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TRANSNATIONAL CORPORATIONS, EXPORT-PROMOTION POLICIES, AND U.S.-MEXICAN AUTOMOTIVE TRADE

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ABSTRACT

Transnational Corporations, Export-Promotion Policies, and U.S.-Mexican Automotive Trade

Automobile manufacture began in Mexico in 1962, following the imposition of local content requirements. The industry was quickly dominated by subsidiaries of transnational corporations, although firms manufacturing parts were required to be majority Mexican-owned. In 1969, the thrust of policy was shifted from import substitution to export promotion, firms being obligated gradually to compensate imports of components with exports of automotive products. After disappointing results in 1974-75, this was reconsidered; but in June 1977 a new auto industry decree reaffirmed the export-promotion direction of policy, significantly increasing the exports required of all automobile firms.

This paper analyzes the setting of the agenda and the bargaining between the Mexican government and the transnational automobile firms (and their home-country governments) over this 1977 decree.

There was opposition from some of the firms, particularly Ford, and from the U.S. government. Although the firms objected to the volume of the exports, the short time in which they would have to be generated, and a requirement that 50 percent of these exports would have to be sourced from parts firms, they did not object to the basic thrust of the policy because they were engaged in major global reorganizations of their production networks, and Mexico could be accorded a share of the new investments with comparative ease. (An import-substituting policy might have interfered with these restructuring plans.) Ford objected more strenuously than the others largely because its plans for restructuring were less well-developed when the decree appeared. The objections of the U.S. government--it had been brought into the fray partly at the behest of U.S.-based firms and partly out of its own concerns--were deeper, drawing together the Departments of State, Treasury, and Commerce. The principal issues on this bargaining front involved allegations of discrimination against U.S.-based firms, performance requirements, and export subsidies.

The opposition of the firms collapsed when one of them, G.M., announced new investments to comply with the decree. Because of a long-established dynamic of follow-the-leader defensive investments, the other firms quickly followed suit. The collapse of opposition from the firms undermined the cross-departmental unity within the U.S. government. A sharply-worded diplomatic note was sent in February 1978, but there was no follow-up. Nevertheless, significant opposition from the United States to Mexican automotive policy remains a distinct possibility.

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Preface

A number of Latin American countries embarked upon economic growth through industrialization following the Great Depression and World War II in order to change, and hopefully to break, a pattern of dependency characterized by exports of primary products and imports of manufactured goods.[1] The terms of trade were biased against developing countries in this kind of exchange. Moreover, a development strategy organized around primary-product exports led to the creation and maintenance of export enclaves which contributed little to the development of other sectors and regions, and to a badly skewed pattern of income and significant life chances. Stagnation and continued underdevelopment were the nearly certain results.

The development of domestic manufacturing, it was hoped, would significantly change this pattern of dependency. It would mean economic growth that was less dependent upon volatile world market prices for agricultural and mining products. Domestic manufacture would create a national bourgeoisie less subservient to foreign interests. And wages paid to industrial workers would create an expanding domestic market that would mean a wider sharing of the fruits of development.

Industrialization as a deliberate policy was first pursued via import substitution. Imports were restricted and domestic manufacture encouraged in a succession of industries beginning with consumer nondurables and proceeding (as these opportunities were exhausted) through consumer durables and capital-goods industries. More recently, export-promotion strategies of industrialization have found favor in the region, increased manufacturing being sought through a reorientation of established industries toward wider foreign markets rather than through further, more costly, and inefficient doses of import-substitution policy.

This process of industrialization via import substitution and export-promotion has been accompanied by significant involvement of transnational manufacturing firms.[2] When tariff and quota barriers were erected to exclude imports of their manufactured goods, TNCs established manufacturing subsidiaries in these Latin American countries. When export-promoting strategies have been adopted, the TNCs' superior access to global markets has put them in a position to make or break such policies. Transnational firms have tended to displace or buy out smaller, domestically-owned firms in the same industry, to maintain R&D capabilities only in their home-country bases (thus slowing technological progress in Latin America), and to introduce products and production processes developed in more advanced countries and thus inappropriate to Latin America. Moreover, the penetration of TNCs into Latin America has been assisted by the foreign economic policies of their home-country governments. Thus, the process of industrialization in Latin America over the past quarter century has tended to replace one form of dependency with a new and different form of dependency in which transnational corporations play a central role.[3]

Under what conditions and to what extent can the state break or alter the terms of this new form of dependency? In the developing countries of Latin America, does the state have the will and the power to make transnational corporations alter the ways in which they do business? Can pressures from home-country governments be resisted?

This paper is part of a more extensive study of these questions that focuses upon the automobile industry in Mexico. When the process of import substitution had reached the "exhaustion" of the "easy stage" (consumer nondurable industries) toward the end of the 1950s, the Mexican government selected the automobile industry as a key sector around which to mount a new surge of industrialization. The long-reaching forward and backward linkages of the automobile industry into a diverse array of manufacturing and service sectors made it a prime candidate as a centerpiece of industrial growth. In 1962, the state promulgated a decree requiring that firms selling motor vehicles in Mexico had to manufacture a minimum of 60 percent of each vehicle (measured by cost of production) in Mexico. The major transnational auto firms were sufficiently eager to maintain a share in an important future market that 10 firms (eventually winnowed down to 7) commenced manufacture in Mexico (see Table 1). The fragmentation of the domestic market among so many firms insured that none of them could achieve production volumes that took advantage of existing scale economies in the industry.

In 1969, after an extended debate over whether to continue along this import-substituting route (by raising the level of mandatory local content), the government began implementing an export-promoting policy requiring the automobile firms to compensate a steadily rising percentage of their imports of parts with exports of automotive products (parts or finished vehicles). In 1974-75, this policy was dealt a setback when the auto firms (caught in a global recession) failed to achieve the required exports (see Table 2). After a serious reconsideration, the export-promoting policy was reconfirmed with a new auto industry decree promulgated in June 1977.

Our analysis of this course of events focuses upon two sorts of matters: (1) the character of dependency in and around the industry--its domination by subsidiaries of transnational firms, their responsiveness to the dynamics of the world auto oligopoly as much as to domestic conditions in Mexico, and foreign control of investment decisions, technology, products, and international trade opportunities--and (2) bargaining between the Mexican state and the transnational auto firms (often involving domestic parts-supply firms and the TNCs' home-country governments as well) over initiatives to change the character of this dependency. There have been three major episodes of bargaining: in 1961-62 (when import-substituting industrialization was first begun in the industry), in 1969

TABLE 1

THE MEXICAN AUTOMOBILE INDUSTRY (Terminal Firms)[a]

Firm	Ownership	Market Share 1970	1975	1980
Chrysler de Mexico	99% foreign 1% domestic	20.9	18.5	23.2
Diesel Nacional[b] (DINA)	100% domestic (Mex. govt.)	9.7	9.4	4.3
Ford Motor Co.	100% foreign	20.1	16.4	18.9
General Motors de Mexico	100% foreign	14.2	11.0	8.4
Nissan Mexicana	100% foreign	8.4	9.1	10.4
Renault de Mexico[b]	40% foreign 60% domestic (Mex. govt.)	NA	NA	4.7
Vehiculos Automotores Mexicanos	6% foreign 94% domestic (Mex. govt.)	7.1	6.8	6.0
Volkswagen de Mexico	100% foreign	19.2	28.4	23.8
Others		0.4	0.4	0.4
Total Production		185,031	341,419	456,372

[a]Cars and trucks less than 13,500 kgs.

[b]Renault de Mexico was created in 1978 by separating the automobile operations from the rest of Diesel Nacional. Diesel Nacional continues as a truck manufacturer.

SOURCE: AMIA.

TABLE 2

EXPORT PERFORMANCE OF THE MEXICAN AUTOMOBILE INDUSTRY, 1969-1976
(Millions of pesos)

Year	Imports of Assembly Material (A)	Net Exports of Auto Products (B)	A-B	$\frac{B}{A}$	Level of Mandatory Compensation
1969	1789.8	185.9	1603.9	10.4%	0
1970	1913.3	320.6	1592.7	16.8%	5%
1971	2095.1	449.4	1645.7	21.5%	15%
1972	2401.8	699.7	1702.1	29.1%	25%
1973	2899.2	1233.6	1665.6	42.6%	30%
1974	4109.5	1555.2	2554.3	37.8%	40%
1975	6157.2	1784.6	4372.6	29.0%	50%
1976	7426.5	3072.3	4354.2	41.4%	60%

SOURCE: Guillermo Salas V., "Política Industrial e Industria Automotriz en México, 1947-1979," (tesis: El Colegio de Mexico, 1980), cuadro 23.

(when the first turn toward export promotion was taken), and in 1977 (when the export-promotion route was reconfirmed). Our analysis here focuses upon this third episode of bargaining.

In each bargaining encounter we are interested in questions of (a) agenda setting, (b) decision making, and (c) implementation. With regard to agenda setting, we are concerned not simply with examining which issues became items of conflict but also which issues did not, because the actor who would have raised the issue was excluded from the bargaining, because one actor was sufficiently powerful to prevent the issue from being raised at all, or because the interests of the actors in the bargaining were so convergent that the issue never needed to be discussed. With regard to decision making, we are concerned not just with the actual power that was exercised but with the potential power of each actor and the reasons why such power might not have been used. With regard to implementation, we are concerned with unintended as well as intended consequences of policy, particularly with the formation of new structures of dependency. The discussion here of the 1977 bargaining will focus on agenda setting and decision making, touching only briefly on implementation in the conclusion.

We are concerned co-equally in the larger project with questions of dependency and of bargaining because "men make their own history, but they do not make it just as they please." Our approach is thus historical-structural, emphasizing "not just the structural conditioning of social life, but also the historical transformation of structures by conflict, social movements, and class struggles."[4]

Introduction

Less than seven months after it had taken office, the government of José López Portillo promulgated a new, comprehensive policy for the Mexican automobile industry.[5] The speed with which this was accomplished would not have been so surprising if the new decree had followed the general outlines of a draft decree that had been prepared in early 1976 by the Echeverría administration but which fell victim to the economic and political chaos of the last months of the Echeverría sexenio. The Echeverría draft decree would have returned government policy towards the industry to an import-substituting orientation after a five-year, less-than-successful attempt at an export-promoting route.[6] Already designated for ministerial appointments in the new administration, Carlos Tello and José Andres de Oteyza had lobbied successfully within the Echeverría administration to allow the new government to put out an auto industry policy that would be unmistakably its own. It was known that Tello and Oteyza dissented from some of the provisions of the draft decree, but when the Echeverría administration decided to shelve its plans to bring out its own auto industry policy, there was little expectation that the decree which the López Portillo administration promulgated in June 1977 would be wholly different in character. Instead of returning to import substitution, the new decree pressed forward vigorously with export promotion.

