TABLE 40--Continued

Exporter					
Brazil	Mexico	Paraguay	Uruguay	Venezuela	Total
2,058	419	. .	. .	. .	7,496
5,864	5,977	31	6	2,222	32,576
469	2,791	1	1	4,673	12,106
413	1,104	. .	. .	101	7,842
1,724	5,354	23	182	5,236	28,450
30,292	7,259	2,105	786	9,157	60,273
. .	4,549	. .	597	11,096	39,949
4,632	. .	2	12	. .	20,525
2,030	168	. .	182	. .	7,213
3,667	667	14	. .	. .	12,359
2,069	7,114	. .	4	. .	19,930
53,218	35,402	2,176	1,591	32,485	248,532

17.7 per cent of Argentina's regional imports of manufactures, however, came from the Andean Group. To a large degree, this lack of reciprocity in the trade of manufactures is traditional, and predates the formation of LAFTA, but as it was pointed out before, Argentina's protectionist policy is also an important factor determining the lack of reciprocity in trade in manufactures between Argentina and the Andean Group. Like Argentina, Brazil imported very few of its manufactured imports from the Andean Group in 1967 (8.6 per cent) while exporting 19.7 per cent of its regional manufactured exports to the Andean Group in 1967. Mexico however, received 55.5 per cent of its regional imports of manufactures from the Andean Group while sending 44.2 per cent of its exports of manufactures to the Andean Group in 1967. Although Mexico's imports of manufactures from the Andean Group were greater than their exports to the Andean Group in terms of percentages of total Mexican regional imports and total Mexican regional exports in 1967, it should be pointed out that Mexico's regional exports of manufactures were 72.5 per cent greater than Mexico's regional imports of manufactures in 1967. The Andean Group, therefore, accrued a trade deficit in manufactures of 4.3 million dollars with Mexico in 1967.

It would appear that trade with the Andean Group is very important to Mexico's plans to promote manufactured exports. Referring to Table 41 it can be seen that the Andean Group's imports from Mexico contain a very high percentage of manufactured goods: Bolivia, 80.4

TABLE 41

THE COMPOSITION OF MEXICO'S EXPORTS TO LAFTA MEMBERS IN 1968
(Thousands of Pesos)

Country	Total imports from Mexico	Imports of manufactures from Mexico	Imports of manufactures as a percentage of total imports
Argentina	130,997	86,683	66.2%
Bolivia	9,320	7,497	80.4
Brazil	162,895	58,075	35.7
Colombia	78.277	58,607	74.9
Chile	153,061	78,700	51.4
Ecuador	21,434	17,626	82.2
Paraguay	3,871	3,815	98.6
Peru	60,546	52,000	85.9
Uruguay	18,509	8,590	46.2
Venezuela	139,113	99,060	71.2
Total	778,023	470,653	60.5

Source: Calculated from: Secretaria de Industria y Comercio, Direccion General de Integracion Economica Latinoamericana, "Evolucion Global del Intercambio Comercial de Mexico con la ACALC, 1961-1968" (Mexico, D.F.: Direccion General de Integracion Economica Latinoamericana, March, 1969), Anexo B. (Mimeographed.)

per cent; Colombia, 74.9 per cent; Chile, 51.4 per cent; Ecuador, 82.2 per cent; and Peru, 85.9 per cent. As LAFTA trade expands, assuming that the composition of Mexico's exports to the LAFTA members remains relatively the same, the Andean Group could become much more important to Mexico's efforts to expand manufactured exports.

While Mexico's exports to the Andean Group contain a high percentage of manufactured goods, these exports generally have a low content of sophisticated manufactures such as machinery and machine parts. In 1968 the Andean Group's imports of Mexican machinery and machine parts (18,210 thousand pesos) represented only 8.5 per cent of their total imports of Mexican manufactures, and 78.4 per cent of those imports of machinery and machine parts went to one country--Chile. If Chile's trade is discounted from the Andean Group, it is found that machinery and machine parts constituted only 2.9 per cent of the Group's imports of Mexican manufactured goods.[10]

Brazil, on the other hand, was a large importer of Mexican machinery and machine parts, despite the fact that only 35.7 per cent of Brazil's imports from Mexico in 1968 (Table 41) consisted of manufactured goods. Of the 58 million pesos of manufactured goods that Mexico exported to Brazil in 1968, 22.2 per cent of those exports consisted of machinery and machine parts. It would appear that while the Andean Group is a good market for Mexico's exports of manufactures in general, it is not such a good market for Mexico's exports of sophisticated manufactures such as machinery and machine parts. Machinery and machine parts, while constituted 12.4 per cent of

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[10]Mexico, Secretaria de Industria y Comercio, Direccion General de Integracion Economica Latinoamericana, "Evolucion Global del Intercambio Comercial de Mexico con la ALALC, 1961-1968" (Mexico, D. F.: Direccion General de Integracion Economica Latinoamericana, March, 1969), Anexo B. (Mimeographed.)

Mexico's regional exports of manufactures in 1968 (58.4 million pesos), were almost entirely absorbed by the four largest and most industrialized members of LAFTA (other than Mexico). In 1968, 93.3 per cent of Mexico's regional exports of machinery and machine parts were absorbed by Argentina (6.1 million pesos), Brazil (12.9 million pesos), Chile (14.3 million pesos), and Venezuela (21.2 million pesos).[11]

Mexico's major manufactured exports to the region and their values in 1968 were the following: books, 100.3 million pesos; tar, pitch and resin, 40.3 million pesos; organic and mineral materials for industrial use, 39.3 million pesos; tubes of iron and steel, 33.5 million pesos; motors for autos, 20.6 million pesos; poliphosphates of sodium, 19.1 million pesos; and parts for radios and radio cabinets, 18.6 million pesos.[12] Altogether, these products accounted for 57.7 per cent of Mexico's regional exports of manufactures in 1968. It is interesting to note that as the complexity of these products increases, the domination of Mexico's exports of the above products by the more industrialized members of LAFTA apparently increases. While only 55 per cent of Mexico's regional exports of books went to the four most industrialized trading partners of Mexico, 73.6 per cent of Mexico's exports of tar, pitch, and resin went to Argentina, Brazil, and Chile. Of Mexico's regional exports of organic and mineral

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[11] Ibid.

[12] Ibid., p. 4.

materials for industry, 75.6 per cent went to Argentina, Chile, and Venezuela. Mexico's regional exports of motors for autos were completely absorbed by Chile and Venezuela and 95.8 per cent of Mexico's regional exports of poliphosphates of sodium were imported by Chile. Finally, 100.0 per cent of Mexico's exports of parts for radio's and radio cabinets were imported by Argentina and Brazil. [13]

The larger countries of LAFTA not only absorb the largest part of Mexico's exports of sophisticated manufactures, they also, with the exception of Chile, represent the fastest growing markets for Mexico's region exports. This trend has, in part, been fostered by the move toward subregional integration within LAFTA in recent years. While Chile is one of the larger markets for Mexican products, Chile is also a member of a subregional group--the Andean Group. Chile's imports of Mexican goods have actually been declining in recent years, as have Peru's imports of Mexican goods. During the period 1965-1968 Chile's imports of Mexican goods declined by 12.2 per cent (from 13.9 million dollars in 1965 to 12.2 million dollars in 1968). [14] For the period 1967-1969, Chile's imports from Mexico declined by 15.1 per cent (from 14.1 million dollars in 1967 to 12.0 million dollars in 1969) and Peru's imports from Mexico declined by 0.3 per cent (from 5.92 million dollars in 1967 to 5.90 million dollars in 1969). [15]

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[13] Ibid.

