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MEXICO FROM BUST TO BOOM: A POLITICAL EVALUATION OF THE 1976-1979 STABILIZATION PROGRAM

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ABSTRACT

Mexico from Bust to Boom: A Political Evaluation of the 1976-1979 Stabilization Program

This paper evaluates Mexico's recent experience of economic stabilization policies (under the three-year Extended Fund Facility arranged with the IMF in September 1976) from a comparative-politics standpoint. By comparison with various South American experiences of inflation and stabilization that were discussed in the same Wilson Center workshop, Mexico's short-term performance must be rated quite favourably. This was not a case in which Fund orthodoxy prevailed at every point, nor was the Fund analysis accepted without qualification by Mexico's policy makers. At the end of the period, economic disequilibria, as measured by IMF criteria, remained considerably larger than the three-year plan had envisaged, but "confidence" had been restored and rapid growth was in prospect. The interpretation offered in the paper is that Mexico's cyclical pattern of presidential politics largely determined the effective contents of the stabilization package, and that the resilience of the Mexican system of political management goes far to explain why the economic outcome was more favourable than in the South American cases. An accident of geological endowment (the nation's huge oil resources) certainly accentuated the process of recovery from "bust" to "boom," but this factor did not operate in isolation, and should not be considered an adequate explanation on its own. The impact of a geological endowment upon economic conditions depends upon political mediation. However, although this paper seeks to highlight the contribution of Mexican political management to the recent short-term economic improvement, it concludes with some qualifications. The final section considers some constraints on the scope and efficacy of Mexican "reformism," particularly in relation to longer term and more structural problems.

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Introduction

On September 13, 1976 the Mexican government applied to the IMF for financial assistance in tackling its acute balance-of-payments difficulties. It required (i) immediate assistance to replenish official foreign-exchange reserves, and (ii) longer term support while it implemented a three-year plan of economic stabilization intended to restore external and internal balance to the economy.

The immediate assistance was needed to help carry the country through the acute uncertainties that would surround the change of administration on December 1. It was recognised that the Mexican authorities would be virtually incapable of providing effective economic management until President López Portillo had assumed the reins of power, announced his cabinet appointments, and made his first public policy announcements from the presidency. From September 1 (when the scale of private capital flight had forced the outgoing Echeverría administration to suspend official intervention in the foreign-exchange markets to maintain the parity of the peso to the dollar) until November 30, there would be something of a power vacuum. During those months, the Bank of Mexico would abstain from net intervention in the currency markets, confining itself to the conservation of official reserves and the honouring of foreign contracts. In effect, the purpose of immediate assistance from the Fund would be to help the authorities meet their international obligations despite the financial crisis and the collapse of confidence that was accepted as an unavoidable feature of the internal situation until the political interregnum had passed.

However, although the Mexican authorities might temporarily lack the means to exercise effective control over the internal economy, there was to be nothing like the degree of discontinuity between one administration and the next that characterises various of the South American economic crises to be considered in this workshop. On the contrary, the continuities of personnel between the Echeverría administration and that of López Portillo would prove very marked (in particular the incoming President was the former Treasury Secretary); and, although the circumstances made for inevitable strains between one government and the next, the underlying reality was of collaboration and the maintenance of shared priorities. Two features of this underlying collaboration are of particular interest here: they concern the distribution of blame for the immediate crisis, and the process by which the longer term proposals for economic stabilization were generated and put through. My impression is that the outgoing government, perhaps reluctantly, made a gift to its successor by abandoning efforts to postpone the economic crisis three months before its mandate was due to expire. By these means, it accepted blame that in most countries would have been disputed between the partisans of the two rival administrations. In return for this gift, the incoming government bound itself to a formula for economic stabilization that it had not really negotiated for itself--although there must have been intensive consultations at a high level. This was particularly serious since, if taken literally, the formula appeared to dictate most of the main parameters of government action over the next three years. (The terms of the 1977-1979 Extended Fund Facility will be outlined later in this paper.)

These are my impressions of the nature of the underlying political collaboration between the two administrations, but it is as well to recognise the great difficulties in obtaining conclusive proof of such assertions. In addition to the problem of evidence, there is a question of counter-factual interpretation. An alternative school of thought could claim that I have overstated the scope for political choice during this crisis, and that economic necessity would have forced Echeverría to shoulder the blame for it however much he wished to transfer the unpopularity to his successor, and that the terms of the three-year stabilization program were likewise dictated by economic necessity without a significant margin for political negotiation. Such disagreements over the interpretation of specific historical episodes often reflect broader problems of analysis that ought to be addressed. It seems to me that much of the social science literature concerning the processes of inflation and stabilization treat questions of political management (and of the operation of institutional devices for processing distributional conflicts) as epiphenomenal.[1]

By contrast, in this "political evalution" of the recent Mexican experience I shall attribute a central importance to such factors. They require close attention if we are to explain accurately why the macro-economic disequilibria that developed under Echeverría took the form and acquired the scale that they did. They also played a major independent role in contributing to the character and speed of the relative economic recovery experienced in Mexico since 1976, and they will go far towards shaping the country's future economic performance and the pattern of its future economic crises. These political arrangements that can produce such significant economic effects are not just "manna from heaven," or an automatic adaptation to market realities, or the inevitable consequence of a certain stage in the development of capitalism. They have been created and are sustained by a continuing process of political organisation and struggle. Their effectiveness can be greatly improved, or gravely impaired, by the deliberate actions of those who engage in Mexican politics, and of those external interests which have sufficient leverage to influence Mexican affairs. At least, these are the type of assertions on which my analysis of the Mexican example rests. Clearly, I am attributing a greater degree of autonomy and more strategic importance to political-management factors than is generally accepted. By arguing these contentions in a strong form I hope to sharpen the focus of workshop discussion.