The new decree showed a technical sophistication that far outstripped the earlier auto industry decrees of 1962 and 1972. It had clearly been prepared with the aid of econometric models, and was replete with complex algebraic formulas. Its principal provisions were the following: (1) The terminal firms would have to move steadily over the next five years towards a position where their operations generated no balance-of-payments deficit. Not only would the terminal firms have to compensate with exports their imports of parts for vehicles assembled in Mexico (as the 1969 policy had required), they would also have to compensate for their other foreign payments (for freight and insurance, technical assistance, repair parts for their dealers, etc.) and for the imported content of the parts they procured domestically. (2) The burden was placed squarely on the transnational auto firms in the terminal industry to generate these exports, but half would have to be sourced from firms in the supplier industry (by law, all firms in the auto parts industry are required to have a minimum of 60 percent Mexican ownership). (3) Some special consideration would be given to the two remaining majority Mexican-owned firms in the terminal industry, in recognition of their greater difficulty in finding export opportunities. (4) While the new decree was strongly export-oriented in character, import substitution was not wholly abandoned. Terminal firms would have to maintain a minimum level of local content slightly higher than previous policies had required. (5) The regulatory apparatus was changed substantially: price controls were eliminated, and in other ways there would be more reliance on market constraints rather than on direct proscriptions of behavior.

While the Echeverría administration had conducted extensive discussions with both the terminal and the supplier industries before preparing the 1976 draft decree, the decree of June 1977 was promulgated with scarcely any discussions between the new administration and the industry. Both before and after a set of "Rules for the Implementation of the Decree" was published on October 18, 1977, there were attempts by some of the terminal firms, led particularly by Ford, to modify the terms of the new policy. The major concern was not with the overall export orientation of the new policy. Instead, the complaints were about how quickly the firms would have to move toward full compensation of their foreign payments, about having to shoulder the burden of compensating for the imports of their domestic suppliers, and about what they considered the discriminatory treatment of foreign-owned firms. The U.S. government joined in the opposition, objecting to the discriminatory treatment of U.S. investment, the use of performance requirements to generate exports, and alleging the employment of export subsidies. A sharply worded "Diplomatic Note" was sent in February 1978 (see Appendix). In the bargaining that preceded the 1962 decree which established auto manufacturing in Mexico, the Mexican government had conceded on several major points to the opposition from transnational automobile firms and their home-country governments.[7] In this episode of bargaining, however, the Mexican government stood firm behind its new policy.

Our examination of these events focuses first (agenda setting) on why there was conflict between the transnational auto firms and the Mexican government on some issues but not over the basic thrust of export-promotion policy, why Ford led the opposition, and why the U.S. government became involved over the issues that it did; and second (decision making) on how and why the Mexican government stood firm against this opposition, why Ford toned down its objections, and why the Mexican auto policy has persisted as a topic of bargaining between the Mexican and the U.S. governments.

Agenda Setting

Because the government took the industry so much by surprise, one might be tempted to assert that the bargaining agenda was set simply and fully by the government--that it established what issues would be items of concern. For a number of reasons, however, this would be a misleading view. First, there were what one official termed "los vicios de origen," (roughly, the vices of the origination). Auto manufacturing had begun 15 years before in Mexico. Some characteristics of the industry were now deemed as given, as insusceptible to change. Most importantly, there were seven firms in the terminal industry, and while it was acknowledged that greater efficiency could be achieved with fewer firms, the domestic and international costs of forcing some of these firms out of Mexico were now considered too great. Rationalization of the industry had been on the agenda in the 1962 bargaining and again in the 1969 bargaining, but now it could no longer be seriously considered.

Secondly, as in 1962 and 1969, some actors were excluded altogether from the bargaining, and thus the issues of particular concern to them were unlikely to be brought forward. In this bargaining, the domestically-owned supplier industry played a more prominent role than it had previously;

it had begun to come of age. Representatives of labor in the industry were not involved in the bargaining at any stage, however. As in the past, labor was an excluded actor.

Finally, the items that came to be bargained over were only those issues on which there was a conflict between the interests of the firms and the interests of the state. Some issues never appeared on the bargaining agenda because there was a convergence of interest between the firms (particularly the transnational terminal firms) and the government. In 1962, one such basic convergence of interests had set the industry along the road of import-substitution industrialization. Now the distinct experiences of the state and of the transnational auto firms over the previous years led to quite a different convergence of interests in a more export-promoting direction. But in order to see which issues became items of contention and which did not--to see how the bargaining agenda was formed--we have to review the interests of each of the major actors.

The interests of the firms. The interests of the terminal firms were significantly altered from what they had been in 1962 or even in 1969. The restructuring of the world industry during the 1970s had transformed the strategies of the TNCs and the place of their Mexican operations within their global networks. In general, export requirements were much more congenial to the firms than they had been in the past. In 1969, Ford had agreed to mandatory exports to halt the possibility that Fabricas Automex (the Chrysler subsidiary, then domestically owned) might succeed in consolidating half of the industry in a single Mexican-owned firm. By the logic of defensive investment, the other foreign-owned terminal firms had been compelled to agree as well or face exclusion from the Mexican market. But in 1969 the transnational auto firms were not in a position to reorganize their global operations to accord a significant place for Mexican parts exports. In 1977, impelled by the impending stagnation of demand in the industrialized countries, the rapidly rising price of petroleum, and a host of new, intrusive government policies in developed and developing countries, most of the major world auto producers were in the midst of, or about to embark on, significant reorganizations of their global production networks. Volkswagen and Renault were looking to set up manufacturing operations in the United States, while Ford, Chrysler, and G.M. were having to "downsize" their entire lines to meet consumer demand for energy-efficient vehicles and to satisfy government-mandated fuel efficiency standards. All of the firms were seeking to incorporate new automated production technology and to find other ways of cutting production costs--including manufacturing parts in lower-wage sites such as Mexico. In this conjuncture, the TNCs were compelled to make substantial investments in their global operations; it was only a question of where. Unlike 1969 when the firms were required to make investments in Mexico simply to maintain their share of the domestic market, in 1977 it was more a question of asking the firms to divert some of their new investments to Mexico.

Only DINA and VAM were not so inclined to favor the export-promotion route. Because they were the two remaining Mexican-owned firms, they lacked significant export opportunities. World automotive trade was dominated by the dozen or so major transnational auto firms, and it was doubtful that these TNCs would accord a significant place in their global sourcing networks to a subsidiary they did not completely control. When the new decree appeared, the five wholly foreign-owned firms (Ford, G.M., Chrysler, Nissan, Volkswagen) were pleased that it stayed with the export-promotion route rather than returning the industry policy to import substitution as the 1976 draft decree had threatened, because it accorded them better opportunities to adjust to the restructuring of the world industry.

If the restructuring of the world industry inclined the firms to a generally favorable disposition toward the new export requirements, there were also significant differences among their strategies in the face of the restructuring which affected how they would react to the new decree. The Japanese firms (having helped precipitate the need for the restructuring) could continue with their strategies of producing at home for export, though they did begin to explore possibilities of foreign investment in the United States and Europe. For the most part, Nissan would have to look to export parts for expanded new car production in Japan or for the spare parts market in the United States (in early 1980 Nissan announced plans to open a small-truck assembly plant in Tennessee). The burden of adjustment fell most strongly on the U.S.- and European-based firms. The European-based firms particularly looked to co-production agreements (to share capital costs and to move more quickly to introduce new technology) and to the establishment of manufacturing operations in the United States to protect and expand their share of this largest market. The U.S.-based firms concentrated on downsizing their models for the U.S. market and on rationalizing their global production through coordinated world-wide sourcing of parts. Both strategies provided opportunities for increased parts exports from Mexico.

Even among firms following roughly similar adjustment strategies, there were important differences of timing. Volkswagen had already located the site for its U.S. plant in New Stanton, Pennsylvania 10 months before the new decree appeared, while Renault was still involved in protracted negotiations with American Motors. Volkswagen could move more quickly to plan which parts it would manufacture in Mexico for export to the New Stanton plant. By June 1977, General Motors had made a decision to downsize its entire line, and had begun planning the necessary investments.[8] The promulgation of the decree in Mexico merely gave G.M. extra reason to consider Mexico as a site for some of these new facilities. Ford, on the other hand, had not yet committed itself to such a large-scale investment program. It could not begin thinking about which parts to source from Mexico until it decided how it would adjust to the restructuring of the world auto industry. Finally, Chrysler was just beginning to feel the bind of its escalating financial troubles, although of the "big three," it had the most substantial set of export projects already in place in Mexico.

Thus, before the June 1977 decree was promulgated, the major transnational auto firms with subsidiaries in Mexico were already exploring new global investment programs which might accord their Mexican operations a more substantial role. A government policy promoting exports from the industry was far more consistent with these investment programs than an import-substitution policy. Nevertheless, because some of the firms were more advanced in this planning of their global reorganization, there would be differences in how they reacted to the Mexican auto decree when it was issued in June 1977.

The firms in the parts industry were much more divided than the terminal firms on the question of export promotion vs. import substitution. An export orientation accorded well (as it had in the past) with the interests of those larger firms that were joint ventures between Mexican capital and transnational parts firms (Tremec, Spicer, Eaton, etc.). These firms had quickly come to dominate parts exports from Mexico after the 1969 export Acuerdo,[9] and higher export requirements (and the higher percentage that would have to be sourced from independent parts firms) would mean further expanded sales. For them, export promotion meant guaranteed access to the world auto market. Higher local content requirements would not help these firms at all since their components were already being incorporated by essentially all of the terminal firms in Mexico.

The smaller parts firms, far more numerous and for the most part wholly domestically-owned, were more inclined to favor a return to an import-substituting orientation. Lacking the international market access of a transnational joint-venture partner, they had much less chance of finding export opportunities. Many of these smaller firms made components that were domestically sourced by only one or two of the terminal firms, the others continuing to import. Higher local content would provide these smaller firms with expanded sales opportunities.

In the bargaining that preceded the formulation of the 1976 draft decree, the parts industry as a whole had worked out a compromise position which provided for a measure of higher export requirements and a measure of higher mandatory local content--a piece of the pie for both segments of the industry. This position was presented again in March 1977 to Ernesto Marcos, the new Director of Industries in SEPAFIN. Marcos had hinted at that meeting that the decree then being prepared would be strongly export-oriented in character. Thus, while the smaller parts firms were disappointed with the decree when it appeared in June, they were relieved to find that it did provide for some increase in the level of mandatory local content.

