Bankers' demands on Mexico are intolerable: the import question

by David Goldman, Economics Editor

Pemex's announcement June 15 that it would lay off 1,000 permanent oil workers and 3,000 temporary workers due to decreased drilling and construction activity could mark the crack in the dam of Mexican employment. That the Mexican national oil company itself—the core of the four-year Mexican economic boom—has cut back its labor force points to the potential for *mass unemployment* on the scale of Chile in 1974, were Mexico's creditors to succeed in imposing their terms on the beleaguered country. These terms, which include a 40 percent reduction in imports, are a means to make the Wharton School prophecy of "Iranization" self-fulfilling.

A detailed analysis of Mexico's import position demonstrates that the massive import reduction demanded (supposedly in order to bring down the 1982 borrowing requirement from the range of $20 billion to about $14 billion) would devastate the Mexican economy.

First, Mexico faces revenue losses of at least $3 billion and additional debt service of at least $5 billion due to the external conditions imposed by the Federal Reserve's monetary policy, including collapsing raw-materials prices and enduring high interest rates. Secondly, the underlying structural flaws in Mexico's economic growth of the past four years, especially what Mexican political leader Marivilia Carrasco has called "the failure to transform the import-substitution economy," now represent a gigantic bomb, to be triggered by falling imports of so-called intermediate goods.

Import structure

So-called intermediate-goods imports constitute a full 57 percent of the total import bill as of 1981, and a full *three-fifths* of these imports, according to the breakdown provided by Mexico's central bank, are consumer-directed. Mexico's tariff structure, designed to protect national industries, contains one fatal loophole: it permits local industrialists to import foreign, mainly American, consumer goods in the form of parts, and assemble them with low technology and skill levels for sale as Mexican goods on the domestic market. Thus the "import-substitution economy" has generated a deep-going import dependence.

To a staggering extent, Mexico's oil revenues have purchased a flood of such "intermediate goods" rather than purchasing the capital equipment required to create the same industries locally.

In presenting a computer-based analysis of the Mexican economy projecting a possible 12 percent growth rate for the rest of the century, the Mexican Association for Fusion Energy (AMEF) and the Fusion Energy Foundation (FEF), which have worked with *EIR* on

Figure 1

Mexico's overall import dependence

	Import categories as percentage of total imports		
	1979	1980	1981
Consumer	9%	13%	12%
Intermediate	62%	61%	57%
Capital	29%	27%	31%
	Import categories in dollars (billions)		
Consumer	$1.102	$2.246	$2.773
Intermediate	$7.406	$11.206	$13.141
Capital	$3.577	$5.032	$7.190

The extraordinary dominance of "intermediate goods" in Mexico's foreign imports disguises a persistent dependence on consumer goods, since three-fifths of the intermediate goods categories are transformed into repackaged or assembled consumer goods, mainly for the domestic market.

analyses of the Mexican economy, warned in July 1981:

"These growth rates are not arbitrary, representing targets that would be 'nice' to achieve. They are variables that depend on detailed time-phase investment decision, estimates of when plant, equipment, and elements of infrastructure representing such investments will come on line, and how these will effect production and growth rates. They conform, on the other hand, to an absolutely essential structural requirement for the Mexican economy, without which large-scale social dislocations and the dreaded 'Iranization' of the country may in fact become consequences of insufficient development."

It is evident that the import boom of the last three years has run precisely contrary to the infrastructure- and capacity-building recommendations of the AMEF-FEF's proposed program. As Figure 1 makes clear, the Mexican economy, which began the 1970s as a semicolonial import-substitution economy, maintained precisely the same import structure through the oil-funded import boom of 1978-81.

Figure 1 shows that the proportion of capital-goods imports in the total bill did not rise, despite the doubling of the total import volume (from about $11 billion to $23 billion); it remained at about 30 percent of total. Since the largest portion of capital-goods imports went into petroleum investment, the fact that capital-goods imports doubled in absolute terms had even less effect on the internal Mexican economy than the figures might otherwise show.

Meanwhile, the proportion of consumer goods in total imports rose slightly, from 9 percent to 12 percent. But most important is the "intermediate-goods" category, which represented 62 percent of total imports in 1979 and still represented 57 percent in 1981 (the majority of the decline arising from higher consumer-goods imports rather than capital-goods imports).

The fact that three-fifths of the total import bill is listed as "intermediate goods" betrays an economy that functions as an assembly arm of other economies. Much of the "intermediate goods" imports are, in fact, improperly listed consumer goods. Food products repackaged in Mexico represent $1.9 billion of the total "intermediate" imports of $13 billion. Packaging materials represent nearly $1 billion, including half a billion dollars' worth of paper packaging materials.

An enormous amount of other intermediate-goods imports represent parts for assembly. Auto parts alone represent $1.1 billion of imports. Half of the $2 billion in steel imports in 1981 were made up of sheet and other steel products for stamping into consumer products. At least $800 million of the $1.4 billion in "chemical intermediate-goods" imports represent inputs for detergents, pharmaceuticals, soap, and other consumer products. Textile raw materials absorb about $200 million.

Figure 2

Mexico's industrial import dependence

(large establishments only)

Industry	Number of employed workers
Food processing	74,172
Soft drinks and beer	67,172
Cigarettes	5,525
Textiles	58,555
Woodworking	5,742
Paper	30,663
Tires	10,947
Chemicals	38,923
Pharmaceuticals	23,817
Consumer electronics	19,039
Industrial electronics	21,138
Auto assembly	51,992
Total	**587,149**
Subtotal of import-dependent industries	407,685
As percentage of total	**70 percent**

Altogether, the "intermediate goods" imported for repackaging or assembly, under the peculiarities of the Mexican tariff laws, comprise about three-fifths of the total goods listed as intermediate imports. That is to say that *fully half of all Mexican imports are consumer-goods imports* directly and indirectly. This does not count capital equipment imported for consumer goods industries, or authentic feedstock for consumer goods industries that do more than assemble or repackage imported materials.