Consider a couple of specific (but of course hypothetical) examples. If essential foreign assistance to Mexico's stabilization efforts had been made conditional on the provision of assurances that there could be no repetition of Echeverrismo, this would have polarised political divisions within Mexico and impaired the effectiveness of the established system of political management. The same would have been true if essential collaboration from the Mexican labour movement had been made conditional on an inflexible preservation of Echeverría's social and distributive policies. In my view, both of these hypothetical developments were sufficiently real possibilities that active planning and organisation were required to head them off. One purpose of the international comparisons that we can develop during the workshop discussions might be to test claims such as this in the light of experiences in other countries. Do the comparisons with South American experiences of stabilization crises indicate that these questions of political management are epiphenomenal to the underlying pattern of economic performance? Do international comparisons support the idea that the necessities of the economic situation left Mexico with no alternative but the strategy of stabilization actually adopted by the López Portillo administration? Or would a less united and disciplined political system have given rise to a deeper stabilization crisis and more lasting damage to the country's capacity for economic and social recovery? On the second view, the strengthening of political institutions and attitudes favourable to the maintenance of economic equilibrium could be a more important and lasting determinant of the viability of stabilization policies than the more short-term fulfillment of certain rather arbitrary economic-performance targets. From the way these comparative questions have been framed, it will be apparent which answer I tend to favour. And so the rest of this paper seeks to bolster my preferred answer with evidence from the Mexican case.

Unfortunately, as I have already acknowledged at certain key points, my account of the Mexican case must rest on a number of impressions and interpretations each of which is also controversial. The types of explanation with which we are concerned in this workshop are not subject to conclusive proof, only to informed and reasoned judgement, and are certainly open to discussion. Here then are some necessary stage-setting contentions:

1) The most important external features shaping Mexico's economic and political possibilities are not adequately captured by the abstract categories of "dependency" theories or any other general accounts of centre-periphery relations. Whatever their insights, all such Latin America-wide models abstract from the distinctive circumstance of Mexico that crucially differentiates its case--a degree of

geographical and economic involvement with the United States that creates exceptional possibilities and dangers, and a unique tradition of political responses. This circumstance may make the segregation between internal and external causal factors even more difficult than for other Latin American cases. But it also makes such a disentangling of factors more essential.

2) The overall character of the Echeverría administration--including its choices of economic strategy--cannot be understood unless the gravity of the 1968 legitimacy crisis is grasped. The need to recapture popular credibility after that confrontation cannot be used to explain or excuse every decision of Echeverría's administration, of course, but nothing it did can be properly understood unless that priority is seen as central.

3) Echeverría's decision to expand the role of the public sector in the overall economy was not a purely economic strategy, but nor was the political rationale for it socialist in character. Therefore, judgements of the results based purely on the criteria of allocative efficiency are incomplete, and attacks based on the assumption that the government was trying to destroy the private-enterprise system are misconceived. In fact, the political element in the motivation was to strengthen the state's capacity to arbitrate between economic interests, and to marshal national support for a populist regime operating a mixed economy.

4) Despite the rumours and panic of late 1976, there was never a serious likelihood of a coup, or a rupture of Mexico's established political institutions, or a breakdown of the normal mechanisms of social control. There was just an unsettling interregnum, exacerbated by the financial crisis.[2]

What follows is a preliminary evaluation of Mexico's experience with stabilization policies, 1976-1979. The basic assessment is that compared to what it was realistic to expect in 1976, and to what other Latin American countries have been experiencing in their stabilization endeavours, the short-term performance of the Mexican economy has been pretty good. This is not, however, a case in which firm adherence to IMF-approved guidelines restored equilibrium and produced economic recovery. Nor is it simply a case in which the revelation of Mexico's vast hydro-carbon reserves overrode all previous considerations, although of course the country's greatly increased export potential did greatly accelerate the restoration of confidence in its economic prospects. In this paper, attention will be focused upon the ways in which political continuity and social control were maintained through the extremes of the economic cycle. Some distinctive features of the Mexican political system contributed substantially to the recent performance of the Mexican economy. They are also central to any assessment of the economy's longer term prospects.

The argument will be presented under the following headings: domestic and international contributions to disequilibrium; relations with the Fund; distributive effects of inflation and stabilization; organised labour; the private sector; the impact of oil; and concluding evaluation: the scope and limits of Mexican reformism.

Domestic and International Contributions to Disequilibrium

Although there were various serious deficiencies in the economic strategy practised by Mexican authorities during the 1960s, by many standard criteria the country's performance was gratifying. Real GDP grew fairly steadily at around seven percent per year, domestic prices kept very close to U.S. levels, both the public-sector deficit and the current-account deficit remained at levels that could be fairly readily financed, and on the supply side most sectors of the economy displayed considerable flexibility and responsiveness. Free convertibility with the dollar at a fixed rate (12.5 pesos) had been maintained without variation since April 1954. The American Chamber of Commerce offered this forecast at the outset of the Echeverría administration:

> If prices do rise this year, say by 4.5 percent to 5.0 percent in terms of the new retail price index, the consequence will depend on how prices move in the rest of the trading world. Since 1958 only the US and Germany can boast of a better average record of price stability than Mexico. With the powers possessed by the Mexican monetary authorities over the money supply and the distribution of financial resources, and more important their proven determination to make use of them, no runaway increase in prices is reasonably predictable.[3]

In reality, as the statistical record at the end of this paper shows, the public-sector deficit widened year by year throughout the sexenio. Consumer price inflation soon accelerated far above U.S. levels, stimulating imports and foreign travel by Mexican nationals, and discouraging exports. To maintain the process, it became necessary to increase the foreign debt at a very rapid rate, to curb imports by administrative means, and to raise bank reserve requirements so that domestic savings were "forced" to finance the fiscal deficit. When these expedients had reached their limit, and still the public-sector deficit was not reduced, speculation against the fixed exchange rate became irresistibly attractive and impossible to control. In 1976-1977, the speculators reaped the benefits of an 80 percent devaluation against the dollar.

This brief account has focused attention on the public-sector deficit as the strategic variable, but there is a rival view--according to which adverse developments in the international economy caused most of the disequilibria experienced under Echeverría.[4] Firstly, it is true that inflation in the United States reached double digits by 1974. With the peso pegged to the dollar and Mexico's trade and finance closely integrated with that of the United States, it was very unlikely that her inflation could be kept much below the American rate--especially since, until 1976-1977, the annual real growth rate of the Mexican economy remained at levels substantially higher than in the United States. (Cumulatively the Mexican economy grew about 57 percent between 1969 and 1978, compared with about 28 percent for the United States.) In Mexican conditions, rising inflation was likely to aggravate the fiscal deficit as public-sector costs and wages and borrowing charges exceeded expected levels, whilst many tax revenues and public-enterprise selling prices tended to lag behind. Secondly, the Mexicans had to contend with an international economy that was not only more inflationary and less expansionary than before, but was also much less predictable. Many of Mexico's public-expenditure commitments, for example, concerned major development projects that would not reach fruition for a number of years, by which time the international economic parameters might have shifted drastically. At least part of the difficulties of Echeverría's ill-fated iron and steel project at Las Truchas (which had World Bank funding) can be attributed to the unforeseen problems of that sector; and equally well the greatest success of his public expenditure plans (the decision that PEMEX should step up its expenditure on drilling for hydrocarbons) was taken in 1971, at a time when few would have forecast how favourable the international market for oil and gas was likely to become. Much of the expansion of public-sector spending that occurred between 1972 and 1974 reflected rising expectations about the expansionary capacity of the world economy that misled not only Mexican policy makers, but also the governments of most developed countries, and the international financial community in general. The international recession that struck in 1975 was unexpectedly severe, and all the more disrupting to Mexican policy makers because it was the second to strike the economy in a single sexenio, and at the point in Mexico's six-year political cycle in which the resort to austerity measures is least possible.