The interests of the government. One of López Portillo's first steps after taking office on December 1, 1976 was to effect a significant reorganization of the ministries charged with planning and managing economic growth. The Ministry of the Presidency was reorganized, strengthened, and renamed to reflect its actual functions: Programming and Budgeting. The Ministry of Industry and Commerce was divided in two. There would now be a separate Ministry of Commerce, and the other half of this original ministry was joined to the existing Ministry of National Properties to create the Ministry of National Properties and Industrial Growth (SEPAFIN). By these moves better coordination of auto industry policy was made possible. No longer would the direction of policy in the industry be the responsibility of one ministry, with nominal control over the state-owned firms in the industry (DINA, VAM, and about ten parts manufacturing firms) the responsibility of another.[10] The Ministry of National Properties and Industrial Growth would now control all of the significant instruments of policy toward the industry except for tax rebates, subsidies, and other fiscal stimuli, which remained lodged in the hands of the Ministry of

Finance and Public Credit. When the auto decree was promulgated, it provided for an Inter-Ministerial Commission of the Automotive Industry to include two representatives each from the Ministries of National Properties and Industrial Development, Commerce, and Finance and Public Credit.

López Portillo appointed José Andres de Oteyza as Minister of SEPAFIN. Natan Warman was named Deputy Minister for Industrial Growth, Ernesto Marcos became Director of the General Bureau of Industrial Development, and Juan Wolffer became Sub-Director for the Automobile Industry in SEPAFIN. Other key ministerial positions went to Carlos Tello (Programming and Budgeting), Julio Rodolfo Moctezuma Cid (Finance), and Fernando Solana (Commerce).

This reorganization did promise better coordination of government policy, but it was not founded upon any significant change in the goals or the strategies of policy. The central goals remained very much as they had been in 1962: stimulation of industrial growth, creation of employment opportunities, development of domestic technological capability, and improvement in the balance of payments. How best to serve these goals remained basically a question of whether to orient the industry principally towards the domestic market (an import-substituting route) or to face the industry outward, towards the international market (an export-promoting route). The new team responsible for industrial policy rejected the analysis of the Echeverría administration (based on the disappointing export results of 1974-75) and elected to stick with the export-promoting orientation that had first been adopted in 1969. Their reasoning was that industrial growth--in general, not just in the automobile industry--was constricted by a small domestic market and by increasingly severe balance-of-payments problems. Only 15 percent of imports of manufactured goods were covered by exports of manufactured goods; the rest were paid for by exports of agricultural and mining products. While a higher local content requirement in the automobile industry could decrease the sector's drain on the balance of payments (it accounted for over 10 percent of the deficit on current account in 1975), the industry would have to continue to import production equipment and some raw materials. Import substitution could not promise a complete solution to the industry's balance-of-payments problems.

Even more important than their potential contribution to the balance of payments, manufactured goods were seen by Oteyza, Warman, and their subordinates in SEPAFIN as crucial to stimulating industrial growth. The Mexican automobile market was still small by international standards (about 300,000 vehicles in 1976), and fragmented among a large number of manufacturers. In the current situation, it was impossible to take advantage of available economies of scale that could increase efficiency and productivity, lower costs, and allow the industry to serve as an engine of wider industrial growth. An outward turn would eliminate this constraint on the domestic market: export production would allow greater efficiency and expanded sales volumes as well as earn foreign exchange.[11]

There were, it should be noted, other ways that more efficient production could be achieved without ceasing to focus on the domestic market. A reduction in the number of firms in the industry from seven to three would allow each remaining manufacturer to produce more efficiently.

But 15 years after the first decree initiating automobile manufacture in Mexico, this was no longer considered a viable option. The domestic and international ramifications of eliminating well-established firms from the Mexican market were considered too great. The number of firms was simply one of the vicios de origen. Alternatively, greater efficiency in production could be achieved by more stringently limiting the number of models each manufacturer could produce and by requiring that each model be produced for a longer period. Together these steps would have extended production runs, but they also would have isolated Mexico from international changes in technology and made exports not just difficult but impossible (since Mexican-made vehicles and components would no longer conform to current specifications elsewhere).

Export promotion seemed the far better strategy to the new administration, but they realized it would depend for its success on the willingness of the major transnational auto firms to purchase parts from Mexico. Mexico was far more likely to be price competitive in the manufacture of specific components than of finished vehicles. Competitive price and quality would not be sufficient, however, to win Mexico a significant share of world trade in auto parts, because there is no open, competitive market in these products: there is only one buyer of Rabbit doors and only one of LTD fenders.[12] SEPAFIN officials were aware that the auto TNCs were embarking on huge investment programs. The moment seemed right for Mexico to make its bid for a share of the investments for the worldwide sourcing of parts.

The first drafts of the June 1977 decree were even more resolutely export-promoting in orientation than the final version. The report that Ford (still the leading voice in the Mexican industry) had submitted to the Echeverría administration in May 1976 presented one persuasive, carefully supported case for a full-blown export route.[13] Moreover, Warman, Marcos, and Wolffer were, at first, quite taken with the U.S.-Canadian Automotive Products Trade Agreement of 1965 (APTA). Under this agreement, Canada has had only a small balance-of-payments deficit in automotive trade with the United States (if any at all). Perhaps Mexico could achieve the same position under a vigorous export-promotion policy. Two factors seem to have been responsible for restoring a measure of import-substitution logic to the final decree. One was the lobbying of the parts firms, who argued that any relaxation of local content requirements would lead to the destruction of the smaller parts firms. The terminal firms (they argued) would import nearly all the parts of their vehicles, compensating for these imports with massive exports of a few parts manufactured by themselves or by the largest parts firms, the ones that already dominated parts exports. This line of reasoning was supported by a more careful examination of the APTA. Before the APTA was signed, Canada had an integrated auto industry of its own. The plants were owned by the major U.S. makers, but substantially all of the principal components of a vehicle were manufactured in Canada. Canada even had its own makes and models. In the ensuing dozen years, however, the Canadian plants have been more fully integrated into the U.S. auto industry. To a large extent it has ceased to make sense to speak of a Canadian automobile industry--or at least that was the perception of the officials formulating the new Mexican auto policy. The prospect of a similar fate for the Mexican auto industry bespoke an unacceptable dependency on the United States.

Consequently, the final decree retained a substantial local content requirement. In several ways this new local content requirement differed from the one that had been in force during the first 15 years of Mexican auto manufacture. Local content would be calculated in a new way, on a cost-of-parts rather than a cost-of-production basis.[14] The mandatory level of minimum local content would now be 50 percent (for cars, 65 percent for trucks), but because of the new basis of computation, the new level of required local content was about 8 percent higher than before. (This increase, it was expected, could be fulfilled simply by taking advantage of excess capacity of the supplier firms.) Local content would now be measured on a per-model not a per-plant basis. Firms would no longer be able to average higher local content on one model against lower local content on another. A reduction in the number of models was the expected result. Finally, in addition to the required minimum level of local content there would be a recommended level of local content which would rise to 75 percent by 1981. Firms could choose not to fulfill this higher recommended level, but as an incentive to increase their local content, they would have to compensate the difference in imports by more than 1:1.

Notwithstanding these local content provisions designed to maintain a broad spectrum of auto manufacturing operations in Mexico, the primary thrust of the new decree was to require the transnational auto firms to undertake significantly increased exports from Mexico. While complex formulae determined the precise export volume each firm would have to generate, these rested upon a few straightforward principles. By 1982, each terminal firm would have to fully compensate its imports with exports, and in the intervening years the firms would have to make steady, prescribed progress toward this goal. Under the 1969 export policy, the firms were obligated to compensate only their imports of assembly parts. Under the new policy, the firms would have to compensate for all their foreign payments: for production equipment, for replacement parts for their distributors, for technology payments, even for the imported content of the parts they obtained from supplier firms. When and if the terminal firms fulfilled these export requirements, one of the industry's primary goals would have been achieved: to make the industry "a source of net foreign-exchange generation in the medium term."

Several provisions of the 1977 decree were designed to protect and to strengthen Mexican ownership in the industry. Fifty percent of the exports of each terminal firm (up from 40 percent in the 1969 policy) would have to be sourced from supplier firms (by law majority Mexican-owned). A "fudge factor" was introduced into the export-promotion formulae to decrease somewhat the exports that would be required of DINA and VAM. (In addition, the provision concerning the recommended level of local content gave these two firms an alternative way to fulfill the terms of the decree.) Finally, certain activities were reserved for majority Mexican-owned firms, most significantly the manufacture of diesel trucks.

The 1977 decree also embodied a substantial overhauling of the government's regulatory apparatus with regard to the industry. Price controls and production quotas (maxima)--both in place since 1962--were eliminated, the latter being replaced by a foreign-exchange budget for each firm. Firms in both ends of the industry would continue to be eligible for a complex array of tax rebates, subsidies, and other fiscal stimuli; but if a terminal firm should fail to meet its export obligations, it would be punished by fines and forfeiture of these fiscal benefits rather than by reduction of its production quota (the penalty under the 1969 policy, one that had proved difficult to apply). Except on some parts of obligatory domestic manufacture (essentially the power train), import licenses would be replaced by tariffs, and these gradually lowered to encourage greater efficiency on the part of Mexican manufacturers. Broadly speaking, the new regimen sought to utilize more general rules (rather than ad hoc bargaining with each of the firms) and to utilize the constraints of the market (albeit a carefully structured one) rather than direct proscriptions to regulate the industry.

Setting the bargaining agenda. A few days before the decree itself was promulgated, the government announced the lifting of price controls, a steady source of complaints from the terminal firms. As a consequence, the first reaction of the industry to the new policy was almost uniformly favorable.[15] But shortly, complaints began to emanate from the firms in the terminal industry, particularly from Ford.[16] Even after a second look, the supplier firms seemed satisfied. A variety of issues were raised in the ensuing bargaining among the firms, their trade associations, and the government, but four issues emerged as particularly important:

(1) Degree of compensation. The terminal firms argued that the levels of exports required of them were too high, particularly the obligation to compensate for the imported content of parts they obtained from domestic suppliers. "That's carrying the joke too far," one executive said.

(2) Timing. The terminal firms complained that the new policy required them to generate exports too quickly. Increased exports would require new investments, they argued, and these would require several years to plan and bring to fruition.

(3) Sourcing. Finally concerning the export provisions, the terminal firms complained about being required to source half from independent, majority Mexican-owned parts firms over whom they had no control.

(4) Discrimination against foreign-owned firms. A number of provisions in the new decree seemed to favor the Mexican-owned firms in the industry. DINA and VAM would have lighter export burdens. Certain segments were reserved for Mexican-owned firms; Ford was particularly upset at the provision allowing only Mexican-owned firms to install diesel engines in trucks.