[14] Ibid., Anexo B.

[15] Ibid.

Increased inter-Andean Group trade by these two largest members of the Andean Group was largely responsible for these countries' declining imports from Mexico in recent years. The major exception to this trend in the Andean Group's trade with Mexico is found in Colombia, whose imports from Mexico increased by 449.5 per cent during the period 1967-1969 (from 3.7 million dollars in 1967 to 20.1 million dollars in 1969).[16] With greater progress toward integration within the Andean Group, however, it is likely that Colombia will transfer much of its trade with Mexico to its fellow Andean Group members.

Argentina, Brazil, and Venezuela, on the other hand, have rapidly increased their imports from Mexico in recent years. Argentina and Brazil absorbed only 28.3 per cent of Mexico's regional exports in 1965. During the period 1965-1968, however, the growth of Argentina's and Brazil's imports from Mexico (41.9 per cent and 153.3 per cent respectively) exceeded the overall growth of Mexico's regional exports (41.6 per cent). As a result, Argentina and Brazil absorbed 37.4 per cent of Mexico's regional exports in 1968. If Venezuela, whose imports from Mexico increased by 40.1 per cent during the period 1965-1968, is included with Argentina and Brazil, the importance of Mexico's trade with the more industrialized members of LAFTA is more clearly seen. During the period 1965-1968,

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[16] Ibid.

Mexico's exports to LAFTA increased by 18.3 million dollars (from 44.0 million dollars to 62.2 million dollars). During this same period, the combined Mexican exports to Argentina, Brazil, and Venezuela increased by 13.8 million dollars (Argentina, 7.4 million dollars to 10.5 million dollars; Brazil, 5.1 million dollars to 12.8 million dollars; and Venezuela, 7.3 million dollars to 10.3 million dollars).[17] Collectively, Mexico's exports to Argentina, Brazil, and Venezuela, therefore, accounted for 75.4 per cent of the total increase in Mexico's regional exports between 1965 and 1968.

It might be concluded from the above observations that while the Andean Group is a very important market for Mexico's exports of manufactures, Mexico's manufactured export to the Andean Group (with the exception of Chile) appear to have a relatively low content of sophisticated manufactures (i.e., consumer durable and capital goods). Moreover, Mexico's exports to the two largest members of the Andean Group, Chile and Peru, have declined in recent year. This decline in Chile's and Peru's imports from Mexico may be an omen of the future trend of Mexico's trade with the Andean Group as subregional integration proceeds within the Andean Group.

While Argentina, Brazil, and Venezuela collectively had a lower average content of manufactures (56.3 per cent) in their total imports from Mexico than did the Andean Group (66.5 per cent) in

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[17] Ibid., Anexo B.

1968 (Table 41), it would appear that the larger, more industrialized members of LAFTA have a higher content of sophisticated manufactures in their total imports of manufactures from Mexico than do the Andean Group members (with the possible exception of Chile). Argentina, Brazil, and Venezuela, moreover, have significantly increased their collective share of Mexico's total exports in recent years.

As it will be pointed out in this chapter, the mechanisms that Mexico has employed to expand its regional exports of manufactures have increasingly been directed towards expanding trade with Argentina, Brazil, and Venezuela. The success of these mechanisms, however, has produced a strong motive for subregional groupings. Such subregional groupings could, moreover, result in a slowing down of the growth of Mexico's manufactured exports to the members of such subregional groupings. This has been the experience of Mexico with the two largest members of the Andean Group, Chile and Peru. Barring an improbable new direction to the current restructuring of LAFTA, it would therefore appear that Mexico's trade with Argentina, Brazil, and Venezuela will provide an even greater impetus to Mexico's expansion of regional exports of manufactures in the future than it has in the past.

At present, the imports of Mexican manufactures by Argentina, Brazil, and Venezuela exhibit a substantial degree of diversification. Mexico's major exports of manufactures to Argentina and their

percentage shares of total Mexican exports to Argentina in 1968 were as follows: pitch and tar, 15.6 per cent; printed books, 11.6 per cent; radios and parts, 11.5 per cent; dodecylbenzene, 6.6 per cent; iron and steel piping, 2.3 per cent; apparatus for installing electrical conduits, 2.3 per cent; spare parts for auto motors and agricultural machinery, 2.5 per cent; iron and steel tanks and containers, 1.5 per cent; and typewriters, 1.2 per cent. The above manufactured goods accounted for 55 per cent of Argentina's total imports from Mexico and 83.3 per cent of Argentina's imports of manufactures from Mexico in 1968.[18]

Mexico's major exports of manufactures to Brazil and their percentage shares of total Mexican exports to Brazil in 1968 were as follows: pitch and tar, 6.7 per cent; propeller-driven boats, 1.5 per cent; machinery parts, 4.0 per cent; typewriters, 3.1 per cent; electric meters, 2.4 per cent; iron and steel piping, 2.3 per cent, radio parts, 2.2 per cent; dodecylbenzene, 1.7 per cent; and printed books, 1.2 per cent. The above manufactures accounted for 25.1 per cent of Brazil's total imports from Mexico and 70.4 per cent of Brazil's imports of manufactures from Mexico in 1968.[19]

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[18]"Trade Relations Between Mexico and Argentina," Comercio Exterior de Mexico, XVI, No. 10 (October, 1969), p. 36.

[19]"Mexican-Brazillian Trade Relations," Comercio Exterior de Mexico, XVI, No. 8 (August, 1969), p. 22.

Mexico's major exports of manufactures to Venezuela and their percentage shares of total Mexican exports to Venezuela in 1968 were as follows: printed books, 18.9 per cent; automobile engines, 9.9 per cent; medicine, 2.8 per cent; typewriters, 2.5 per cent; iron and steel machine parts, elbows, and couplings, 4.2 per cent; and propeller-driven boats, 1.9 per cent. The above manufactures accounted for 40.2 per cent of Venezuela's total imports from Mexico and 56.5 per cent of Venezuela's imports of manufactures from Mexico in 1968.[20]

It is apparent that Mexico's exports to the above LAFTA members are not only diversified, they also contain a large measure of consumer durable and producer goods, inter alia, auto engines and parts, propeller driven boats; iron and steel pipes and parts, machinery parts, chemicals, and pitch and tar. Mexico's large exports of books to these countries is notable because of the strong linkage effects that such exports have with Mexico's fledgeling pulp and paper industry.