Such considerations explain why government spokesmen laid such stress on the international economy as the essential cause of the macro-economic disequilibria that were visibly developing throughout Echeverría's term. Nevertheless, the scale of Mexico's 1976 adjustment problem was larger than could be explained solely by reference to these international developments. In this context, it is important to note that by comparison with most of the other countries under discussion in this workshop (Chile, Jamaica, Peru, Uruguay) Mexico's foreign-trade sector is a very small proportion of total economic activity. In addition, the Mexican economy has a relatively greater capacity to substitute domestic sources of supply for unavailable imports. Therefore, although rising import costs and diminishing availability of imported supplies certainly produces significant effects in terms of both domestic inflation and loss of internal efficiency, the Mexican economy, like that of Brazil, is capable of considerable flexibility of response, and with appropriate policies can absorb relatively strong shocks from abroad.

Therefore, various economic advisers, including Echeverría's first Secretary of the Treasury, and concentrated their attentions on the domestic instruments of economic management. In particular, they had warned against a too-drastic expansion of public expenditure unless combined with very strenuous efforts to raise public-sector income. Apparently accepting this argument, Echeverría came very close to adopting an ambitious tax-reform measure in 1972, before diluting the scheme (and dropping the Minister) and resorting instead to increased foreign borrowing. The ready availability of Euro-credits for long-term public-investment projects must have acted as a temptation to the government, offering as it did the means to expand state activities and implement cherished programmes without aggravating the already very poor relations between the administration and the business community. Probably the most conclusive objection to the proposed tax reform is that it would have precipitated such capital flight that the government would have been forced into a devaluation before its internally re-legitimising policies had even begun to take effect. It is difficult to know how far to classify these considerations as "domestic" and how far to regard them as aspects of Mexico's mode of insertion into the international economy.

But whilst such semi-international factors may explain the failures to increase government revenues more rapidly, the determination to persist with very expansionary public-sector expenditure plans must be explained in essentially domestic terms. Internally, there were a series of compelling reasons why public expenditure was required to rise so fast. Many urgent forms of social expenditure (e.g., on primary education, or on urban water supply) had lagged behind demographic developments to an extent that was becoming politically dangerous. The 1968 crisis had highlighted these threats to the regime's stability, and had deepened divisions that could only be covered over by policies involving new forms of public expenditure. To counteract what the new administration viewed as the excessive political influence of the private sector, it was necessary to breathe new life into the pro-government mass organisations; and since these were essentially distributive agencies, their revitalization would require an increased flow of public resources. By 1973 the authorities were coming to recognise that such internally redistributive objectives would be attainable only if internal restraints on inflation were substantially relaxed. Fiscal and credit policies were no longer designed primarily to keep down the overall price level, and soon substantial increases in wage rates, guaranteed prices, and utility charges were authorised as well. There was in effect a governmental decision to respond to the upsurge of imported inflation by accepting a burst of domestically generated price rises as well, the object being to adjust relative prices and factor incomes in accordance with the new political priorities, and to capitalize lagging sectors of the economy. However, the intention was not to set off an uncontrolled wage-price spiral. Thus one essential tool for the restraint of inflation was not relaxed: the exchange rate remained pegged to the dollar, with free convertibility still fully maintained.

In retrospect, then, the economic strategy adopted in the early 1970s responded to some rather urgent political concerns. Mexican leaders have some grounds for their belief that by preserving their established system of political representation and control they are enhancing their country's long-term capacity for effective economic management and the promotion of development. Echeverría's economic strategy is best evaluated not as a mere product of arbitrary and irresponsible personal leadership, but as a reasonably rational attempt to reinvigorate that political system, accepting a certain loss of short-term economic equilibrium as a regrettable consequence. In the event, of course, the short-term economic consequences were far more damaging than he could have intended, and they threatened to spill over into grave political damage as well. This was the domestic sequence that, at least as much as any shocks from the international economy, contributed to the financial crisis of 1976.

Since we know the unhappy end of the Echeverría administration, does it follow that the crucial domestic strategy decisions of 1972-1974 must be evaluated with corresponding harshness? If so, many other governments (including those of the U.S. and the U.K.) require comparably stern criticism, for this was a period when many countries adopted economic strategies that can be seen in retrospect to have produced seriously undesired results. In reality, a fair evaluation of Echeverrismo must rest on some quite difficult questions of judgement. How much scope was there for the achievement of the administration's minimum political objectives with a smaller fiscal deficit? The conclusion I have argued elsewhere is "not much."[5] Alternatively, how unrealistic was it to believe that after the 1973-1974 rise in domestic costs, relative to those of the United States, it would still be possible to maintain the parity of the peso (aided by foreign borrowing) and to use the stability of the exchange rate to bring domestic inflation back down to U.S. levels? According to a respectable estimate, the peso was only slightly more "overvalued" in relation to the dollar in 1974 than it had been during the previous worst year, 1967.[6] But of course in 1975 the United States entered a sharp recession, so that the Echeverría administration was confronted with a worse balance-of-payments deficit, and less stimulus from external demand, than could reasonably have been anticipated. To avoid another "halt" to economic growth, such as had been suffered in 1971, the administration increased its restrictions on imports, extended its programs of foreign borrowings, and scaled down the determination of its anti-inflation stance. The consequences of this external shock, superimposed on the earlier decision to risk a bout of domestically induced inflation, both creating effects that the government felt too weak to absorb, was to produce by mid-1976 a rather severe degree of exchange-rate overvaluation, and quite severe domestic imbalances. These disequilibria were comparable in gravity to those occurring in most of the other countries considered in this workshop. Compared to those other cases, Mexico seemed to have two main advantages that should have kept the disequilibria on a smaller scale. The Mexican economy had a relatively high capacity to adapt to external shocks without sharp losses of output; and one might have expected the famous resilience of the political system to have facilitated a relatively rapid and effective response before the troubles grew too serious. However, there were offsets to both these advantages. The Mexican economy was exceptionally vulnerable to capital flight, a fact that had constrained the government's capacity to raise public-sector revenues when required; and in consequence public policy had become so severely slanted towards private wealth-holders that it threatened the social bases of the political system. Despite its many formal advantages, these underlying social tensions greatly limited the government's real freedom of maneuver, particularly as the end of a sexenio drew near, and above all if open repression was to be avoided.