These were the four major issues on the bargaining agenda between the firms and the government during the months that followed the promulgation of the decree. Because of the way the government had prepared the decree, there had been no bargaining before its appearance, but there were serious discussions after June 20 and even after the publication of the clarifying and implementing Reglamentos on October 18.[17] Why were these four issues the major items of contention between the firms and the government? Why were other issues not on the bargaining agenda? And why were these issues of more concern to some of the firms than to others?

Some issues were not raised because they were issues of too substantial conflict between the firms and the government: these were issues which the government knew would be so strenuously opposed by the firms that it made no attempt to include them in the decree. Most important among these were the number of firms in the terminal industry and their foreign ownership. Both of these issues had been on the bargaining agenda in 1962 and 1969. In neither episode had the government been able to limit the number of firms to what efficiency considerations dictated or to insist upon majority Mexican ownership for firms in the terminal industry. Now with the terminal firms deeply entrenched in Mexico, these two issues were considered vicios de origen. These were issues too costly to raise because of the domestic and international opposition they would arouse. Neither was raised in the decree, and thus neither became a subject of bargaining. They were givens to be taken account of in formulating other provisions.[18]

Other issues were not raised because of a fundamental convergence of interests between the terminal firms and the government. These issues were not in the bargaining agenda because of a basic agreement between the two sides.

Nothing in the decree challenged a fundamental assumption of the Mexican growth strategy over the past half century: primary reliance on private-sector investment and state responsibility for maintaining conditions for capital accumulation.[19] The new decree sought, in effect, to induce substantial private-sector investments both by foreign and domestically-owned firms. If the state was obtrusive in directing the general character of these investments, it also offered a variety of fiscal stimuli (as well as the lifting of price controls) to ensure a profitable return. A central item in this basic convergence of interest among the state, the TNCs, and the national bourgeoisie was the situation of labor. Not only was labor excluded from the bargaining (as it had been in the past), the decree came just six months after López Portillo had announced, as part of his "Alliance for Production," an agreement from labor leaders to hold wage demands to 10 percent, well below the prevailing rate of inflation.[20]

Beyond this, there was a basic convergence of interests between the transnational auto firms and the government concerning the export-orienting thrust of the new decree. The firms might complain about the volume, the timing, and the sourcing of the required exports, but these were objections to the manner in which export promotion was to be carried through, not objections to the overall thrust of policy. The firms might have preferred no new policy at all, but given that the government saw a need to do something in the industry to promote industrial growth and to reduce the industry's drain on the balance of payments, an export orientation was far more preferable than an import-substituting one. All of the firms were engaged in reorganization and rationalization of their global operations. An export-promoting orientation gave them far more latitude than an import-substituting one to integrate their Mexican subsidiaries into the global sourcing networks they were establishing. It is not an exaggeration to say that the new decree compelled the firms to follow a route they were already travelling.[21] Conceivably the government might have seen the choice between import substitution and export promotion somewhat differently if either a reduction in the number of firms (rationalizing the domestic market) or a return to domestic ownership in the terminal industry had been possible. But export promotion was perceived as the clearly rational strategy once these were accepted as given. Efficient production could be achieved with so many firms only through production for the international market, and foreign ownership of the terminal firms provided the necessary access to that international market. In the particular context in which both sides found themselves, export promotion was the preferred policy.

Because of this basic convergence of interest, the export-promoting thrust of the new decree was never a topic of bargaining between the firms and the Mexican government. The issues that were raised were more minor--which is not to say that they were unimportant to the firms that raised them. The main issues that were raised were of concern to all of the transnational firms. The extent, the timing, and the sourcing of the required exports did obligate the firms to commit themselves to substantial exports and substantial investments in Mexico in a very short time span. Compliance with the new policy would mean some diminution of managerial flexibility in siting component production around the world. Whatever fairness there might be in Mexico's requirement of 1:1 export compensation, extending this to oblige compensation of the imports of the parts firms as well seemed too much. The firms would have to more than double their exports by 1982; and half of these would have to be procured from parts firms.

Each of the terminal firms did have its own particular problems with regard to these issues. Renault and American Motors (being only minority partners in joint ventures) would be reluctant to absorb substantial imports from DINA and VAM. Lacking manufacturing facilities outside Japan, Nissan would face high transportation costs for its parts exports. Having achieved an unusually high degree of vertical integration, Volkswagen would have particular difficulty in satisfying the requirement that 50 percent of its exports come from parts firms. Chrysler faced the prospect of losing its diesel truck line (it had been granted the right to install diesel engines in trucks before it was denationalized in 1970-71, and it was currently the only foreign-owned firm to be engaged in this).

Why, then, was it Ford that was most vocal in opposition? Ford's traditional leadership position in the Mexican industry is one possible explanation--it is the one offered by Ford executives themselves. Ford had taken the lead in the bargaining leading to the 1962 decree, and it was Ford that made the offer which led to the 1969 export Acuerdo. Why shouldn't Ford again take the lead in 1977? There are short-run situational factors that might play a role in explanation as well: Ford felt that the future in trucks lay in diesels. Its management had been engaged in extended negotiations to win approval for Ford to manufacture diesel trucks in Mexico. They had just turned down one offer from the government as requiring too many concessions. But the new decree foreclosed the possibility together.

There is a deeper, more structural explanation, however, one rooted in Ford's predicament in 1977 in adjusting to the changes in the world auto industry. G.M. had made a corporate commitment to downsize its entire U.S. line more than a year before the Mexican decree appeared. By June 1977, its planning for new models and production facilities was sufficiently advanced that it could immediately begin programming which components it might source from Mexico. Ford was in a more precarious position, however. It had opted for a slower, wait-and-see attitude toward downsizing.[22] When the June 1977 decree appeared with its obligations to make large investments and export commitments, Ford had a much less clear basis for planning quickly what Mexican-made parts would best fit into its global sourcing network (see Chronology). Ford was in no position to enter into discussions with parts firms, and the volume and the timing of the exports required pressed Ford very hard. Ford had been a dominant firm in Mexico from before the 1962 decree. In the mid-1970s, it found itself in difficult straits in the U.S. market because of the Japanese challenge and G.M.'s quicker response in downsizing. The Mexican auto decree threatened Ford in a market it had counted on as a source of strength at a time it could scarcely stand another threat.

Bargaining

The bargaining that took place over the 1977 decree followed rather than preceded its promulgation, and took place along two fronts. First, there were discussions between the Mexican government and the transnational auto firms in which the firms sought to soften the terms of the decree, to slow or postpone its implementation, or to win approval for certain exceptions to its terms. Second, there were bilateral discussions between the Mexican government and the U.S. government both because some of the U.S.-based transnational firms sought the assistance of their home-country government and because the U.S. government found that the Mexican auto decree challenged certain tenets of its foreign economic policy. These discussions focused on more fundamental issues in the decree, the U.S. government seeking basic changes in the new policy or, at the very least, a commitment from the Mexican government that similar policies would not be enacted in other industrial sectors.

The first front: the terminal firms vs. the Mexican government. Having avoided discussions with the terminal firms over the shape of the new policy before it was promulgated, there were extensive discussions with all of the firms after June 20, 1977. The Asociación Mexicana de la Industria Automotriz (AMIA, the terminal firms' trade association) held a series of urgent meetings. There were joint meetings between AMIA and government officials, between corporate officials and government officials, and between Mexican managers and their home offices. Several CEOs flew to Mexico for high-level talks including discussions with López Portillo himself.

To some extent these meetings sought clarification: a number of key items were not spelled out in the decree, awaiting the more detailed set of Reglamentos that eventually appeared in October. To some extent these meetings sought to influence the content of the Reglamentos. There were attempts to win exceptions of various sorts: Volkswagen, for example, is reported to have offered a much higher level of export compensation in return for permission to manufacture all of its exports itself rather than sourcing 50 percent from parts suppliers. Finally, there were attempts to soften or slow implementation of the decree. In various ways the firms

CHRONOLOGY

Year	Events Outside Mexico	Events Inside Mexico
1976		Jan.: G.M. de Mexico becomes part of North American Assembly Div.
	mid: G.M. reaches downsizing decision	
	Sept.: Volkswagen selects New Stanton, Pa. for plant	Dec.: José López Portillo takes office
1977		May : Bilateral Consultative Mechanism established
**********	**********************************	June: AUTO DECREE***********
		Oct.: Reglamentos
		Nov.: Bilateral Consultative Mechanism meeting
	fall: Chrysler earnings-slump begins	Nov.: G.M. announces expansion of Ciudad Juarez maquiladora
1978		Feb.: U.S. sends "Diplomatic Note"
		Feb.: G.M. announces 4 new plants
		Mar.: Ford and Volkswagen announce expansion plans
		July: Renault buys 40% equity in DINA
	Aug.: Peugeot buys Chrysler's European subsidiaries	
1979	Jan.: AMC and Renault sign U.S. licensing and sales pact	
		Feb.: Ford signs agreement with Grupo Alfa for joint venture
	Aug.: Chrysler asks federal loan guarantees 1980	
	Oct.: AMC and Renault sign U.S. coproduction agreement	
1980		
	July: Nissan announces U.S. small truck plant	

sought to convince the Mexican government that the terms were excessive: that they called for too much investment or that they called for it too fast or that they allowed the terminal firms too little control over how they complied.

In all these discussions Ford led the opposition. "G.M. and Chrysler stood in back of Ford," one industry executive said, "which is not to be confused with backing Ford." The tenor of the opposition was set in a visit of Henry Ford to Mexico just a few days after the decree appeared. Ford had a half-hour meeting with López Portillo late one afternoon that touched on a number of concerns--how inflationary the new decree would be, how short the deadlines were, etc.--and finally mentioned the issue of discrimination in excluding foreign-owned firms from installing diesel engines. According to one account of the meeting, López Portillo said there was no discrimination on this issue, that Mexico needed diesel trucks and that Ford could install them if it wanted. (According to another account of the meeting, Ford simply misunderstood López Portillo, who told him that there was no discrimination because Ford had only to Mexicanize to be able to install diesels.) That evening there was a dinner at the home of Fernando Solana (Minister of Commerce) attended by Ford, Oteyza (Minister of SEPAFIN), and other officials responsible for automotive policy (none of whom had been present at the Ford-López Portillo meeting). At this dinner Ford casually mentioned that López Portillo had given the firm permission on diesels. That can't be, Oteyza remonstrated. The decree is very clear about that and it bears the President's signature. Ford was urged by his staff to proceed quietly on the issue by writing a letter to the president reminding him of their conversation and asking him about what Oteyza had said. But at a press conference just before leaving Mexico, Ford was asked what he thought of the new decree, and he launched into a public tirade against the decree's discriminatory features. The gauntlet had been thrown down.