It is reasonable to expect that as Mexico's trade with Argentina, Brazil, and Venezuela assumes an ever larger share of Mexico's total LAFTA trade, the above manufactured goods will assume ever larger shares of Mexico's LAFTA exports. This trend has in fact, been established in recent years. Based on the first months of 1969, the

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[20] "Mexican-Venezuelan Trade Relations," Comercio Exterior de Mexico, XVI, No. 3 (March, 1969), p. 24.

major Mexican manufactured exports to LAFTA and their percentage share of Mexico's total exports were as follows: machinery and machinery parts, 11.5 per cent; books, 10 per cent; tar, pitch, and organic or mineral materials for industrial use, 8.0 per cent; iron and steel pipes, receptacles, and structures, 7.6 per cent; and auto motors and parts for auto motors and transmissions, 6.7 per cent. These products accounted for 43.8 per cent of Mexico's total exports to LAFTA for the first nine months of 1969 in comparison to a 34.4 per cent share of Mexico's LAFTA exports for the same period in 1968.[21]

The dynamic benefits of participation

Philippe C. Schmitter and Ernst B. Haas, in their discussion of the factors which motivated Mexico to join LAFTA in 1960, suggested that Mexico's participation in LAFTA would depend upon Mexico's ability to expand regional exports of what were considered "priority" manufactures.[22]

"Priority" manufactures were considered to be those manufactures that were currently being produced under conditions of industrial undercapacity due to limitations in the domestic market or a

[21] "Mexico's Latin American Trade," Review of the Economic Situation of Mexico, XLV, No. 531 (February, 1970), p. 36.

[22] Schmitter and Haas, Mexico and Latin American Economic Integration, p. 24.

lack of rationality in their initial development. Fostered under the umbrella of national protection, often in monopoly positions, the firms producing such products had both high production costs and high profit margins. Because these "priority" products had strong linkages with other major Mexican industries, they served to transmit their high cost to a wide spectrum of Mexican industries. It was also noted that these products were subject to potentially high economies of scale that could only be attained through gaining access to a larger market than the domestic market offered. It was felt by the Mexican planner that the solution to the "dilema" of Mexico's development in 1960 involved the rapid outward promotion of such "priority" products. But, these products could not at that time effectively compete in world markets. An immediate solution to this thorny problem was found in Mexico's participation in LAFTA.

Those "priority" products around which Mexico's expectations revolved were identified by Philippe C. Schmitter and Ernst B. Haas as being machinery, vehicles, metals, metal products, chemicals, and petro-chemical products.[23]

The above analysis of Mexico's LAFTA trade would appear to indicate that Mexico's expectations concerning trade in "priority" products shows much promise of being satisfied. As it was pointed

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[23] Ibid.

out before, while only 7.9 per cent of Mexico's total exports went to Latin America in 1967, 24.9 per cent of Mexico's total manufactured exports and 40.4 per cent of what might be termed Mexico's "priority" exports went to Latin America in that year. In 1967 Mexico's exports of manufactures to Latin America largely came from five classes of manufactures: chemicals paper products; metal and metal products; machines and electrical materials; and transportation equipment. Together these classes accounted for 91.8 per cent of Mexico's total Latin American exports of manufactures in 1967. (Table 38).

Not all of the dynamic benefits that Mexico has acquired or will acquire from participation in LAFTA can, however, be associated with the improvements which might take place in the production of those "priority" products referred to by Philippe C. Schmitter and Ernst B. Haas.

Another important by-product of Mexico's participation in LAFTA has been the inflow of foreign investment to Mexico and other LAFTA members in those areas of manufacturing where a high level of regional trade is expected. Specific examples of this foreign investment were given in Chapter I.

The one dynamic benefit of Mexico's participation in LAFTA that is most visible, however, has been the contribution of LAFTA trade to the transformation of Mexico's export sector. As it was pointed out in the last chapter, Mexico's traditional exports have been

performing poorly for the last decade. Mexico's capacity to import has been severely restrained as a result of this poor export performance. Alternative sources of foreign exchange such as long-term capital inflows and border trade and travel inflows have largely been offset by more rapidly growing foreign exchange outflow items such as investment income outflows and border trade and travel outflows. These alternative sources of foreign exchange, therefore, can no longer be expected to compensate for Mexico's chronic trade deficits. To continue to satisfy its crucial import needs, Mexico must, therefore, accelerate the growth of its export earnings. It was concluded in Chapter IV that such an acceleration of export earnings can only be realistically accomplished through a transformation of Mexico's exports--from traditional exports to manufactured exports.

A distinction was made, however, between two general categories of manufactured exports--labor-intensive manufactures and consumer durable and capital manufactures. It was pointed out that while the promotion of labor-intensive manufactures is desirable, it is not as desirable as the promotion of sophisticated manufactures. Because of the high income elasticity of world demand for sophisticated manufactures and the relatively few trade restrictions hindering the export expansion of such manufactures, the world exports of sophisticated manufactures have been growing at a significantly faster rate than the world exports of labor-intensive manufactures.

Through participation in LAFTA, Mexico has been able to generate a viable trade in sophisticated manufactures. Such LAFTA exports of sophisticated manufactures not only complements Mexico's world exports of largely labor-intensive goods, they also serve to create those conditions prerequisite to the export of such sophisticated manufactures to world markets.

The short-run benefits of participation

Another benefit that Mexico has received from participating in LAFTA is found in Mexico's growing regional trade surplus. This trade surplus has been referred to as a short-run phenomena because it is doubtful that Mexico will be able to maintain this surplus in the face of the growing pressure for increased trade reciprocity in LAFTA. It can be seen from Table 42 that Mexico's LAFTA trade surplus has grown rapidly since 1960. From 1960 to 1969 the trade surplus increased from 61.9 million pesos to 429.1 million pesos. In 1969, the largest part of the 429.1 million pesos surplus came from Mexico's trade with Colombia and Venezuela (Table 43). Mexico's trade surplus with Colombia was 243.5 million pesos and Mexico's trade surplus with Venezuela was 140.7 million pesos in 1969. This sizeable regional trade surplus has served to at least partially offset the chronic world trade deficits of Mexico.

TABLE 42

THE COMMERCIAL BALANCE OF MEXICO
WITH THE COUNTRIES OF LAFTA
(Thousands of Pesos, Current Prices)

Year	Exports		
	Value	Percentage of world exports	Percentage change over the previous year
1957	122,490	. .	. .
1958	103,665	. .	. .
1959	120,175	. .	. .
1960	110,708	1.0	- 7.9
1961	137,255	1.3	23.9
1962	264,273	2.3	92.0
1963	399,336	3.3	51.0
1964	572,029	4.4	43.0
1965	549,602	3.9	- 3.9
1966	803,154	5.4	46.0
1967	715,993	5.0	-10.8
1968	778,000	6.0	8.7
1969	1,076,887	6.0	38.0

Notes: The data presented does not include free zone transactions and is not strictly comparable to other data because of recent re-evaluations of LAFTA trade statistics for 1966 and 1967 when Bolivia and Venezuela joined LAFTA.

Source: Mexico, Secretaria de Industria y Comercio, Direccion General de Integracion Economica Latinoamericana, Integracion Latinoamericana (Mexico, D.F.: Direccion General de Integracion Economica Latinoamericana, No. 18, February, 1970), p. 10.