Relations with the Fund

In his September 13, 1976 letter of intent to Director Witteveen of the IMF, Treasury Secretary Mario Ramón Beteta characterised the balance between internal and international factors contributing to the disequilibrium as follows:

> The Mexican government maintained the level of national economic activity in the face of the international recession by raising public expenditure. This caused pressures on the public finances despite the strong increase in government and public sector incomes. Unfortunately, the combination of international inflation and recession, and the financial costs of our efforts to reinforce key sectors of the economy with their consequent effects on the national price level, produced an adverse effect on our balance of payments. These disequilibria, both internal and external, accentuated the erosion of Mexico's international competitiveness. This loss of competitiveness only became clear to us when our major trading partners began an economic upswing, in which our economy did not participate to the degree we had anticipated.[7]

The Fund staff produced an internal memorandum dated September 22, 1976, recommending acceptance of the Mexican application for assistance, but arguing that adverse international trade accounted for less of the disequilibrium than the Mexican authorities seemed to be suggesting. The Fund view was that, of the $2.4 billion deterioration that had occurred in Mexico's current account deficit between 1973 and 1975, only one-third appeared attributable to factors beyond the responsibility of the government. They also estimated that, between 1973 and August 1976, Mexico's competitiveness had declined by 40 percent, implying that the "equilibrium" exchange rate at the moment of the peso "float" was about 17½ pesos to the dollar.[8]

However responsibility for the 1976 disequilibria was to be apportioned, the Fund and the government of Mexico were in agreement that it would require several years to correct the economic imbalances. This was in marked contrast to the attitudes both had adopted at the time of the previous Mexican devaluation (of 31 percent against the U.S. dollar). In the words of the Fund memorandum: "Unlike the previous peso devaluation of April 1954, when there was a move from one fixed rate to another, on this occasion the Mexican authorities feel themselves unable to bring about the required adjustments in demand, in administration, and in incomes policies all at one go. Instead they decided to let the peso float for some time and to elaborate a three-year adjustment plan."[9]

In contrast to much that is written about the IMF's power over those member states requiring assistance with their stabilization plans, this part of the memorandum conveys the impression that the initiative for policy formulation still rested very much in the hands of the

Mexican authorities. (Footnote 9 strongly conveys the same impression with regard to 1954.) The Mexican letter of intent stated firmly that the objectives of their three-year stabilization program would be to accelerate the underlying rate of growth (seven percent per year was the figure proposed), expand the provision of new jobs for the growing labour force, and stimulate domestic savings in order to reduce dependence on external sources of finance. Only after these three objectives came the conventional nods towards price stability and the restoration of balance-of-payments equilibrium. (In fact, the results of Mexican policies since 1976 confirm that the first three objectives have been pursued with greater vigour and success than the latter two.) My impression of the negotiating sequence is that the Mexican authorities planned out their approach to the Fund, making a well-informed assessment of what disagreeable conditions they would have to accept, and on what issues they could refuse to budge. Differences in priorities between different branches of the Mexican bureaucracy, and between the outgoing and incoming administrations, were apparently resolved within Mexico before the Fund was approached. Therefore, the Fund found itself presented with a united front, but more than that with a front that had united around proposals that could be accepted as realistic according to Fund criteria. If true, this would run counter to the widespread view that when Latin American governments approach the Fund they invariably capitulate across the whole range of economic policy issues, more often than not even "internalising" Fund interpretations and priorities. Workshop participants may wish to discuss in the light of the Mexican experience how much scope Latin American policy makers may have to secure Fund approval for independently generated economic strategies, and what the political or economic conditions may be for maximising such scope.

In answer to its critics, the Fund can point to the limited monitoring resources at its disposal, and the internationally agreed character of its Articles of Agreement and its policy guidelines. Because of these characteristics, it is argued that the Fund must rely very heavily on the information and assistance available from the authorities of the member country, and must abstain from making proposals that would constitute internal political intervention.[10] Since the Mexican authorities have their own highly elaborated (and centrally coordinated) view of economic management, they naturally sought to make the Fund "internalise" their own economic interpretations and priorities. The most they seem to have achieved was to persuade the Fund to include this passage in its staff memorandum: " A well-known characteristic of the outgoing Echeverría administration was its emphasis on income redistribution and support for the long-neglected agricultural sector. It allocated new responsibilities to the public sector and increased public spending. But during that six-year period there was a certain shift of emphasis from considerations of economic productivity to those of social content."[11] After these fairly restrained nods in the direction of the Echeverría administration's arguments, the staff memorandum switched into a more familiar vein: "Strong opposition must be overcome before it will be politically possible to stop the provision of consumer subsidies on basic consumption items, and to dismantle the associated bureaucracy. Perhaps it will be even more difficult to get it recognized that the wage rises of recent years caused Mexico's loss of competitiveness, and to obtain the necessary support for a policy of real wage cuts."[12] There are genuine grounds for doubt whether this stress on wage push was based on adequate staff work,[13] but the real point is that neither the Fund's limited monitoring resources, nor its Articles of Agreement, nor any counter-arguments from the Mexican authorities, seem to have modified its standard requirements for politically painful real wage and public-subsidy cuts. Another passage in the memorandum is even more explicit in its political concerns:

> In theory, with a floating exchange rate the balance of payments can be kept healthy whatever the defects of other economic policies. But in the absence of corrective action in other fields the result will probably be a continuous devaluation of the peso and an accumulative inflationary spiral. If this were to occur it would probably have effects on Mexico's commercial and financial relations with the rest of the world, and provoke radical alterations in the country's economic and political system, and in its national objectives. It is therefore of critical importance to act as quickly as possible on various political fronts to reduce pressures on the exchange rate.[14]