No doubt the issue of diesel trucks was important to Ford, but other issues weighed at least as heavily: the volume of the exports that would be required, the short time period in which to generate them, and the necessity of sourcing half of them from domestic supplier firms. Ford's strategy was to seek a softening of the new policy in the Reglamentos, but it stood to succeed in this only if none of the other transnational firms announced plans for new investments to begin complying with the decree. Ford threatened, more than once, to pull out of Mexico if the decree were not changed, but both sides understood this to be posturing. Ford alone could not force a change; concerted action was the key to winning concessions. So long as the transnational terminal firms showed a unified front, the government would be under pressure to modify the decree, but as soon as one of them "broke the circle" the government could play them off against each other, threatening those refusing compliance with exclusion from the Mexican market. The new policy was troublesome for the other terminal firms, but they preferred to keep a low profile. Nor could Ford find other allies inside Mexico: there seemed to be no opposition to the decree within the government (ministries could not be played off against one another); and because the parts firms were on the whole quite pleased with the new policy, it could not be painted as anti-business to mobilize more general private-sector opposition. Ford quickly found an ally, however: the U.S. government.

The second front: the U.S. government vs. the Mexican government. The U.S. government was brought into the fray along several routes. Ford (and perhaps the other U.S. firms) discussed the decree with the Motor Vehicle Manufacturers Association (MVMA) and the "big three's" lobbying arm in the United States, which in turn raised the various issues with the Departments of Commerce, State, and Treasury. Henry Ford himself contacted Secretary of State Cyrus Vance and U.S. Ambassador to Mexico Patrick Lucy. There were discussions of the decree at meetings of the Export Promotion Committee of the American Chamber of Commerce of Mexico attended by the managers of the U.S.-based terminal firms and by officials from the Economic and Commercial Section of the U.S. Embassy.[23] Reports of these meetings were sent to the Departments of State and Commerce.

The timing and the character of the U.S. government response was certainly influenced by these direct and indirect approaches of the firms seeking to draw the U.S. government into the bargaining, but it is important to recognize that the U.S. government had concerns of its own, independent of the TNCs, which might have drawn it into the conflict even if all the firms had decided they could live with the policy. It appears that officials of the Commerce Department took some initiative in contacting the U.S.-based firms to learn their positions on the decree shortly after it was promulgated. Though championed by different agencies and departments, three kinds of issues found concern within the U.S. government: trade issues involving "performance requirements" and export subsidies, investment issues concerning discrimination against U.S. firms abroad, and labor issues.

(a) Trade: performance requirements and export subsidies. An important backdrop for the trade question was the context of the U.S. balance of payments in the late 1970s. Because of the rising price of oil, increased world competition in manufactured goods, and declining productivity in the United States, a U.S. balance-of-trade surplus of $9 billion in 1975 had turned into a disturbing cumulative deficit of $75 billion over the next three years.[24] While trade with Mexico was hardly the cause of this deficit, the new auto policy did seem to portend a new, worrisome current in world trade: the use of government export subsidies and industry-specific performance requirements to generate exports. To the Commerce Department this appeared as unfair competition to manufacturers based in the United States. "The Mexicans have realized that if they are going to expand industry they've got to force exports; and with our geographic proximity we'll get the brunt of such moves," one official told us. "Mexico," he added, "believes that the U.S. has the responsibility to absorb their production no matter how bad the quality is."

To the Treasury Department and the State Department's Bureau of Economic Affairs this issue appeared as a fundamental challenge to the free-trade regime the United States had been sponsoring since the Second World War. Before taking his post as Assistant Secretary of the Treasury for International Economic Affairs, C. Fred Bergsten had written of the danger of "coming investment wars" as governments got more involved in the management of trade.[25] The espousal of free-trade principles by the Bureau of Economic Affairs (headed by Under Secretary of State for Economic Affairs Richard Cooper) had put it at loggerheads with those sectors of U.S. business who were seeking protection from cheaper imports. But those same principles placed it in tacit alliance with the transnational manufacturing firms who wanted as few constraints as possible on transactions among their international subsidiaries. Free-trade principles seemed threatened by the new Mexican automotive policy in two ways. First, Mexico was mandating a sectoral balancing of its trade position by requiring each individual firm to compensate its imports with exports, rather than seeking a trade balance across the whole economy via the play of international market forces.[26] Moreover, it was mandating these performance standards in an industry where Mexico would not have been expected to have a comparative advantage. This suggested a second issue: that Mexico could not genuinely be competitive in international automotive trade and thus must be subsidizing these exports. Treasury and State concluded that certain of the fiscal stimuli being offered the firms were, in fact, export subsidies. This raised the possibility of placing counterveiling duties on U.S. imports of automotive products from Mexico.

(b) Investment: discrimination against U.S. firms. Within the Bureau of Economic Affairs, the Office of International Finance and Development under Deputy Assistant Secretary of State Charles Meissner was more concerned with investment issues than trade issues: discriminatory treatment of U.S. firms to be specific. The lighter export burden for domestically-owned firms and the exclusion of foreign-owned ones from diesel truck manufacture were cited as examples. It is a distinct possibility that Ford complained as loudly as it did about the diesel truck question because it knew that this would engage the State Department's longstanding concern with discrimination against U.S. foreign investment.

(c) Labor. Finally there were concerns that the new policy would take jobs away from U.S. workers. The Labor Department itself did not champion this issue as strongly as might have been expected (apparently it checked with, but heard no urging to action from, the U.A.W.), but there continued to be a concern in the State Department--in the Policy Planning Staff for example, that there was a substantial threat to U.S. labor in the offing.

In addition to these specific issues concerning trade, investment, and labor, the State Department (particularly Policy Planning and the Mexico Desk) had to maintain a concern with the broader context of U.S.-Mexican relations. Questions of illegal immigration and of oil and gas sales would need to be weighed in deciding how to proceed. The complexity of the bilateral relationship was recognized by the two governments in the creation in May 1977 of a Consultative Mechanism consisting of a Social Working Group (with subgroups on illegal aliens, drug traffic, and other border issues) and an Economic Working Group (with subgroups on trade, tourism, finance, and industry, investment, energy, and minerals). The question of auto industry policy--one of the earliest thorny issues the Consultative Mechanism was called on to deal with--was assigned to the subgroup on industry, investment, energy, and minerals.

Two things should be noted about these interests of the U.S. government with regard to the Mexican auto decree. First, the U.S. government's concerns were rooted in deeply embedded orientations with regard to international economic affairs. Particularly in touching on questions concerning interference with free trade and investment discrimination, the decree could have raised the ire of the U.S. government even if the firms had not sought its assistance. There was a degree of convergence of interests between the U.S. government and the U.S.-based transnational auto firms that led them both to challenge the decree.

It is also important to see that the U.S. government response arose from several diverse concerns spread across the Departments of State, Treasury, Commerce, and (to a lesser degree) Labor. These various interests ran parallel to one another with regard to the decree but were by no means identical. Within the U.S. government itself, the opposition to the decree was a broad alliance, but a potentially fragile one. Under the aegis of the State Department, these different agencies were brought together to confront the Mexican government at a special meeting of the U.S.-Mexican Consultative Mechanism in November 1977. Representatives of the U.S.-based firms were also invited to attend, but they declined.

At this meeting, representatives of the various interested U.S. government departments presented their queries and points of opposition. The Mexican position was defended by Natan Warman and Juan Wolffer from SEPAFIN. Concerning investment discrimination, they argued that exclusion of foreign firms from selected activities was a longstanding policy of the Mexican government; the discrimination was against all foreign-owned firms, and yet only the U.S. government had objected. In addition, they argued that firms without foreign capital had an intrinsic disadvantage in exporting; Mexico certainly did not want to discriminate against Mexican-owned firms. The charges concerning export subsidies were denied: this was simply a deduction based on erroneous estimates of costs and of labor productivity in Mexico. The only tax rebates being given to the firms were CEDIs (Certificados de Devolución de Impuestos)--rebates of domestic taxes. Why should Mexico export taxes? Finally, concerning performance requirements and sectoral compensation, Warman and Wolffer acknowledged that Mexico did have plans to extend this kind of policy to other sectors, but only those with reasonable export possibilities. They sympathized with those who wanted greater trade liberalization, but Mexico needed some compensating mechanism. The country still had a huge trade deficit in the automotive sector. If this could be reduced, perhaps more progress could be made in the direction of true liberalization.

There were quite different assessments of what happened at this meeting and quite divergent conceptions of what should follow from it. On the U.S. side, the Bureau of Economic Affairs saw a number of possibilities for future negotiations to get the Mexican government to modify the volume or the sourcing of the exports that were to be required and to allow market forces to play a larger role in bilateral auto trade. It was joined by others in the State Department and in Treasury who saw this confrontation as a chance to develop a more general U.S. policy concerning performance requirements and export subsidies. At a minimum, everyone on the U.S. side hoped the Mexicans would hear a strong warning not to extend the policy to other sectors.

The Mexicans saw the meeting as a chance to explain and clarify the policy rather than as the first in a series of negotiations. After the meeting they considered the policy no longer an issue of bilateral discussion, an attitude that angered the Mexico Desk and the Bureau of Economic Affairs when reports to this effect came back from the U.S. Embassy in Mexico. There was some eagerness to pursue the matter further, but events on the first front made this more difficult.

The closing of the first front. After the November 1977 meeting of the Consultative Mechanism, the U.S. subsidiaries in Mexico found themselves on the receiving end of stern admonitions from the Mexican government to discontinue efforts to mobilize U.S. government pressure. Such efforts would only be "counterproductive." "The decree is here to stay," SEPAFIN told Ford pointedly. "This kind of reaction could lead to real conflict. We could go back to price controls." The message was clear: the firms needed smooth relations with the Mexican government in further negotiations over interpretation and implementation of the decree. Even if the government were unwilling to change the basic policy, there might be flexibility or leniency in meeting deadlines and targets. The managers of the Mexican subsidiaries may have been chary all along of headquarters' attempts to bring in the U.S. government, but now they were eager to dissociate themselves from the assistance. As one executive put it:

> We here in Mexico have taken the position that because of the idiosyncrasies of the Mexican government it would be counterproductive to have the assistance of the U.S. government in settling our "differences" with the Mexican government. What's more, we don't think we need that assistance. People who would do us a good turn in the U.S. government are not as well acquainted with the situation as they might be. There might be an honest intention to help, but they could create a nasty situation. We don't need their help.

The message was relayed from Mexico to Detroit and from Detroit to Washington. The U.S.-based firms distanced themselves from the U.S. government's efforts to change the decree. The firms had discovered that in this matter, at least, their interests converged as much with those of the Mexican government as with those of the U.S. government.