TABLE 42--Continued

Imports			Surplus Balance
Value	Percentage of world imports	Percentage change over the previous year	
67,302	. .	. .	55,187
46,286	. .	. .	51,379
69,781	. .	. .	50,394
48,822	0.3	-30.0	61,886
56,286	0.4	15.2	80,969
78,847	0.5	40.0	185,426
142,572	0.9	80.0	256,764
242,725	1.3	70.0	329,304
374,780	1.9	54.0	174,822
435,771	2.1	16.2	367,383
482,070	2.2	10.6	233,923
535,678	2.2	11.1	242,322
647,791	2.5	20.0	429,096

TABLE 43

MEXICO'S TRADE IN LAFTA IN 1969 BY COUNTRY
(Thousands of Pesos)

Country	Imports	Exports	Balance
Total	647,791	1,076,887	429,096
Argentina	154,875	174,823	19,948
Bolivia	16,797	11,759	- 5,038
Brazil	142,502	182,983	40,381
Colombia	7,780	251,326	243,546
Chile	104,063	149,812	45,749
Ecuador	9,270	17,270	7,885
Paraguay	4,779	4,344	- 435
Peru	136,849	74,070	- 62,779
Uruguay	20,272	19,431	- 841
Venezuela	50,389	191,069	140,680

Source: Calculated from: Mexico, Secretaria de Industria y Comercio, Direccion General de Integracion Latinoamericana, Integracion Latinoamericana (Mexico, D. F.: Direccion General de Integracion Economica Latinoamericana, No. 18, February, 1970).

The long-run and short-run costs of participation

The costs associated with a country's participation in a free trade association of less-developed countries such as LAFTA are most often thought of as emanating from trade diversion. Trade diversion within a regional grouping occurs when members of such a grouping divert their imports from lower priced third country products to higher priced regional products. Such a diversion is in effect, an income loss to the importing member. While it is certainly to be expected that some trade creation (i. e., a members diversion of imports from higher priced third country products to lower priced regional products) will result from participation in a free trade association such as LAFTA, it has generally been the concensus opinion of development economist that trade diversion will be significantly greater than trade creation in a regional grouping such as LAFTA. One might expect, therefore, that Mexico has probably accrued a short-run income loss from its participation in LAFTA.

Because of disparities in internal prices and exchange rates, as well as the effects of subsidies on the prices of exported products, it is difficult, however, to develop the real cost of trade (trade diversion - trade creation) resulting from an integration scheme such as LAFTA.

First, LAFTA is a proposed free trade area that has achieved only limited success in establishing regional free trade. Secondly, many of the members of LAFTA still carry on a majority of their trading outside of LAFTA.

Because a country such as Mexico is actively involved in promoting manufactured exports in the world market as well as in LAFTA, a reduction in those subsidies, price disparities, and exchange rate disparities associated with regional exports of manufactured products can not be effected without endangering Mexico's competiveness in world markets.[24]

Therefore, the "cost" of participating in LAFTA is more truely reflected in the difference between the real social cost of producing a regional export bundle and the regional export price to the importing member country. The short-run costs of participation, in other words, are largly born by the exporting members rather than by the importing member. This observation appears to be born out by the following study.

In an attempt to estimate the short-run cost of Mexico's participation in LAFTA for 1968, the itemized listing of Mexico's imports in Anuario Estadistico del Comercio Exterior de los Estados Unidos

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[24] To reaquaint himself with this situation, the reader can refer back to the discussion of Latin American price and exchange rate disparities in Chapter III.

Mexicano, 1968 was categorized according to each Capitulo of La Tarifa de Impuesto General de Importacion. These imports were further divided into manufactured and non-manufactured products using the INTAL classification of manufactured imports.

To determine the cost of participation for each imported item in which a LAFTA country participated, the average over-all per unit price of that imported item was calculated. Then the per unit price of that item for the LAFTA country or countries was calculated and subtracted from the overall average price of that item. The difference was then multiplied by the number of units of that item imported from the LAFTA country or countries. This value, if negative was listed as a cost of participation under the assumption that the item listed was homogeneous, and that Mexico could have purchased all of the item at the average overall price. If the value was positive, it was listed as a benefit under the same assumptions. The results of these calculations are shown in Table 44.

Overall, these calculations show that Mexico's imports from LAFTA in 1968 did not impose a cost in the form of trade diversion on Mexico. Instead, Mexico's imports from LAFTA resulted in an income gain, using the above methedology, of 25. 9 million pesos. An income gain was registered for both manufactured imports and non-manufactured imports from LAFTA. The income gain from the former (22. 6 million pesos) was nearly seven times the size as the income

TABLE 44

THE SHORT-RUN COSTS AND BENEFITS OF MEXICO'S PARTICIPATION IN LAFTA IN 1968
(Thousands of Pesos)

Costs/Benefits	NABALAC Sections (Capitulo's)									
	I. Live animals and products of live animals		II. Vegetable products		III. Oils, etc. animal & vegetable		IV. Food, drinks, tobacco		V. Mineral products	
	Manuf.	Non-manuf.	Manuf.	Non-manuf.	Manuf.	Non-manuf.	Manuf.	Non-manuf.	Manuf.	Non manuf.
Cost	0.5	3.6	. .	234.2	27.9	. .	44.1	. .	. .	410.0
Benefit	1.0	56.0	. .	236.8	133.2	49.4	57.0	. .	. .	4,687.6
Net cost or benefit	0.5	52.4	. .	2.6	105.3	49.4	13.2	. .	. .	4,271.7

	VI. Chemical products		VII. Plastics, celulose, resins		VIII. Hides & leathers		IX. Lumber, cork, wood		X. Pulp & paper products	
	Manuf.	Non-manuf.	Manuf.	Non-manuf.	Manuf.	Non-manuf.	Manuf.	Non-manuf.	Manuf.	Non-manuf.
Cost	10,710.9	5.1	168.7	. .	0.1	. .	91.6	51.8	4,452.3	272.9
Benefit	5,718.7	42.6	599.2	. .	24.9	. .	680.2	178.3	2,453.5	261.7
Net cost or benefit	-4,992.2	37.4	430.5	. .	24.8	. .	588.5	126.4	-1,998.9	-11.2

TABLE 44--Continued

Costs/Benefits	NABALAC Sections (Capitulo's)									
	XI. Textiles		XII. Hats, shoes		XIII. Cement, glass		XIV. Jewelry		XV. Metals	
	Manuf.	Non-manuf.	Manuf.	Non-manuf.	Manuf.	Non-manuf.	Manuf.	Non-manuf.	Manuf.	Non-manuf.
Cost	25.1	24.8	75.0	. .	32.9	. .	. .	2,127.0	175.2	118.5
Benefit	9.8	934.4	87.1	. .	9,465.4	57.1	. .	. .	1,075.9	64.9
Net cost or benefit	-15.3	909.4	12.1	. .	9,432.5	57.1	. .	-2,127.0	897.8	-53.6
	XVI. Machines, Electrical materials		XVII. Transport equipment		XVIII. Optics, electronics		XIX. Munitions		XX. Others	
	Manuf.	Non-manuf.	Manuf.	Non. manuf.	Manuf.	Non-manuf.	Manuf.	Non-manuf.	Manuf.	Non-manuf.
Cost	1,607.3	. .	22.9	. .	180.1	. .	0.8	. .	38.2	66.6
Benefit	16,178.6	. .	1,719.0	. .	1,384.0	. .	85.2	. .	0.8	56.7
Net cost or benefit	15,178.6	. .	1,696.1	. .	1,203.9	. .	84.4	. .	37.4	- 9.8

	Total LAFTA Imports		
	Manufacturing	Non-manufacturing	Total
Cost	17,654.0	3,355.5	21,009.5
Benefit	40,278.3	6,620.7	46,899.0
Net cost or benefit	22,624.2	3,265.2	25,889.5

TABLE 44--Continued

Note: Only ordinary imports were examined. Free zone imports were not examined because they represented only ten per cent of total imports and contain few items from LAFTA members. Figures may not add because of rounding.