Here we see glimpses of some of the assumptions underlying Fund policies that are not apparent from its technical and legal self-description. International commercial banks look to the Fund as a kind of guarantor of the credit-worthiness of non-Communist debtor governments, and of course (as recent experiences in Iran have illustrated) sovereign credit-worthiness relates not just to financial variables, but to political will and commitment as well. The Fund's first obligation is to the maintenance of a certain structure of international economic relationships (one in which not all countries participate, and from which some countries may withdraw--as Cuba did in 1964) rather than to the principle of non-intervention in internal political affairs. In fact, this obligation to a certain type of international economic structure may require the Fund to involve itself very deeply in the internal affairs of debtor countries whose national institutions are very fragile, but whose continued solvency is of strategic interest to what used to call itself the "Free World."[15] Since the Fund's first obligation is to this international system, governments that are forced to turn to it for assistance have discovered that the Fund cannot put even the preservation of a member state's existing social fabric above the restoration of its short-term credit-worthiness in international capital markets, where these considerations tug in opposite directions.[16]

Fortunately there was not a fundamental divergence between these two objectives in the Mexican case. The agreement with the Fund created some political difficulties for the López Portillo administration, and gave those who suffered from the austerity measures of 1977 a target for attack on nationalist grounds. But these reactions were relatively minor and easily absorbed. At the governmental level, the major problem appeared in December 1977 when (in a move that was a departure from Mexican political traditions) the President accepted the resignation of his Planning Minister, Carlos Tello, whose letter of departure spoke openly of the country's "grave economic crisis" and the need to "rectify the contractionary policy adopted by the Treasury and supported by the IMF." Traditionally, Mexican governments go to great lengths to avoid the appearance that external pressures have produced internal divisions. In this case, both the Planning Minister and the Treasury Secretary were replaced so that the principles of governmental unity and independence could be reasserted. The nationalist potential of this issue was diminished by the fact that it was a previous administration with strong nationalistic pretensions that had created the conditions for dependence on the Fund's assistance. Also, by the end of 1977 the worst phase of the austerity had occurred, and the prospects of recovery, and reduced dependence on Fund surveillance, were in sight.

In contrast to some of the other stabilization experiences considered in this workshop, Mexico's vulnerability to Fund disapproval quickly passed. The amount of financial resources directly provided by the Fund was quite small both in relation to Mexico's balance-of-payments needs, and to its normally available resources. It was for little more than a year that these funds were urgently needed--by the autumn of 1978 early repayments were being made. If the agreement with the Fund is viewed from a political, rather than a narrowly financial, perspective it appears that the main function was to provide an external guarantee to the private sector and the international banks. During the "lame-duck" period of Echeverría's term, and the earliest phase of the López Portillo administration, the Mexican government lacked the authority on its sole initiative to enter into commitments that the private sector would find credible. However, Mexican commitments to the Fund carried an imprimatur that would convince even the most nervous of private wealth-holders (who were Mexican capitalists rather than foreign bankers). In the normal course of events, Mexican governments are accustomed to negotiating their bargains with these private interests directly, and without external supervision. By the beginning of 1978, the López Portillo administration had established its solidity and effectiveness, and no longer required any external intermediation. Of course the increase in Mexico's oil reserves was important in restoring confidence (a factor that will be evaluated later in this paper), as were the IMF-approved measures to restore financial incentives to the private sector and to restrict public spending. However, the reestablishment of political stability, unity, and a sense of effective leadership were at least as important as these economic developments in reassuring traditional creditors and investors, and thus enabling the Mexican authorities to free themselves from the straitjacket of their stabilization agreement with the Fund. In comparing Mexico with other countries, three dimensions would need to be considered: (i) the orthodoxy of the agreed stabilization package, and the wholeheartedness with which it was implemented, (ii) the governmental system's capacity to inspire confidence in its determination, competence, and command over internal political forces, and (iii) the scale of economic and financial resources that the national authorities could activate independently of Fund approval. Mexico's great strength on the second and third counts, compared to the other countries under consideration, gave it more latitude with respect to the first heading, and therefore minimised the severity of the stabilization experience.

Even in the Mexican case, of course, it was necessary to accept a certain number of specific commitments to the Fund that were not just technical in character, but involved serious domestic political consequences. As it turned out, the Mexicans have eluded the necessity to carry through these commitments to the full, by entering into a phased three-year program whilst the Fund has only been in a position to insist on complete fulfillment of its conditions during the first phase. Perhaps this was foreseeable, but in view of the pessimism and alarm observable in official circles in 1976-1977, it may be assumed that both sides considered it possible that all stages of the program might be carried out to the letter.[17] The program specified a series of targets, mainly concerning public-sector finances, and it was assumed that with the fulfillment of these commitments the Mexican authorities would be well-placed to fulfill the five priority economic objectives listed above. Limits were placed on net public-sector foreign borrowing, limits which to date have been respected as far as I can discover. This has been less onerous than might have been feared, however, owing to the substantial inflows of private capital that occurred when the panic conditions inducing the 1976 capital flight were reversed (see the "errors and omissions" item in the statistical record at the end of this paper), and when subsequent growth prospects attracted private investment capital. These private capital movements reduced official concern about the deficit in the current account of the balance of payments, a deficit that was sharply reduced in 1977 although it rose again in 1978 and shows signs of persisting in 1979, despite the rapid build-up in oil exports. The program specified no quantitative target for the current account deficit, but it did indicate specific targets for the public-sector deficit. This was to be reduced from 9.6 percent of GDP in 1976 (a figure inflated by the effects of the currency collapse and domestic cost leaps of the last few months of interregnum) to 6 percent in 1977, 4 percent in 1978, and 2½ percent in 1979. In the event the recession and high interest costs of 1977 kept that year's deficit at 7½ percent despite very tight controls on public expenditure. To reactivate the economy in 1978, restraints on public spending and the credit system were relaxed with the result that the money supply was expanded by 31.7 percent (a larger increase than in any year of Echeverría's government). The reactivation helped the public-sector deficit fall, but only to 6.4 percent of GDP--still larger than the level attained under Echeverría before 1975 and far above the 4 percent target for the year. These internally expansionary (and inflationary) policies fall far short of full compliance with the Fund-approved stabilization program--as the future statistics on the inflation rate and the public-sector deficit for 1979 will doubtless make clear. These policies are more accurately viewed as an escape from Fund prescriptions that would have sacrificed output and employment in pursuit of financial stability. Since confidence in the currency had been restored, and domestic and foreign savings were made available, the Fund had no real grounds for complaint, however. Certainly not if, as I have argued, its essential concern is with the maintenance of the international credit system, rather than with the internal policy preferences of credit-worthy nations.