Bottlenecks and inflation

By this breakdown, no more than 10 percent of the total Mexican import bill pays for contributions to basic industrial or infrastructural improvements. What was an import-substitution economy to begin with has been inflated into a gigantic import-substitution economy, and the immense development potential targeted by the López Portillo government during the past six years has been limited to a few, albeit important, showcase projects.

However, no fundamental progress has been made towards cracking the underlying development bottlenecks of the Mexican economy, namely energy, water, and transportation. In the latter case—the case of the disastrous Mexican road and railway system—neglect is especially apparent. Imports of railway equipment fell from $159 million in 1979 to $154 million in 1980 and only $85 million in 1981.

The irony in the "import-substitution" process is, as might be expected, that consumer-goods availability has been insufficient to meet the requirements generated by the capital-investment programs in oil and infrastructure. As I wrote last June 30, "Output as a whole has grown by about 8 percent per year during the past three years, while output of non-durable consumer goods has only grown by 5 percent on average. Meanwhile, agricultural output has risen by less than 3 percent a year over the same period. This contrasts with an increment of output during those three years of 47 percent in petroleum, 45 percent in chemicals, and 53 percent in capital goods (the latter from a very low starting point)."

Mexico's home-bred inflation in 1979-81 represented perhaps half of the total inflation rate (which was roughly 30 percent over the 1980-81 period). It is not due to high import prices, but to structural inefficiencies in the internal economy. As I reported a year ago, the "shortage of basic goods in real terms translates, in financial terms, into a net negative savings position of the banking system," and interest rates considerably higher than American rates. The inflation and interest-rate imbalance made Mexico vulnerable to pressure from abroad. As Mexican businesses built up more than $20 billion in outstanding debt to American banks, borrowing less expensive dollars rather than Mexican pesos, the effects of the Volcker policy in the United States were translated into monetary inflation in Mexico. With the two devaluations so far this year, the Mexican inflation rate is now at 60 percent and may well reach 100 percent. "Under a worst-case scenario," i.e., the events of the past year, "Mexican inflation could double by the end of 1982," I wrote on June 30, 1981.

The nasty underside of this import and inflation picture is the makeup of the Mexican private sector, now pulled into the spotlight by the bankruptcy of Mexico's largest private industrial group, the Alfa company. Mexican "entrepreneurs" typically expect an after-inflation rate of return of over 20 percent, higher than anywhere in the advanced sector. They obtain this through a de facto subsidy, that is, a tariff policy which prevents imports of some foreign consumer goods, but permits Mexican companies to assemble the same foreign consumer goods with cheap labor and inefficient methods. Although the protection policy itself is well-directed, its implementation has left a problem just as bad as direct import dependency.

Employment endangered

What happens now that the bankers propose to pull the plug? Figure 2 lists the employment (from a government survey of the 1,200 largest enterprises) of industries heavily dependent on "intermediate goods" imports which, as noted, constitute 70 percent of the labor force surveyed. Since these figures only take into account the largest enterprises, and smaller enterprises are more heavily weighted to assembly operations, the percentage figure is probably somewhat higher. In short, about 70 percent of the labor force works in industries which stand to lose the most output if imports are shut down.

If imports are cut by 40 percent, as the bankers demand (the government has pledged to cut them by 25 percent already), what will happen?

Assume that both consumer and capital-goods imports are cut in half, i.e., that the development effort comes to a grinding halt. That would account for no more than a 20 percent reduction in total imports. The rest would have to come from the intermediate-goods category.

But, as we have shown, the intermediate-goods imports translate into labor-intensive industrial employment in the home economy. To cut a further 20 percent of total imports, at least one-third of the total "intermediate" category would have to be shut down. Although it is impossible to forecast the effect with precision, the result of the reduction in availability of inputs for assembly and repackaging industries, combined with the spinoff effects of lost incomes, would be a *reduction of total Mexican industrial employment on the order of 30 to 40 percent.* Alfa announced June 14 layoffs of 10,500 workers, a quarter of its labor force; and Alfa is still not out of the woods.

Politically, such a reduction could occur through denial of import licenses by the Mexican government, or through forced bankruptcy of private firms, the cost of whose dollar debt service (of over $4 billion per year) has doubled, in peso terms, since the last devaluations, or a combination of both. The banks' (and the Federal Reserve's) crucial demand upon the Mexicans is to eliminate tariff protection, in other words, permit foreign goods to wipe out the local assembly industries at one blow. This is precisely the treatment that Chile received after the overthrow of the Allende government in 1973, with reductions of employment and incomes in that country in the order of 50 percent.

Mexico cannot survive such brutal economic treatment. The creditors' program is intolerable. No choice is open except to conduct a major transformation of economic policy under the most intense political fire, the same transformation which the Mexicans failed to make during the relatively calm days of 1979-81. As *EIR*'s founder Lyndon H. LaRouche, Jr. has suggested, Mexico could obtain the political leverage to do so by joining with Argentina and other Ibero-American nations in a common front for the renegotiation of their foreign debts. Although the Mexicans have shown no sign yet of adopting it, such a strategy would work. The alternative borders on national dissolution.