Source: Calculated from: Mexico, Secretaria de Industria y Comercio, Anuario Estadistico del Comercio Exterior de los Estados Unidos Mexicanos, 1968 (Mexico, D. F.: Talleres Gráficos de la Nación, 1969).

gain from the latter (3.3 million pesos).

Mexico's greatest income gains from LAFTA imports were registered in Section XVI imports (machines and electrical materials) and Section XII imports (cement and glass). The largest income losses were registered in Section VI (chemical products) and Section X (pulp and paper products).

In a comprehensive integration scheme, the prophesized large degree of trade diversion, in the form of higher regional import prices, probably would materialize in the trade accounts of participating members. But as it stands, participating in LAFTA appears not to be imposing a short-run cost on Mexico in terms of an excess of trade diversion over trade creation in its LAFTA imports. Mexico's short-run costs of participation in LAFTA, if any, are to be found in the subsidies, the price disparities, and the exchange rate disparities which in part determine the prices of Mexico's regional exports. As such, these costs would be found in Mexico's world exports as well as

in Mexico's regional exports.

Mexico's regional trade: Concluding remarks

It would appear that the benefits that Mexico has received from participating in LAFTA have exceeded the costs of such participation. It is, of course, Mexico's intent to maximize the benefits it receives from participating in LAFTA and to minimize the costs of participating in LAFTA. Towards this end Mexico has been actively involved in restructuring the trade liberalization mechanisms of LAFTA. Like all LAFTA members, Mexico is attempting to change LAFTA into a mechanism that will be more responsive to its needs. The future of Mexico's participation in LAFTA will, therefore, largely depend on the degree to which Mexico's views on LAFTA's restructuring prevail.

The Restructuring of LAFTA's Mechanisms of Trade Liberalization

The causes for the current restructuring of LAFTA's mechanisms of trade liberalization were discussed in Chapter I. In essence, the restructuring of LAFTA's mechanisms of trade liberalization has been caused by the extreme disparities in the development levels of the various members of LAFTA. Because the initial instruments of trade liberalization in LAFTA were only designed to promote trade in manufactured goods through the creation of a tariff free regional

market, it was natural that such trade would be dominated by the most industrialized members of the region--Mexico, Argentina, and Brazil.

In view of the domination of regional trade in manufactures by the most industrialized members, it was to be expected that the less-developed members of the region would attempt to restructure LAFTA's mechanisms of trade liberalization in such a way as to enable them to attain a more equitable share of the regional trade in manufactures.

Sidney Dell has observed that, "In LAFTA, it was inevitable that the process of reducing trade barriers should grind to a halt so long as no agreement was reached on the distribution of industry. The lack of such a policy means that the weak countries in the region have no assurance that their own infant industries will not be overwhelmed."[25]

The process of trade liberalization nearly did grind to a halt in 1967. By 1967 the Common List had suffered a de facto demise by the failure of LAFTA's Conference VII to develop a second addition to the Common List. National List concessions in 1967 increased by only 3.7 per cent. While the National List concessions of Argentina, Brazil, and Mexico increased by 5.4 per cent, 6.0 per cent, and 9.0 per cent respectively in 1967, the National List concessions of the

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[25]Dell, "Obstacles to Latin American Integration," p. 65.

remaining members increased by only an average 1.7 per cent.[26] By 1967 the less-developed members of LAFTA had, in essence, rejected the initial trade liberalization mechanisms of LAFTA. The impact of this rejection was clearly reflected in LAFTA trade for 1967. In 1967, LAFTA trade (exports plus imports) decreased by 2.9 per cent (Table 1), with trade decreases occurring for six of the nine LAFTA members.

While rejecting LAFTA's initial trade liberalization mechanisms, the less-developed members have not rejected the concept of LAFTA. They have only chosen a new course towards the objective of Latin America integration. This course was subregional integration within the framework of LAFTA. The Colombian representative to the Andean Common Market negotiations in 1968 expressed the sentiment of the less-developed members of LAFTA in his observation that: "Our nations, which compromise two-thirds of LAFTA, are convinced that Latin American integration will sooner or later be a reality. It would be extremely unwise not to prepare themselves through the subregional union so as to participate in ultimate economic from a position of strength."[27]

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[26] "Monthly Report on Latin American Integration," Comercio Exterior de Mexico, XVI, No. 9 (September, 1969), p. 6.

[27] "Monthly Report on Latin American Integration," Comercio Exterior de Mexico, XV, No. 10 (October, 1968), p. 20.

The more industrialized member of LAFTA faced with the prospects of a possible reduction in their trade with subregional group members while they prepare themselves for participation in the ultimate integration of the region, have intensified their efforts to increase trade among themselves.

In the remainder of this chapter the basic instruments of trade liberalization in LAFTA will be examined on the basis of three questions: 1) how has this instrument of trade liberalization evolved? 2) how does this instrument of trade liberalization function? and; 3) how does the functioning of this instrument affect Mexico's participation in LAFTA? Finally, some general observations on the future of LAFTA and Mexico's participation in LAFTA will be offered.

The demise of the Common List

The Common List, as established by Article 7 of the Treaty of Montevideo, was intended to be the key instrument for attaining the objective of completely free regional trade by mid-1973. It was to be, in fact, the only treaty devise guaranteeing a planned degree of irrevocable free trade within the region during the transitional period (1960-1973). Under Article 7 of the Treaty of Montevideo, LAFTA members were obligated to augment the Common List with products constituting twenty-five per cent of intra-regional trade in 1964, 1967, 1970, and 1973. Items once placed on the Common List could

not be removed from the Common List.

In 1964 the first addition to the Common List was successfully carried out by the members of LAFTA. The items contained in that first addition, however, consisted almost entirely of primary products. In 1967, however, an impasse was reached over the second addition to the Common List. The Seventh Ordinary LAFTA Conference in 1967 proposed an addition to the Common List consisting of two products--petro-chemicals and wheat. These two products accounted for 28.0 per cent of intra-regional trade in 1967. The inclusion of wheat to the Common List was opposed by Venezuela, Mexico, and Paraguay and the inclusion of petro-chemicals was opposed by Peru and Mexico. Since any member of LAFTA can veto a Common List proposal and since it was generally agreed that the inclusion of either wheat or petro-chemicals was necessary if the second addition to the Common List was to be accomplished, the impasse seemed hopeless.

Negotiations on the second addition to the Common List continued through 1968 and through most of 1969, ending with the suspension of Common List negotiations for a minimum of five years by the Ninth Ordinary LAFTA Conference in December of 1969.

The failure of the Common List was directly attributed to the impasse over the inclusion of either wheat or petro-chemicals to the second addition to the Common List, but the underlying causes for the

failure of the Common List are found in the divergent philosophies of the commercialist members and the integrationist members of LAFTA.