In my view, therefore, the impact of the three-year stabilization agreement was far less politically stressful, and violatory of Mexican political autonomy, than might have been feared in 1976. Nevertheless, even this agreement produced powerful effects on the internal distribution of resources between economic groups and sectors. These effects were bound to be politically contentious. The next section considers how such internal political conflicts were processed and contained.

Distributive Effects of Inflation and Stabilization

Any attempt to analyse this aspect must be extremely tentative for three reasons. The information available is very limited and highly suspect. Even with much better information, the conceptual tools for analysing it are rudimentary, crudely aggregative, and the object of much controversy. Even if this were not so, the problem of disentangling the distributive effects of the inflation and the stabilization policies from the effects of other related processes--the recession, the sectoral problems of energy and agriculture, and the underlying demographic pressures--might seem insoluble. But regardless of these difficulties, some attempt at analysis is called for since people hold strong beliefs about the causes of distributional shifts, and those strong beliefs are themselves an important factor in the political process.

The overall distribution of family income in Mexico has long been highly unequal, and apparently became more regressive with each study that was conducted from the mid-1950s to 1975--although the data used to support this claim are very questionable.[18] Government policies since 1970 have emphasized the need for a more equitable pattern of economic development, a concern that was reiterated in the 1976 letter of intent, but there is considerable confusion about what this really means, how we would know that it was being achieved, and above all how to achieve any kind of lasting improvement in the distributional pattern within a market economy. In view of this lack of clarity, both the Fund and the Mexican government were able to agree on the principle, despite considerable differences of emphasis on the specific steps to be taken. For example, the Fund could consider that a reduction in real wages and in public consumption subsidies was compatible with increased equity, because permanent employees were a privileged minority, public subsidies were subject to corruption and skewed towards the urban middle classes, and it was the rural poor and the informally employed who had least defence against the inflation caused by deficit spending. By contrast, the Mexican authorities might consider precisely these steps to be regressive short-term necessities, favouring the employer class and withdrawing state protection from vulnerable groups of consumers. On the second view, the inclusion of a distributive equity clause in the stabilization program would provide a defence against excessive cuts in these categories of public expenditure. Which of these two strategies would produce a more progressive distribution of overall family income? There is no generally accepted answer.

In any case, when considering the internal political consequences of a particular economic strategy, changes in the overall concentration index may be of far less significance than other more disaggregated types of distributional shift. In other work I am doing on Mexican politics, I am reaching the conclusion that there are complex political structures regulating the distribution of certain resources (land, water, access to credit, jobs, licenses). This political distribution system has a vital function in the organisation and control of popular forces, and it parallels and even modifies the functioning of the open market system (a system in which only a small fraction of the population can participate with any sense of confidence). Therefore, a key distributive issue in Mexican politics may be the division of resources between the "free market" sector and those official institutions whose allocative criteria have more to do with the purchase of loyalty and the maintenance of social control. In practice, these two systems are closely enmeshed (and not sharply polarised as, for example, in Allende's Chile), so that direct clashes between them are--where possible--avoided, or muffled by compensating movements within each system. Nevertheless, one theme of the Echeverría years can be seen as the attempt to divert more resources from the free market into the political distribution system, and some part of the inflation and capital flight can be attributed to attempts by the market sector to resist or counteract this shift. The recession of 1977 reduced the resources available for distribution through either of these systems. Although the stabilization program appeared to contain assurances of a permanent shift towards free-market principles of distribution, that reflected the regime's transient weakness in relation to private wealth-holders. Once capital flight had been reversed and the scale of Mexico's prospective state-owned oil revenues became apparent, the political distribution system recovered some of its vitality. On this interpretation, a key distributive issue confronted by the present administration is to reach a viable accommodation between the two systems that will satisfy each as to its share in the coming oil wealth.

It would require too much space to expand on the foregoing interpretation, which is of course extremely schematic and oversimplified. It might be interesting to compare the economic consequences of Mexico's system for maintaining social control and support with that of a dictatorial alternative. My impression of the southern cone regimes is that they have dismantled the economic institutions that used to function in a somewhat Mexican manner, arguing that these were conduits for subversion, were starving the productive sectors of the economy (based on private enterprise), and had raised popular expectations that the country had no means to satisfy. Thus the political distribution system was dissolved, leaving free-market principles as the sole mechanisms of allocation. . . except that a substantial proportion of the population in all these societies would not voluntarily accept the economic fate dictated for them by the unfettered play of market forces. Therefore these governments espousing free-market principles still faced an urgent need to resolve the problem of social control, and to orchestrate their own sources of political support. In order to achieve these aims it was found necessary to divert resources from the productive system to maintain control through repression, and to purchase political loyalty.

Apart from any ethical considerations, what are the economic consequences of the southern cone formula, as I have outlined it here? Are there good grounds for the basic supposition of these dictatorships that fewer resources will be diverted from the free-enterprise (and by assumption "productive") sector of the economy when social control is maintained through repression rather than political distribution? In principle, both methods of containing pressures from below would become excessively wasteful and difficult to control. Is there any evidence that the southern cone formula is turning out to be less parasitic (i.e., destructive of underlying productive capacity) than the Mexican formula? This may be to frame in very narrow terms a set of alternatives that in fact have much broader moral and social implications, but perhaps it clarifies the way the alternatives have been apparently perceived in Mexico over the past decade. Whatever prescriptions Mexican policy makers receive for the correction of their economic disequilibria they cannot dismantle their system of political distribution unless they can find some other cheaper or more reliable way of maintaining social control. Is there any evidence that the southern cone formula meets even this minimum economic efficiency test, let alone any broader standard of justification?