Something else happened in November which completely altered the bargaining on the first front between the firms and the Mexican government: G.M. announced the first of a series of investments which would generate sufficient export volume to comply with the decree. It announced plans to expand a subsidiary in Mexico, a maquiladora (in-bond assembly plant) called Conductores y Componentes de Juarez that makes automotive wiring systems in Ciudad Juarez.

Resisting pressure to change the decree was an important part of the battle for the Mexican government, but equally important was winning compliance from at least one of the larger firms. The major sanction the government could level against noncompliance was to restrict a firm's access to the growing domestic market. By cutting its foreign-exchange budget in accord with lack of export compensation for imports, the terminal firms would be restricted in production, sales, and market share. But for such a threat to have force, there had to be other firms poised to increase their market shares--other firms who were complying with the decree and thus had sufficiently large foreign-exchange budgets to cover the imports for increased domestic sales. If all the firms refused to comply (with or without explicit collusion), however, it seemed unlikely that the government could force them all to cut back production for the domestic market. The outcry from disappointed consumers and laid-off workers would be too great.

The government was counting on the defensive investment dynamic that has characterized the world auto oligopoly since the late 1950s. Competition among the firms for market share, particularly in large and in rapidly growing markets, is such that if one firm makes an investment the others make move-matching defensive investments to protect their position.[27] It was precisely such a defensive investment dynamic that visited upon Mexico such an overcrowded auto industry in the wake of the 1962 decree, as all of the major world firms scrambled for a place in the Mexican market. This time the Mexican government would rely on the follow-the-leader pattern. After the decree appeared, the government entered into discussions with each firm individually, trying to find one that would be willing to make the needed new investments and counting on the others to follow suit. In both 1962 and 1969, the firm that made the first move was Ford. In 1977, however, after negotiations that ranged to Detroit, Paris, Wolfsburg, and Tokyo, it was (to the surprise of many) G.M. that stepped forward.

Already launched on a massive investment campaign to downsize its U.S. models and to reorganize its global production facilities, G.M. was well-positioned to make such a move. If the other firms were less well-positioned (and some of them, including Ford, surely were) then "breaking the circle" could win G.M. a surge in market share. In the past, however, G.M. had been a quiet firm in the Mexican industry ("Talk about a clam," an executive in a rival firm said); it had been most reluctant to make aggressive moves. Changes in G.M. strategy and organization served to change that. First, G.M. decided to seek to dominate Ford as much abroad as at home. While G.M. had been a market leader in the United States for several decades, Ford traditionally had the stronger foreign operation, selling more vehicles outside the United States than G.M. With the industry restructuring beginning in the mid-1970s, G.M. saw the chance to make its move. All over Latin America, it began to be more aggressive. In Argentina it decided there was little chance of future growth, so it withdrew altogether. But in Brazil, Venezuela, and Colombia, it made large new investments in the late 1970s. In Mexico, things happened differently, because in January 1976 the Mexican subsidiary ceased to be a part of G.M. Overseas Operations and became part of the North American Assembly Division. With this corporate reorganization, Mexico became a prime candidate for a share of the investments needed to downsize G.M.'s U.S. models.

G.M.'s announcement of the maquiladora investment in Ciudad Juarez in November 1977 was only the dropping of the first shoe, and a small one at that. In February 1978, G.M. President Elliot Estes announced plans to build two large new plants, one for assembly and one for engine manufacture to be located in northern Mexico, close to the U.S. border (Ramos Arizpe, Coahuila was eventually designated as the site), and further plans to build two additional plants in Ciudad Juarez to make engine parts.[28] These investments would expand G.M.'s exports from about $10 million in 1977 to $150-200 million in 1983, and thus would allow G.M. to claim a much larger share of the Mexican market.[29]

Once G.M. had made its move, the other firms quickly followed suit, even Ford. In March 1978, Ford and Volkswagen announced plans to expand production capacity both for export and for the domestic market, but could give only sketchy details.[30] Later, Chrysler began development of a 4-cylinder engine plant (also in Coahuila), AMC announced plans to export more manual transmissions to the United States, Nissan indicated it would increase exports of engine parts to Japan, and so on. For its part, Ford discovered that acceding to the requirement that 50 percent of its exports come from Mexican-owned parts suppliers could be the solution to compliance with the decree without calling on scarce capital resources from the United States. It entered into a series of joint ventures with large industrial groups in Mexico, Ford maintaining some voice in the direction of each but taking only a minority equity holding: one with Grupo Alfa to make aluminum cylinder head castings, one with Vidrio Plano de México to make automotive glass, and one with Valores Industriales S.A. (VISA) to make plastic parts.

<u>The quieting of the second front</u>. Because the U.S. government had its own interests in the decree, the withdrawal of support for U.S. government action by the auto firms did not necessarily mean that pressure on Mexico on this second front would automatically cease. For the U.S. government to maintain effective pressure on the Mexicans to change the decree, however, particularly through the Consultative Mechanism, interdepartmental unity and coordination were essential. The coalition within the U.S. government that had presented a unified front at the November meeting with Warman and Wolffer began to fall apart just a few weeks later. The Commerce Department--widely regarded as faithfully representing the auto industry's wishes within the government--became less than eager to push the trade case against the Mexicans when the companies signalled they would rather handle the matter on their own. Those in the State Department primarily concerned with investment questions also felt less urgency once the firms had indicated that it would be healthier for U.S. investments if pressure were withdrawn. Elsewhere in the State Department there was cautioning that other bilateral issues, particularly the question of natural-gas exports to the United States, required a lower key approach on the auto industry decree. The Bureau of Economic Affairs, however, continued to feel that there should be some follow-up, even if a coordinated policy position could not be formulated. In February 1978, a "Diplomatic Note" was drafted by the Bureau of Economic Affairs with the Mexico Desk signing on. One State Department official said:

> Unable to formulate a position we still had to do something. The companies drew back but we had already gone out there in November and had these talks with the Mexicans. So we decided to just slap the Mexicans on their wrists. This was the purpose of the February note. It was a blunt but technically-worded note. We repeated our criticisms and said that we hope you will change this. Period.

The "Note" raised questions about the full range of issues--investment discrimination, performance requirements, and export subsidies--and hinted broadly at the possibility of countervailing duties (for the full text, see Appendix). It was also meant to be a warning not to extend performance requirements or export subsidies to other sectors. "If Warman had further plans in other fields--which he indicated he had--he should not go ahead with them. We had to hit them with a rock and show them that we would tramp all over them if they tried it again."

The Mexicans, thinking the issue closed, were taken aback at the sharpness of the "Note." They were surprised again when nothing followed. Ambassador Lucy made no mention of the issue in his periodic meetings with government officials. In the Spring of 1978, on the occasion of Secretary Vance's visit to Mexico, Under Secretary of State Richard Cooper brought up the decree again in a meeting of the Consultative Mechanism, but the joint communique that came out after the meeting made no mention of the matter. For the time being at least, pressure from the U.S. government had ceased. Unlike 1962, the Mexican government had stood firm in the face of concerted opposition from the TNCs and the U.S. government.

Elements of bargaining power. How and why did the Mexican state prevail in the bargaining? What was different between 1962 and 1977? It is important to recall, to begin with, that the conflict on the first front was not that severe. There was a basic convergence of interests between the transnational auto firms and the Mexican government with regard to the export-promoting orientation of the new policy. The conflict was over the manner in which this was to be carried through. It would be a mistake to see the Mexican government as having forced the TNCs to export against their will; this would attribute a far greater exercise of power to the Mexican government than was actually the case. (On the second front, the conflict of interests was more deeply rooted, but the lack of unity and determination within the U.S. government prevented it from pushing as hard as it might have.)

On those issues where there was genuine conflict--the degree, timing, and sourcing of the required exports, and discrimination against foreign-owned firms--what was the potential power of each of the major actors and what explains their ability to exercise it? For the Mexican state, one important and relatively new element of bargaining power was technical expertise. Despite the disruptive effects of sexenio change, the new team dealing with autos not only had access to the accumulated data and reports of 15 years but also extensive training and experience with economic planning and with the auto industry. Mexico had moved well along the "learning curve."[31]

A second element was inter-ministerial unity. Unlike 1962 when disagreement between ministries eroded the government's bargaining position, in 1977 the ministries presented a common front. "The TNCs thought if they pushed hard something would break," one SEPAFIN official said. "They shopped around different ministries but this time it didn't work." Partly the unity stemmed from the learning of 15 years, partly it stemmed from the administrative reorganization of the López Portillo administration, partly it stemmed from a common perspective on industrial strategy, but partly it stemmed from the feeling that this first major policy of the López Portillo government would be a test case of the government's determination.

A further factor contributing to government unity (and embodying significant learning) was the construction of the decree's regulatory apparatus: it worked on the basis of general rules applicable to all of the companies on a more or less automatic basis. The two earlier decrees gave considerable discretion to the government for the treatment of individual cases, particularly in the determination of production quotas. In the 1972 decree, for example, there were several different kinds of "extra quotas" that could be earned, many based on special capabilities of particular firms. All sorts of bargaining could and did take place on an ad hoc, individual basis over the assignment of these quotas. This case-by-case determination of policy in the previous decrees allowed their coherence to be nibbled away. An ad hoc provision for one firm would lead to cries of inequity from other firms which in turn sought individual relief. The elimination of production quotas (and price controls), and the establishment of foreign exchange budgets--which were set simply and automatically by export earnings and past performance, and which the firms were relatively free to allocate for production as they saw fit--eliminated much of this earlier bargaining for special advantages. In areas where there was ambiguity and special circumstance, the government took care to make determinations or exceptions applicable on a common basis.

The primary basis of power for the Mexican state remained what it had been since 1962: its control over access to the Mexican market and the eagerness of the firms not to be excluded from it. The discovery of large oil reserves in Mexico promised a booming domestic economy and thus made the firms all the more eager to have a share in it. Moreover, now that the firms were reorganizing their global production networks, Mexico took on added importance to them as a low-wage production site close to U.S. assembly plants.

The primary basis of power for the transnational auto firms also remained what it had been since 1962: their control over automotive technology, managerial expertise, capital, and (a newer element) access to international trade opportunities. But these elements of power could only be effective if the firms stood together to refuse these assets to Mexico. A threat (such as the one by Ford) to withdraw from the Mexican market would have created unemployment, dealership closings, and disruption for parts suppliers and consumers. But it was not a credible threat both because the government suspected that no firm would in fact withdraw (part of the government's learning was an appreciation--that they lacked in 1962--of the power of the defensive investment dynamic), and because with seven firms operating in Mexico, the government would have gladly accepted the short-run disruption of a withdrawal for the long-run benefit in rationalization of the industry.