Argentina, Brazil, and Mexico--the commercialists--appear to be in general agreement that the drive towards regional integration should proceed via carefully constructed bilateral or complementary agreements among concenting LAFTA members. They argue, with some merit, that a tightly structured integration scheme is ill suited to the realities of a politically and economically diverse Latin America. Integration, in their view, can only be accomplished in Latin America through instruments that are flexible enough to change with the changing needs of the region. The Common List, in their view, does not provide this flexibility. The irreversibility of the Common List and its provision for a scheduled freeing of trade, in their view, could be an obstacle to the flexibility of their national development plans. Moreover, the Common List has no provision to promote trade in products not already traded within the region. In that the efforts of the commercialists are increasingly being directed at promoting intra-regional trade in manufactures currently not traded within the region, the Common List has been relegated by them to a secondary position.

The other eight members of LAFTA generally agree with the integrationists' position that regional integration must be tightly

structured, irrevocable, and scheduled. While they agree with the commercialists that the Common List has not provided an impetus to regional trade in manufactures they strongly support the basic principles of the Common List. A delegation of integrationists at the LAFTA Extraordinary Conference of 1968 expressed the sentiment of the integrationists in their observation that:

> The Common List must guarantee that zonal trade of products contained therein will be completely free once the twelve-year transitory period has ended and that, in consequence, any country adhering to the Common List, which developes or sets up an industrial branch, can rely on access to the Latin American market as of 1973. No guarantee can exist without the List. If country A grants a concession and country B establishes an industrial plant in order to exploit it, what is to be the fate of these installations should A decide to withdraw its concessions or to reduce the margin of preference which made its market accessible to goods produced by B ?[28]

If the Common List were to be suspended, the other major instruments of trade liberalization (i. e., the National List and the bilateral agreement) could not provide such guarantees to the integrationists.

The conflict between the positions of the commercialists and the integrationists was clearly reflected in the Ninth Ordinary Conference of LAFTA in December of 1969. While all of the members of LAFTA agreed that the existing Common List schedule was unworkable, their proposed solutions to this problem were very different.

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[28]"The LAFTA: A Year of Important Definitions, " Comercio Exterior de Mexico, XVI, No. 2 (February, 1969), p. 5.

The commercialists proposed an indefinite extension of the free trade deadline. Argentina, moreover, pledged a veto of any proposal calling for a scheduled irrevocable freeing of trade or a common market. The integrationists, on the other hand, proposed a common market deadline of 1985, to be attained in a scheduled, irrevocable fashion. A compromise proposal, the "Caracas Protocol," calling for an extension of the Common List deadline for free trade until 1980 and a suspension of Common List negotiations until 1974 was finally adopted.[29]

The suspension of the Common List in 1969 must be interpreted as a vistory for the philosophy of Mexico, Argentina, and Brazil concerning the course of LAFTA. With the suspension of the Common List, the industry sectoral has emerged as their chief instrument for promoting regional trade.

The industry sectoral

The industry sectoral was established by Resolution 55 and Resolution 119 of the Treaty of Montevideo, The purpose of the industry sectoral was to draw together firms of a particular industry from the various members of LAFTA so as to facilitate an exchange of information on production techniques, consumption patterns, and trade

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[29]"LAFTA's Conference IX," Business Latin America, December 18, 1969, p. 1.

opportunities among the member nations of LAFTA. As a by-product of this exchange of information, it was hoped that the attending firms would examine the possibilities of including the various products of their sector in the program of liberation through National List concessions and through complementation agreements. Such actions were to be taken at annually scheduled sectoral reunions, and the proposed trade concessions developed therein were to be recommended to the national governments of the participating firms for negotiation at the annual LAFTA conference.[30]

To gain acceptance as an industrial sector, LAFTA firms of any particular industry must file a letter of intent with the Permanent Executive Committee (PEC) of LAFTA. If their letter of intent is accepted by the PEC, these firms must then form an industrial association for participating in sectoral reunions.

During the early years of LAFTA, very few industrial associations were formed. It was generally felt by the LAFTA planners that the main impetus to the freeing of regional trade would have to come from direct government action and so little encouragement was initially given to the formation of industrial associations. This lack of encouragement was reflected by the fact that of the 2,318 National

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[30] A discussion of the framework of the sectoral meeting is contained in: Mexico, Secretaria de Industria y Comercio, Direccion General de Integracion Economica Latinoamericana, Integracion Latinoamericana (Mexico, D. F.: Direccion General de Integracion Economica Latinoamericana, No. 6, February, 1969), pp. 4-11.

List concessions proposed by sectoral reunions from 1964-1967, only 602 concessions (26 per cent) were adopted by member governments.[31]

By 1968, however, the sectoral reunion had assumed a new role as the most dynamic instrument of trade liberalization in LAFTA and as the major source of LAFTA National List concessions and industrial complementation agreements. In 1968 seventeen industrial associations held sectoral reunions. Of the 910 National List tariff-cut concessions recommended by these sectorals, 492 concessions (59 per cent) were accepted at the eighth LAFTA conference. These National List concessions represented 67.2 per cent of the 732 National List concessions adopted in 1968.[32]

In 1969 twenty-four sectoral reunions were held, and they were attended by 1,100 delegates from various Latin American industries. The 1969 sectoral reunions reflected a change in strategy by the major industries of the region in that only 345 National List concessions were proposed at these meetings as compared to the 910 concessions proposed at the 1968 sectorals. The focus of attention at the 1969 sectorals was instead directed towards the complementation agreement.

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[31] "Results of the 1968 Sectorals," Business Latin America, January 23, 1969, p. 20.

[32] Ibid.

The complementation agreement, as established by Resolution 99 of the Treaty of Montevideo in 1964, offers a greater degree of flexibility to the industrialist than the other mechanisms of LAFTA. Like the other mechanisms the end result of a complementation agreement (sometimes referred to as a bilateral agreement if only two countries are involved) is a bi-national or multi-national market for the product and the producer with all the benefits thereof. The distinguishing features of the complementation route to tariff concessions are its exclusivity and flexibility.

While National List concessions are open to exports from all LAFTA countries, the tariff cuts negotiated in a complementation agreement benefit only those countries that sign the accord (Bolivia, Ecuador, Paraguay, and Uruguay, however, are automatically extended preferences by Resolution 99). This permits a more selective structuring of multi-national markets, and helps to overcome protectionist resistance. For example, the complementation formula enables Argentina to open its markets to imports from Mexico for a specified item without subjecting its industry to competition from Brazil.

Although most agreements follow a standard format--indicating tariff concessions for specified products to be affected by the participating countries, product origin rules, administration of the accord, and escape clauses--there can be a good deal of flexibility in the accord. Accords can space tariff reductions over a period of years,

they can allow for new product concessions and the removal of old concessions when local production has grown sufficiently to supply the domestic market, and they can be easily withdrawn by a member. Moreover, the complementation pacts tend to reflect the attitudes of industrialists rather than of governments. Most such agreements have in fact been designed by the private sector.

For all of the above reasons the complementation agreement emerged as the main mechanism of trade liberalization in the 1969 sectoral meetings. While only 345 National List concessions were proposed at the 1969 sectoral reunions, 1,455 concessions were proposed in eight new complementation accord proposals and three renegotiated complementation accords. If one considers that only 262 complementation concessions were proposed at the 1968 sectoral reunions and that only nine complement accords have been approved to date by the PEC, the events of 1969 appear most significant.