At a slightly less aggregate level there are a series of politically significant distributive questions that might be relevant for comparative discussion. Space precludes me from case-by-case discussion of debtors versus creditors; exporters versus importers; productive versus financial enterprises; and the differential impact of policy on geographic regions and economic sectors. In all these cases my basic point is that the Mexican government has been sufficiently secure and responsive to a plurality of interests to maintain a degree of balance, and to prevent the emergence of outright winners and losers. This has of course been facilitated by the geographic concentration and administrative centralization so characteristic of Mexico. Another consideration is that many individuals belong to both gaining and losing categories, or have the possibility of shifting from disfavoured to favoured sectors. However, this relative fluidity and atomization is not characteristic of the two largest interests in Mexican society, organised labour and private enterprise. Therefore, their cases will be considered separately.

Organised Labour

We have seen that in September 1976 one of the major preoccupations of the IMF was that a floating (or rather sinking) Mexican peso might stimulate money wage demands that would make control over the public-sector deficit and the domestic price level impossible. An accumulative spiral of devaluation and domestic wage inflation was feared that would produce "radical changes in Mexico's economic and political system and her national objectives." "Perhaps the most difficult task" the Fund memorandum continued, "would be to convince people that previous wage increases had caused the loss of competitiveness, and to muster the political support to secure a reduction in average real wages." After the experiences of Chile in 1972-1973 and Argentina in 1974-1976, it was not entirely implausible to anticipate something similar in Echeverría's Mexico. Robert E. Looney has described the situation in the autumn of 1976 as follows:

> Shortly after the devaluation the government suggested guidelines for an emergency wage increase for organised labour. These guidelines called for increases of 23 percent. It was not clear, however, whether these wage increases were to be additional to, or inclusive of, any increases that had been obtained in collective bargaining sessions earlier in the year. For the most part the 23 percent increase appears to have been viewed as additional. Minimum wages were also increased 23 percent, effective October 1st. Simultaneously with the guidelines for wage increases, the government broadened its coverage of the price control program and issued a decree permitting a 10 percent increase in most prices subject to controls. . . . The combination of wage and price increases led many to suggest that Mexico was entering a more vicious inflationary spiral than had prevailed and that further depreciation of the peso exchange rate was likely . . . rumors began to circulate that bank accounts would be frozen, that foreign exchange controls would be imposed, that the government would nationalize the banks, and that a military coup was imminent.[19]

In the event, of course, none of these gloomy forebodings proved justified. Anyone who spent 28 pesos to buy each dollar in November 1976 made a bad bargain, for the rate has been stabilised under 23 pesos since a very early stage in the López Portillo administration. The new president had scarcely taken office before an agreement was reached with the leadership of the pro-government labour movement. During 1977, the upper limit on annually renegotiated wage increases would be 10 percent. In reality, strong unions may have obtained effective increases larger than that when the cost of <u>prestaciones sociales</u> is included, but controversy over the details need not concern us here. The broad picture is clear. When the exchange rate collapsed, organised labour received an emergency increase of over 20 percent--enough to compensate them for the anticipated effects of the devaluation, but not much more. Having accepted that from an outgoing administration which was in no position to do anything except buy time until the end of its term, organised labour then struck a deal with the new president that would help him overcome his initial weakness, and leave him beholden to the labour sector when, later in his six-year term, his capacity to satisfy labour demands would have been restored. Both in 1977 and 1978, the labour leadership accepted pay rises substantially lower than inflation as shown in the consumer price index. Virtually the entire labour movement fell in with this strategy, and although it produced some inevitable internal strains, these were much milder than most outside observers had anticipated. The incidence of strikes remained quite high by historical standards, but well below the peak reached in 1974 (see statistical record). And the currents of opposition to official leadership within the labour movement, that had grown in strength during the early 1970s, derived no benefit from the new situation. On the contrary, as far as I can determine, they become progressively weaker. All this gives considerable plausibility to the claims of Mexico's old-guard labour leadership that it is they who have effectively rescued the regime. The time for them to claim their rewards is now drawing near.[20] The autumn 1979 wage round may prove quite tense.

Whilst the recent record is extremely clear--and marks an almost unparalleled short-term success for Mexican "reformism," and for the principle of a formally negotiated "incomes policy"--there is no agreement whatsoever on how it is to be explained. No doubt workshop participants can provide an abundance of reasons why such arrangements would be politically impossible in the countries they have studied, or at least would break down within a period of far less than three years. One element that frequently seems to creep into such discussions is a suggestion that Mexican workers may have acquired less of a class consciousness than they "ought" to have. Alternatively, if this line of explanation seems uncharitable, heavy emphasis may be placed on the corruption, gangsterism, and generally authoritarian structure of Mexican labour organisations. No overall verdict can be given here, but a few broad generalizations may be of interest for comparative discussion.

First, within the Mexican historical tradition there is nothing very surprising about the labour movement's strategy of response to the 1976 crisis. Very similar policies were applied (although with a much greater element of corruption and ruthlessness) by Luis Morones and the CROM as long ago as the 1920s. The government-union-business pact of 1977 has considerable similarities to the Pacto Obrero-Industrial of April 1945, which was even negotiated by essentially the same labour leadership. Equally well, Mexican labour responded to the devaluation of 1954 with very similar discipline to that displayed in 1976-1977. Thus expectations of a South American-type wage-price spiral overlooked the importance of Mexico's very different historical and institutional traditions. One part of this tradition is that at the beginning of each presidential term the labour movement has learned to expect a bout of austerity, and has also learned not to over-react during those political cycles. So long as it retains influence with the government, the damage will be limited and patience will be rewarded in the next upswing.

Secondly, although some prominent Mexican labour leaders may indeed be outright gangsters, this characteristic is not unknown in the labour movements of other countries, nor is it sufficient explanation, on its own, for acquiescence in a strategy of wage restraint. Several of the more observant writers on Mexican trade unions have pointed out that most successful labour leaders combine astuteness in the manipulation and control of their membership with a fair degree of alertness and responsiveness to the demands and expectations of their rank and file. José Luis Reyna, for example, argues that "in a political system of the Mexican type no labour or wage policy can be indefinitely sustained against the wishes of the working class sectors." Others have shown the existence of a significant degree of internal democracy within various major trade unions. The "control from above" (charro) versus "control from below" (independent) dichotomy was too crude even at the height of the Cold War. Since 1968, the interplay between these two idealised forms of labour organisation has become more complex, more varied, and more subtle.