Acting in unity has generally not been possible for the major auto firms--in Mexico or elsewhere. The oligopoly shuns price competition all over the world, but it is fiercely competitive, particularly for increased market share, in many other ways. For all of the meetings of AMIA and the joint action through AMIA to protest specific features of the decree, joint action to withhold investment was never even discussed. Given the benefits of increased market share one firm would obtain from complying, given that new global investments had to be made by all the firms anyway, and given the increased attractiveness of Mexico as a production site, one firm was almost certain to agree and thus to trigger defensive investments from the others. Finally, no alliance was possible with domestic entrepreneurs in the supplier industry: the decree was simply too favorable to their interests.

The remaining and substantial element of power for the TNCs was the possibility of mobilizing their home-country governments to bring other pressures to bear on Mexico. Traditionally, the potential power available to the United States in dealing with Mexico has been enormous. The perception of the credit and investment climate in Mexico, for example, is significantly affected by U.S. government statements and policies, and such perceptions have been crucial given the importance of capital flows from the United States to Mexico. The United States is the primary source of direct foreign investment, totalling about $3 billion in 1977. And by the end of 1976, U.S. private banks were carrying a total of $11.5 billion in outstanding loans and credits to Mexico.[32] Trade relations provided a more immediate lever of potential power, however. About 70 percent of Mexico's exports are directed to the United States, and over 60 percent of Mexican imports are of U.S. origin. Given the character of the 1977 decree, the United States could and did threaten countervailing and anti-dumping duties, as well as new legislation restricting imports from Mexico.

There was, however, a serious limitation on this potential power created by the oil import difficulties facing the United States and the recent revelation of vast reserves of petroleum and natural gas in Mexico, all controlled by PEMEX, the state-owned oil company. These oil and gas reserves, outside the Middle East and so close to home, were a new bargaining chip which would henceforth need serious consideration before the United States played its otherwise strong hand.

Notwithstanding this potential need for Mexican oil and gas (and actual negotiations in late 1977 and early 1978 over sales of natural gas to the United States), the United States still sought to flex its economic muscles in November 1977 and in the ensuing months. In the actual case, it was not Mexico's new source of international power that was the immediate cause of the failure of U.S. government pressure. What stopped the U.S. government from transforming its potential power into actual power was the disunity and lack of coordination inside the government, disunity that was in part fostered by the withdrawal of TNC support for its assistance (particuarly through the Commerce Department), as the Mexican government convinced the firms that reliance on U.S. government pressure was counterproductive and as G.M., seeking its own advantage, broke the circle.

Conclusion: The First Three Years of the New Policy

The successful defense of the June 1977 decree has not meant a completely smooth implementation of its provisions. Over the first three years the terminal firms have not generated all of the exports required of them. After a brief dip, Mexico's trade deficit with the United States in auto products started to climb again (see Table 3).

In 1978, the firms did manage to comply with the requirements. In 1979, Chrysler alone failed to comply, and sanctions were meted out. The firm was charged about US$6 million for subsidies it was granted in 1979 that were not justified by its exports. This amount was deducted from

TABLE 3

U.S. AUTO TRADE WITH MEXICO, 1965-1980
(in millions of US$)

Year	Passenger Cars		Auto Parts[a]		Total[b]		Trade Balance in Motor Vehicles
	Exports	Imports	Exports	Imports	Exports	Imports	
1965	51	0[c]	73	0.1	159	0.1	159
1966	53	0	77	1	158	1	157
1967	54	0	79	1	162	1	161
1968	79	0	91	3	206	3	203
1969	71	0	103	9	206	9	197
1970	38	0	129	18	195	18	185
1971	57	0	137	25	218	26	192
1972	76	0	151	35	244	35	209
1973	98	8	209	56	322	76	246
1974	136	8	258	84	465	119	346
1975	150	1	346	131	528	136	392
1976	131	0	337	18	496	18	498
1977	119	0	338	238	482	240	242
1978	93	0.1	594	269	750	280	470
1979	26	0.1	907	321	1056	327	729
1980	18	0	937	242	1067	245	822

[a]As defined and prepared from the end use classifications of the Bureau of Economic Analysis of the Department of Commerce.

[b]Also includes Trucks, Buses, and Special Purpose Vehicles.

[c]Zero indicates less than $100,000.

SOURCE: "Views of the Motor Vehicle Manufacturers Association of the U.S., Inc. on the President's Report to the Congress on North American Trade Agreements," February 6, 1981, Table 2.4 (U.S. Bureau of Census Data).

its 1980 subsidies. In 1980, when it became clear that several of the firms would not comply, the government took a different tack. Under a new policy, the government began to grant the terminal firms advances on the foreign exchange they were required to generate in a particular model year. Interest would be charged on the advance, and the firms would have to provide evidence of detailed investment plans showing how exports would be generated to repay the foreign exchange within two years. Sanctions would be applied only if the firms failed to repay these advances.

The government judged that part of the export shortfall was attributable to an inevitable lag between investment and export production. If the companies were actually making the investments needed for compliance, sanctions would gain little. The carrot and stick of "advances then sanctions" would have the effect of encouraging even larger investments, since the firms would have to generate additional export earnings to pay back the interest on the advances.

There were other reasons why the terminal firms failed to comply fully in 1980, however. Oil revenues meant a booming domestic economy in Mexico and consequently there was increased domestic demand for motor vehicles. This meant higher levels of imports that needed to be compensated, and in some cases even a scarcity of exportable parts. The increased oil revenues also contributed to significant inflation in Mexico. The resulting over-valuation of the peso made Mexican exports less competitive. At the same time as the Mexican economy was booming, the U.S. economy was in recession, the automotive sector being particularly hard hit. Fewer cars being manufactured in the United States meant reduced demand for parts from all over the global sourcing networks--including Mexico. A recession in the U.S. auto industry was a significant factor in the failure of the earlier export policy of 1974-75. Reorientation toward the international market made Mexican auto manufacture more vulnerable to the expansions and contractions of the world economy. That this new export policy was likely to be more successful did not mean that Mexico could escape the effects of this volatility. Finally, there was a shortfall in exports partly because the auto-parts firms did not have sufficient production capacity. This factor was only one manifestation of a wider set of difficulties and conflicts brewing between the terminal firms and the supplier firms as a consequence of the new policy.

The first (1962) auto decree had drawn a sharp line between the terminal and the supplier industries. Terminal firms were restricted to assembly operations, forging and machining of engines, and the manufacture of whatever parts they had been producing before the decree. The rest was to be reserved for domestically-owned firms--firms that would largely be called into being by the implementation of the policy. Though individual terminal firms had won permission to manufacture some additional parts, the line between the two industries remained clear enough. Under the export-promotion policy, the terminal firms had the onus of arranging half their required exports from these supplier firms (the government recognizing that the supplier firms would have few export chances without this requirement).

Over the first two years following the June 1977 decree, however, the investments of the parts firms were only about 10 percent of the total investments of the terminal firms. There were a variety of reasons: difficulties in arranging financing and difficulties in obtaining machinery and certain raw materials, for example. The chief reason offered by the parts firms, however, was uncertainty about what the terminal firms would purchase. The parts firms felt that orders were not placed in sufficient time and frequent changes in orders further hindered resource procurement and new investment planning. The terminal firms contended that the supplier firms were simply unwilling to take normal business risks; they expected too much certainty. What was emerging was a conflict between foreign capital and domestic capital over their future place in the Mexican auto industry.

The government responded to this potentially explosive situation in several ways. The granting of "advances" to the terminal firms if they failed to generate exports helped to protect the parts firms from attempts by the transnational terminal firms to make a massive move into parts production. As one SEPAFIN official explained:

> Ford or G.M. could, at any moment, have sent us 15 auto parts projects and said "here, give us these if you want us to export. We'll do them right away. Or else don't sanction us for not exporting." The advances give us a certain flexibility with the TNCs so the parts projects can be done by Mexican enterprises.

The government also instituted a policy of "Concerted Planning" under which it required terminal and supplier firms to work out mutually agreeable plans which SEPAFIN could oversee. Certain conditions were set down by SEPAFIN about what an adequate plan would look like. The government granted additional fiscal incentives to the parts firms, and it clarified which motor parts terminal firms could produce--a point of previous ambiguity.

There had been tensions between the terminal firms and the parts firms since 1962, but one important consequence of the June 1977 decree was to sharpen that antagonism. The turn toward export promotion strengthened the hand of the transnational terminal firms: they were already at home in the international market. The new policy weakened the position of the firms in the supplier industry; it increased their vulnerability to the terminal firms. The new decree thus introduced a new face of dependency to the Mexican auto industry. If Mexico was to retain a domestically-owned parts industry, the state would need to carefully manage the new tensions between the two halves of the industry.

Another face of dependency was the reviving prospect of trade sanctions from the United States. Concern in the United States over the decree had quieted down after February 1978, but it had never wholly died. The woes of the U.S. auto industry in 1979 and 1980 helped keep it alive. In the last months of the Carter administration, there were conversations between the two governments in which the United States voiced concern over the loss of U.S. jobs as a result of the Mexican decree. Performance requirements have been an emerging issue in international trade, and the Mexican auto policy serves as a ready example. The Reagan administration has asked the GATT for a study of performance requirements, though it is far from clear what attitude it will take toward the auto decree (responsibility for U.S.-Mexican trade questions has been transferred from the

State Department to the Department of Commerce and the Special Trade Representative; Baldridge and Brock are scheduled to meet with Mexican officials this fall). In several arenas there are pressures on the U.S. government to take some action.

In February 1980, Senator Howard Metzenbaum released a set of internal documents from Ford outlining plans to phase out an engine plant in Cleveland and replace it with one in Mexico. The documents indicated that Mexican production of the engines would not have been cheaper than U.S. production without fiscal benefits from the Mexican government--raising again the question of export subsidies. Metzenbaum's major concern, however, was with the loss of jobs and with what he called Ford's "callous disregard" for U.S. workers.

The U.A.W. has taken a more protectionist posture recently, calling on Japanese firms to begin U.S. manufacture and suggesting that the United States institute its own local content requirements, something that could bring the policies of the Mexican and U.S. governments into direct conflict. Several other labor unions (not the U.A.W.) and several firms have joined together to form a Labor Industry Coalition for International Trade (LICIT). LICIT is seeking U.S. government action against "trade-related performance requirements," and considers the Mexican auto decree a textbook case.

A difficulty facing any urging for U.S. government action now is the position of the U.S.-based transnational auto firms. With substantial investments in export capacity in Mexico, Ford, G.M., and Chrysler would certainly oppose any attempt to restrict, or to impose duties on, autoparts imports from Mexico. In the not-so-distant past, these firms routinely looked to the U.S. government for support in bargaining with foreign governments (as in Mexico in 1962 and in the early stages of the bargaining over the 1977 decree). But now it is within the realm of possibility that a situation might arise pitting the U.S. government (or some significant elements of it) against an alliance of the U.S.-based auto firms and the Mexican government.