The sectoral reunions of 1969 represented a wide spectrum of Latin American industry. Farm machinery, office machinery, plastics, chemical, machine tools, and electronics were just a few of the twenty-four industries represented at the 1969 sectoral reunions. Also represented at the 1969 sectoral reunions was a wide spectrum of international firms such as IBM, G. E., I. T. T., Sylvania, Fiat, Sperry Rand, and NCR. Their interest in the industry sectoral has grown as the influence of the industry sectoral has grown. At present

the various industry sectorals are united by the coordinating committee of the Latin American Enterprise Associations which acts as an advisor to the PEC. But, the sectorals are currently formulating a new organization, the Latin American Congress of Enterprise Associations, which would possibly hold a ministerial position at the annual conference of LAFTA nations. If such an organization does evolve, then the sectoral will have brought about a fundamental restructuring of LAFTA.

The question to be asked is, who has benefited from the sectoral and who is likely to benefit from the growing importance of the sectoral? The answer to this question becomes obvious from an investigation of the origin of sectoral National List concession and complementation concession proposals.

Of the 492 sectoral National List concession proposals adopted by the eighth LAFTA conference, 474 were proposed by Argentina, Brazil, and Mexico (each of these countries proposed between 150-160 concessions). The domination of the commercialists in sectoral National List proposals was also reflected in their domination of all National List concessions made in 1968. The commercialists proposed 73.7 per cent of all new National List concessions in 1968 (526 concessions) and 63.5 per cent of all renegotiated National List concessions in 1968 (206 concessions). It is of interest to note that 87.0 per cent of the total National List concessions made in 1968 consisted

of manufactured goods. Practically all of the concessions for manufactured goods consisted of concessions on finished capital and consumer durable goods (approximately 95 per cent).[33]

Of the 1, 821 National List or complementation concessions proposed by the 1969 sectoral reunions, 1, 526 concessions were authored by Argentina, Brazil, and Mexico. Furthermore, the commercialists authored 94. 9 per cent of the 1, 455 complementation concessions proposed at the 1969 sectoral reunions.[34] In addition to the eight new complementation accords and three renegotiated complementation accords proposed by the sectoral reunions in 1969, preliminary discussions on complementation accords by the following countries in the following sectorals were held: photography, Brazil and Mexico; food products, Argentina and Brazil; plastics, Argentina, Brazil and Mexico; pharmaceuticals, Argentina, Brazil, Mexico, Uruguay, and Venezuela; and electric lamps, Mexico and Brazil. Those eight new accords adopted at the sectoral reunions in 1969 and the countries signing these accords included: office machinery, Argentina, Brazil, and Mexico; pharmaceuticals, Argentina, Brazil, Mexico, Uruguay, and Venezuela; electrical and electronics

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[33] "A Monthly Report on Latin American Integration," Comercio Exterior de Mexico, XVI, No. 8 (August, 1969), p. 6.

[34] "Summary of the 1969 Sectorals," Business Latin America, January 1, 1970, pp. 1-3.

industries (four pacts), Argentina, Brazil, Mexico, and Uruguay; and medical and dental equipment (two pacts), Argentina, Brazil, Mexico, and Uruguay.[35]

Whereas in past years the sectoral reunions were well attended by industries from all of the LAFTA members, most of the 1969 reunions were attended by few industries from countries other than Argentina, Brazil, and Mexico. This was a reflection of the growing resentment and suspicion of the integrationists towards the growing domination of the sectoral reunions by the commercialists.

Of the nine complementation agreements already in existance and approved by the PEC (the eight agreements of 1969 are not yet approved) Mexico has requested further study on or signed eight proposals: electronic tubes, electrical domestic appliances (two agreements), electronic and electrical communications, chemicals, petrochemicals, glass, and electrical power equipment. Argentina has participated in six agreements and Brazil has participated in seven agreements.[36] In view of the results of the 1969 sectoral reunions, it would appear that the sectoral reunion will increasingly reflect the views of the commercialists. It would also appear that through the

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[35]Ibid.

[36]Asociacion Latinoamericana de Libre Comercio, Comite Ejecutivo Permanente, Actualizacion de los Acuerdos de Complementacion (CEP/Repartido 1074/Rev. 2), Montevideo, July, 1969, pp. 1-5.

sectoral reunion Argentina, Brazil, and Mexico will have an increasingly large share of their total LAFTA trade going to each other. Towards this end, Mexico and Brazil in 1969 formed a mixed Mexican-Brazilian economic commission, established offices of their national banks in each other's country, and formed a private trading consortium (Combramex) with the object of promoting an additional ten million dollars of trade between their countries during 1970.[37] Similar plans have been discussed by Argentina and Mexico.

To Mexico, the sectoral reunion is a dynamic instrument for promoting its regional trade, particularly in manufactures. Mexico's position of leadership in the sectoral reunions has yielded Mexico important benefits and it promises to yield even greater benefits as the influence of the sectoral reunion increases. But to the integrationists, the sectoral reunion represents an instrument through which the commercialists' domination of regional trade in manufactures will be expanded, and despite the offerings of preferences to the integrationists in the various complementation accords authored by the commercialists, the integrationists have chosen not to participate in such accords. They have, instead, chosen to strengthen their bargaining position in LAFTA through the formation of subregional groupings.

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[37] "Mexico and Brazil Move Toward Expanded Trade," Business Latin America, October 2, 1969, p. 314.

Subregional groupings

The subregional grouping, as defined by Resolution 202 of the Treaty of Montevideo, is looked upon as a temporary steppingstone to a larger area of integration. In this respect, the CACM, CARIFTA, and LAFTA may be viewed as steppingstones to an eventual Latin American Common Market.

There are at present two subregional groupings within LAFTA --The River Plate Group and the Andean Common Market. The River Plate Group was formed by the signing of the River Plate Basin Treaty by Argentina, Brazil, Bolivia, Paraguay, and Uruguay in April, 1969. The River Plate Group has as its purpose the establishment of multinational cooperation in developing regional infrastructure and national resources. The treaty makes no provision for a preferential treatment of trade among the signatory countries, and the treaty does not create a supernational governing board whose authority might pose a threat to national development schemes. Specifically, the River Plate Group will address itself to the integrated use of water resources (both hydro-electric and navigational) of the Plate River Basin and the coordination of the establishment of agricultural and industrial enterprises within the LAFTA framework of complementation agreements. As such, the River Plate Group promises to be little more than an extension of the industry sectoral and the national development plans

of Argentina and Brazil.

The treaty establishing the Andean Common Market (ACM), on the other hand, calls for joint action and harmonization efforts in development planning and monetary and fiscal policies among the five ACM members--Bolivia, Colombia, Chile, Ecuador, and Peru (Venezuela was involved in the formulation of the treaty, but has not yet signed the treaty).

The Andean Common Market agreement signed in Bogota in May, 1969 created a supernational junta and an industrial commission (The Andean Commission) to oversee the complete integration of the region by 1985 (integration between Chile, Colombia, and Peru will be completed by 1980). The ACM will develop its own sectoral reunions for the purpose of developing interim complementation agreements, allocating regional industries, and coordinating industrial investment.

The ACM goes far beyond the scope of LAFTA in establishing regional integration. Yet, the ACM must operate within the framework of LAFTA. Undoubtedly, this situation will be a future source of tension in LAFTA. It is the contention of the ACM members, however, that given the disparities in the levels of development of the various LAFTA members, and given the existing mechanisms of trade liberalization in LAFTA, the achieving of Latin American free trade will only be possible when they can compete on an equal basis with the commercialists. The ACM, in their view, offers the only

realistic means of attaining that position.

It might be expected that Mexico's trade with the ACM will diminish during the next several years as intra-ACM trade expands. While this expectation has been a source of concern to Mexico, Mexico has taken a tolerant long-run view of this situation. This view is represented by the statement of Antonio Carrillo Flores, the Mexican Minister of Foreign Affairs, that, "Mexico continues to favor the idea of subregional groupings and is disposed to back them by either joining in or staying out. It is precisely because subregional integration may make it possible to attenuate one of the LAFTA's major sources of trouble, namely, the co-existence of countries with very different development levels within its framework, that the non-participation of the "big" countries is an important tactic in the integration process strategy."[38]

Mexico's participation in LAFTA: Final remarks

It has been suggested that Mexico's future participation in LAFTA will largely depend on the direction of the current restructuring of the framework of LAFTA. While the restructuring process might involve a short-run decline in Mexico's trade with the ACM,

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[38]"A LAFTA Pilot Sector," Comercio Exterior de Mexico, XVI, No. 4 (April, 1969), p. 4.

this will be more than compensated for by Mexico's increased trade with Argentina and Brazil. Mexico's successes in the sectoral reunions has opened a new dimension of trade expansion for the Mexican industrialist and development planner via the complementation accord. With this new tool, Mexico's ability to expand its manufactured exports will be greatly enhanced!

CHAPTER VI

CONCLUSIONS

In Chapter I it was stated that the analytical basis for evaluating Mexico's participation in LAFTA could be derived from the answers to three questions: (1) Why did Mexico join LAFTA in 1960 after a history of little interaction with its Latin American neighbors, and what benefits did Mexico expect to receive from its participation in LAFTA; (2) To what degree has Mexico received those benefits that it expected to receive from its participation in LAFTA; and (3) What forces will shape Mexico's participation in LAFTA in the future? During the course of this paper the above questions have been answered.

Mexico's decision to join LAFTA in 1960 was necessitated by the growing needs for industrialization in Mexico and the apparent inability of the traditional "inward" tools of industrialization to satisfy those needs. These same motivational factors were also found in Latin America as a whole.

The growing needs for industrialization in Mexico centered around the rapid growth of population in Mexico and the even more

rapid urbanization of that population, and the poor performance of alternative wealth producing economic activities in stimulating economic development.

The dilemma of Mexico's development, as hypothesized by Raymond Vernon, was that Mexico's "inward" tools of industrialization appeared to be increasingly ineffectual in satisfying the above needs. Raymond Vernon hypothesized that Mexico's industrialization was approaching stagnation due to the existence of certain restraints to the further use of "inward" industrialization. Those restraints were the regressive pattern of income distribution in Mexico, the decline of Mexico's import coefficient, the narrowness of the domestic market for sophisticated manufactures, and the poor performance of Mexico's export sector in providing an adequate capacity to import. Raymond Vernon's stagnation thesis was given weight by the fact that much of Mexican industry was operating at less than full capacity and at high costs in 1960, the labor-absorption of industry was not keeping pace with urban population growth, and both GNP per capita and GIP per capita had declined during the period 1955-1962.

Mexico's decision to join LAFTA in 1960 was essentially predicated upon Mexico's attempt to acquire an alternative tool of industrialization to escape from this dilemma. The benefits that Mexico expected to receive from LAFTA participation were chiefly centered around achieving a high level of regional exports of manufactures,

especially sophisticated capital and consumer-durable manufactures. Such benefits would include: a lowering of industrial costs through the exposing of domestic industries to regional competition and through the achievement of economies of scale; the fostering of new industries previously unable to develop within the narrow domestic market; and the transformation of Mexico's poor performing, primary product oriented export sector. The realization of these benefits would, of course, act as a strong stimulus to Mexico's industrialization.

Unlike the case of Latin America as a whole, however, it appears that Raymond Vernon's prognosis of industrial stagnation in Mexico was erroneous. While the needs for industrialization in Mexico have continued to grow since 1960, so has Mexico's ability to satisfy those needs, largely through "inward" industrialization. Industrial growth in Mexico has accelerated since 1960 as has the labor-absorption of Mexican industry. This improved performance is in sharp contrast to the rather dismal performance of Latin American industrialization as a whole since 1960.

The improved performance of "inward" industrialization in Mexico since 1960 should not, however, lead to a diminished Mexican preference for participation in LAFTA. The obstacles to "inward" industrialization in Mexico still exist, and in some cases, they have intensified since 1960. Mexico's ability to accelerate industrial growth since 1960 has been accomplished not so much by the removal

of the restraints to "inward" industrialization as it has been due to a more effective use of "inward" tools within those restraints via a high level of direct and indirect government participation in industry.

Moreover, the undesirable characteristics of "inward" industrialization (i. e., high costs and inefficiency) found in the industries of other LAFTA members are also present in the industries of Mexico. These undesirable characteristics impose a high social cost on Mexico's industrialization efforts--a cost which some planners feel Mexico can no longer afford.

While Mexico has been able to accelerate industrial growth, the performance of Mexico's export sector has continued to be dismal. While William Friethaler, writing in 1967, hypothesized that Mexico had escaped the trade-gap hypothesis of Bela Balassa and was well on the way towards constructing a viable export sector based on diversified foodstuffs and primary product exports, little proof exists to substantiate his hypothesis. Mexico's critical import needs have consistently been greater than the ability of export earnings to satisfy those needs. Whereas, Mexico could rely upon alternative sources of foreign exchange (i. e., long-term capital inflows, tourism, and b order trade) to compensate for trade deficits in the past, they are no longer able to do so in that investment income outflows and tourist outflows now largely offset the above sources of foreign exchange.

To meet its growing critical import needs, Mexico must accelerate the growth and earnings of its exports. To accomplish this goal, it would appear that Mexico must change the composition of its exports. Traditional exports in view of the structuralist arguments and their actual performance, must give way to manufactured exports.

So, despite the changes that have taken place in Mexico's industrialization since 1960, it would appear that the same basic factors that motivated Mexico to join LAFTA in 1960 are still present in Mexico.

LAFTA, as a tool of industrialization, has performed well for Mexico, and it promises to be an ever greater stimulus to Mexico's industrialization in the future. While Mexico's exports to LAFTA in 1961 were largely primary products, by 1969 seventy per cent of Mexico's exports to LAFTA consisted of manufactured goods. Unlike Mexico's manufactured exports to world markets, which consist largely of labor-intensive consumer non-durable manufactures, Mexico's manufactured exports to LAFTA almost entirely consist of durable consumer and capital goods--those manufactured generating the greatest dynamic benefits from expanded trade. Moreover, Mexico's exports to LAFTA have grown at a phenomenally fast rate over the past seven years (approximately 35 per cent in 1968 and 1969).

The rapid growth of Mexico's manufactured exports to LAFTA has, to a large degree, been a product of the restructuring of LAFTA

into a commercialist tool for the expansion of manufactured exports. With the emergence of the industry sectoral meeting as the major instrument of trade liberalization in LAFTA and the binding together of the commercialists through complementation agreements, LAFTA promises to be an even better tool for the promotion of Mexican industry. Because of the above points, Mexico's preference for industrialization through participation in LAFTA should be expected to increase rapidly in the future.

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