APPENDIX

Diplomatic Note

Embassy of the United States of America
Mexico, D.F., February 7, 1978

The Embassy of the United States of America presents its compliments to the Secretariat of Foreign Relations and has the honor to refer to the decree regarding automotive production proclaimed by the Mexican Government in June 1977 and implementing regulations published in October 1977. The United States Government appreciates the opportunity afforded by the Ad Hoc Meeting of the Economic Subgroup of U.S.-Mexico Consultative Mechanism in November 1977 to discuss the potential effects of the decree and the implementing regulations on the U.S. economy and on U.S. firms. As noted by U.S. Government representatives on that occasion, the United States understands Mexico's desire to make its domestic motor vehicle industry more efficient. However, the United States Government believes that the decree and regulations could have a severe, adverse impact on U.S.-Mexican trade.

The Mexican decree essentially requires motor vehicle assemblers to cover all foreign-exchange costs through exports. A foreign-exchange allocation, based on a complex set of interlocking formulas, is assigned to each company of the terminal industry. Fifty percent of this allocation must be met by the export of finished vehicles and parts manufactured in the companies' own plants and the remaining fifty percent through the export of parts or components manufactured by the Mexican automotive parts industry.

The United States Government believes that the regulations are prejudicial to U.S.-owned firms in Mexico since the amount of the foreign-exchange allocations varies directly with the degree of Mexican capital participation. Such inequitable treatment is counter to long-standing U.S. policy opposing discriminatory treatment of foreign investors on the basis of nationality.

Linking foreign-exchange allocations with the export requirement, particularly the obligations to export parts or components manufactured by Mexican-owned firms, could result in a rapid increase of relatively high-cost Mexican exports to the U.S. market. U.S. manufacturers of parts (and the workers involved), losing orders as a result of the U.S. automotive industry's sourcing in Mexico to meet their export requirements under the decree, would likely seek remedial U.S. Government action. In as much as Mexican parts are generally understood to be higher cost than U.S. parts, U.S. industry and labor could easily presume that any significant increase in parts from Mexico in the magnitude contemplated by the decree results from subsidies or dumping with consequent requests for counterveiling or antidumping duties. If the disruption is great enough and/or existing U.S. legal remedies prove inadequate, there may be efforts by the affected U.S. firms and workers to seek remedies through new legislation restricting imports from Mexico.

The U.S. Government is also concerned that the Government of Mexico has the intention to institute similar programs in textiles, pharmaceuticals, and other industries. To the extent that these programs are implemented and affect Mexican exports to the United States, U.S. industry and labor in these sectors will react in the same manner.

These potentially disruptive effects on our trade relationship are of special concern since they stem from the policy of sectoral trade balancing embodied in the decree. Such a policy requires U.S. firms operating in Mexico to export Mexican products without regard to efficiency or cost advantages. Moreover, the implementing regulations compound these problems through the use of devices which artificially inflate the value of automobile component imports. Specifically, the foreign-exchange allocation is inflated by:

A) Including in the formulae the import content of locally procured parts and components;
B) Multiplying the value of imports by the difference between the required degree of local content and the actual degree of local content;
C) Including in the formulae multiplicative factors based on the degree of Mexican capital participation.

The United States understands Mexico's efforts to increase its exports of manufactured goods. If this is accomplished by more efficient production in Mexico, combined with efforts to remove barriers to trade on a mutual basis in the multinational trade negotiations, such a development would be perceived in a positive manner as being in our mutual interest. However, use of artificial and discriminatory devices requiring foreign-exchange balancing by sector can, in the view of the U.S. Government, lead to adverse effects on trade and investment flows between our two countries. The United States Government therefore respectfully requests that the Government of Mexico review the decree and implementing regulations to eliminate the discrimination against U.S. investors and the potentially disruptive effect on U.S.-Mexican trade. In connection with such a review we believe that it would be useful to have further consultations within the framework of the Subgroup on Energy, Minerals, Industry, and Investment, or the Subgroup on Trade.

The Embassy of the United States of America avails itself of this opportunity to renew to the Secretariat of Foreign Relations the assurances of its highest consideration.

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[2]See, for example, Richard S. Newfarmer and Willard Mueller, Multinational Corporations in Brazil and Mexico: Structural Sources of Economic and Non-Economic Power, Report to the Sub-Committee on Multinational Corporations, Committee on Foreign Relations, U.S. Senate, 1975.

[3]Fernando Henrique Cardoso and Enzo Faletto, Dependency and Development in Latin America (Berkeley: University of California Press, 1971, 1979), esp. ch. 6; and Peter Evans, Dependent Development: The Alliance of Multinational, State and Local Capital in Brazil (Princeton: Princeton University Press, 1979).

[4]Cardoso and Faletto, Dependency and Development in Latin America, "Preface to the English Edition," p. x.

[5]"Decreto para el Fomento de la Industria Automotriz," Diario Oficial, June 20, 1977.

[6]For an analysis of the difficulties of the 1969 export policy, see Douglas Bennett and Kenneth Sharpe, "Transnational Corporations and the Political Economy of Export Promotion: The Case of the Mexican Automobile Industry," International Organization, 33 (1979), 177-202.

[7]For an analysis of the bargaining that led to the 1962 decree, see Douglas Bennett and Kenneth Sharpe, "Agenda Setting and Bargaining Power: The Mexican State vs. The Transnational Automobile Corporations," World Politics, 32 (1979), 57-89.

[8]Joseph Kraft, "Annals of Industry: The Downsizing Decision," The New Yorker, 56 (May 5, 1980), 134-162.

[9]See Bennett and Sharpe, "Transnational Corporations and the Political Economy of Export Promotion," esp. 197-199 and Table 3.

[10]Nevertheless, these two areas would be placed in the hands of different deputy ministers within the newly-created SEPAFIN.

[11]For a presentation of the rationale of SEPAFIN in formulating auto policy in the López Portillo administration, see the discussions by Natan Warman and Ernesto Marcos in Memoria: Primer Simposium de Actualización de la Industria Automotriz en Mexico (Mexico: Canacintra, 1978), pp. 11-14 and 60-63.

[12]For a fuller discussion of the demand-side rigidities in world automotive trade, see Bennett and Sharpe, "Transnational Corporations and the Political Economy of Export Promotion," 192-5.

[13] Ford Motor Company S.A., "Estudio Sobre Contenido Nacional y Generación de Divisas por Exportaciones," mimeo, Mexico City, May 1976.

[14] Among other advantages, the new formula would not be subject to artificial changes when the exchange rate between the dollar and the peso changed. The new formula also would not bias against more efficient production in Mexico. Under the old formula, two producers who made identical vehicles and who imported the same parts at the same cost could have different levels of local content if one manufactured its locally-sourced parts at higher cost than the other: the less efficient manufacturer would have higher local content. Under the new formula, both manufacturers would have the same local content.

[15] All of the firms had applied for price increases averaging about 19 percent, but when price controls were ended the firms raised prices on average only 13 percent. It is possible that these price controls had been serving as an informal mechanism of price coordination among the firms, and that the ending of the controls introduced a small measure of price competition among them.

[16] For one published indication of this opposition, see "Closer Look by Firms at Mexican Auto Decree Turns into Frown," Business Latin America, August 3, 1977, 247-8.

[17] "Agreement Establishing the Rules for the Implementation of the Automotive Industry Development Decree," Diario Oficial, October 18, 1977.

[18] To be sure, the decree did provide a bit of encouragement for firms to Mexicanize (by providing special incentives for majority Mexican-owned firms) and to withdraw (by raising the costs of remaining in the Mexican market). But the purpose of these provisions was neither to encourage firms to Mexicanize nor to encourage them to withdraw. One reason the government gave for excluding foreign-owned firms from diesel truck manufacture was that diesel trucks were considered a capital good, and this was a sector being reserved for Mexican-owned firms.

[19] See Douglas Bennett and Kenneth Sharpe, "The State as Banker and as Entrepreneur: The Last Resort, Character of the Mexican State's Economic Interventions, 1917-1976," Comparative Politics, 10 (1980), 165-189.

[20] For a discussion of labor in the Mexican automobile industry, see Kevin J. Middlebrook, "International Implications of Labor Change: The Mexican Automobile Industry," to appear in Jorge I. Domínguez, The International Implications of Mexico's Internal Politics (Beverly Hills: Sage Publications, forthcoming).

[21] The domestic content requirements were somewhat higher than in earlier decrees, but the minimum required level was well below that proposed a year earlier by the Echeverría administration, and the firms were allowed the flexibility to choose between exports and higher local content above that required level.

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[22] See "Big Car Battle: General Motors Moves to Shrink, Lighten Full-Sized 1977s, Steps Up Competition; Rivals Stand Pat; They Try Old Hard Sell," Wall Street Journal, October 29, 1976.

[23] The American Chamber of Commerce in Mexico has been a significant organization for TNCs in Mexico and the auto firms have played leading roles within it. When the June 1977 decree appeared, William Slocum, G.M.'s general manager, was the immediate past president and thus an ex-officio member of its Board. The general managers of Ford (Lynn Halstead) and of Chrysler (Jack Parkinson) were both elected members of the Board.

[24] Fortune, June 4, 1979.

[25] C. Fred Bergsten, "Coming Investment Wars?" Foreign Affairs, 52 (1974), 135-152.

[26] It only added insult to injury, in this view, that the terminal firms would have to compensate for the imports of their suppliers and to compensate by more than 1:1 if they did not achieve the recommended level of local content.

[27] On the defensive investment dynamic, see Frederick T. Knickerbocker, Oligopolistic Reaction and Multinational Enterprise (Boston: Harvard University School of Business Administration, 1973); for a discussion of its role in the automobile industry in Latin America, see Rhys Jenkins, Dependent Industrialization in Latin America: The Automotive Industry in Argentina, Chile and Mexico (New York: Praeger, 1977), pp. 40-42.

[28] "Una Nueva Inversión de General Motors," AMIA Boletin, 159 (March 1979), 1.

[29] "Views of the Motor Vehicle Manufacturers Association of the U.S., on the President's Report to the Congress on North American Trade Agreements," February 6, 1981, Table 2.5.

[30] "Programa de Expansión de Ford," and "V.W. Inicio Su Nueva Inversión," AMIA Boletin, 160 (April 1979), 1.

[31] On this notion, see Theodore Moran, Multinational Corporations and the Politics of Dependence: Copper in Chile (Princeton: Princeton University Press, 1974).

[32] Richard Fagen, "The Realities of U.S.-Mexican Relations," Foreign Affairs, 55 (1977), 685-700.