Thirdly, then, the beliefs and expectations of Mexican union members have been important in facilitating the process of stabilization. How are these beliefs formed, and why do they apparently differ from the attitudes of labour activists in South America? Here are a couple of arguments that are apparently widely propagated (and accepted) within the Mexican labour movement, more so perhaps than elsewhere in Latin America: (i) Generalised full employment is unattainable for the foreseeable future, whatever the political regime. Therefore, with the help of the government, unions give their members job security, which is a valuable privilege. Union members who do not understand their tacit bargain with the government put their privileges at risk. (ii) Through reformist collaboration with the authorities, it is possible to make steady progress in achieving working-class objectives. Revolutionary mobilisation would put in jeopardy the considerable gains already made.

Is it lacking in class consciousness to find such arguments persuasive? An alternative interpretation would focus on the manipulative skills of the political elite (including key elements of the union elite). In a country with Mexico's traditions of both exploitation and revolutionary struggle, it is remarkable that they have created an institutional system within which such arguments can carry conviction.

The Private Sector

Many would say that the long list of distinctively Mexican features and political arrangements emphasised in this paper are of secondary importance. The fundamental reality is that dependent capitalism prevails in Mexico, determining the pattern of its internal economic and social development, and the character of its international relations of exchange. President Echeverría may have entertained some populist illusions about the scope for reshaping these realities by acts of political assertiveness, but on this analysis the real lesson to be drawn from his efforts is that the logic of capitalist accumulation leaves no real scope for political experimentation. Short of a complete mobilisation of society against the existing economic system, half-hearted gestures of reformism only lead to capital flight, political paralysis, and the retribution so invariably administered by the IMF. Some international comparisons can clarify some of the implications of this position.

The example of Cuba has made perfectly clear the meaning of a "complete break" with the capitalist system. Both those favouring the idea, and those threatened by it, have been alerted that it is possible in Latin America, and that the repercussions are very far-reaching. In all the countries under consideration in this workshop, the Cuban alternative has exerted a significant influence, reshaping socio-political attitudes both on the left and on the right. Only in one case were the admirers of Cuba strong enough to directly attempt a socialist transformation of the economy, and even in that case (Chile) the intended structural changes apparently envisaged only a radical renegotiation of the relationship between public and private sectors of the economy, and not the eradication of the latter. Nevertheless, Chilean private enterprise (both domestic and foreign-owned) reacted as though faced with extinction, closing ranks, becoming much more intensely politicised, and eventually uniting around a long-term political and economic project that is intended to consolidate the ascendancy of private ownership, and to provide firm guarantees against any resurgence of the socialist danger. This example naturally has a strong attraction for leaders of the private sector in other Latin American countries, especially those in which the Cuban alternative has an active following, but also in any country where the government is not a reliable supporter of business principles and interests. In Uruguay and Argentina, private enterprise now appears to form a major pillar of the dictatorship, determined to prevent any resurgence of populist or labour radicalism. Perhaps something similar could attract much business support in both Jamaica and Peru if a favorable opportunity presented itself.

Now, reverting to the Mexican case, the question becomes whether a significant degree of variation from this pattern is attainable by political means. Or is the logic of private accumulation entirely inflexible? If forced to choose between a "mixed" economy (with a secure place for private enterprise) and a centrally planned economy, there is no question that Mexico's business interests would respond with total inflexibility, and would carry their policies to the same extremes as can be observed in the southern cone.[21] However, a realistic socialist alternative has never presented itself in Mexican history, and I would argue that the political and social basis for it is still lacking. My account of the labour movement has already highlighted one major contrast with South America; even the famous opposition movement of 1968 was based more on liberal than on socialist ideals; the legacy of the Mexican Revolution is highly favourable to "national" capitalism; and anyway the anticipated U.S. reaction would cause all waverers to desert at the first confrontation.[22] Although important business spokesmen denounced Echeverría's administration as though it were on the same path as Allende, I strongly doubt that they really believed this claim. Carlos Tello is quite convincing when he argues that the practical effects of most Echeverrista economic reforms would be favourable to the long-term development of Mexican capitalism, however much business lobbies protested in the short run. Indeed, some aspects of the present economic boom are testimony to the pro-business elements in Echeverría's legacy.

Even though Echeverría's administration may really have aimed at little more than an improvement in the functioning of the "mixed" economy and the re-establishment of popular confidence in Mexico's reformist institutions, the record makes clear that this stirred strong and effective resistance from the private sector. By the end of his term, the Mexican authorities were faced with a bloc of business interests more extensively organised and outspoken than ever before. Furthermore, President López Portillo was left in no position to bargain effectively with this sector; he had to offer whatever assurances and concessions they might require in order to "restore confidence" and lure back the capital that had fled to the United States.

This provides a vivid illustration of the most important source of private-sector leverage over Mexican economic policy making. Not even a Cuban-style government in Mexico City would be capable of imposing exchange controls strong enough to contain "dollarization" and massive contraband over the U.S. frontier. Geography allows no alternative to voluntary incentives if private savings are to be retained in Mexico. The greater the domestic insecurity, the higher the post-inflation differential over U.S. interest rates that Mexican wealth-holders can demand. No formal organisation is required to present these demands to the authorities, so there are no effective business intermedians for the government to co-opt or control. This unspoken reality drastically and permanently restricts the scope for income redistribution. It is easily concluded that in Mexican politics private enterprise really holds the whip hand. Many Mexican businessmen appear to have reached such a conclusion. At any rate, since Echeverría the private sector's confidence in its own capacity and resources has been strengthened, and any previous inclination to trust the government has been eroded. Although it has frequently been argued that modern Mexican capitalism was "created" by the post-revolutionary state, it seems clear that much of the private sector is no longer very inclined to rely on official tutelage. Over the long term, it may have a growing capacity for "hegemony." At any rate, Echeverría's attempt to renegotiate the balance between business interests and the other politically organised groups that had felt left behind during the 1960s was essentially a failure. Indeed, it proved counter-productive.

This observation leads to some very broad questions about the scope and limits of Mexican reformism which will be set out in the conclusion. On the more specific issue of relations with the private sector, only a very tentative assessment is possible. Against the view that Echeverría's experience shows how little "political autonomy" the authorities enjoy, others argue that this was not a representative test. There was much clumsiness and many misjudgements creating conflicts where these were unnecessary. With more skillful political management, and the more favourable environment provided by the prospective oil revenues, the Mexican authorities can still, according to this view, reassert effective leadership over the private sector, and steer it towards collaboration with a socially progressive and reformist strategy of development.

One interesting recent episode is quite illustrative of the "political management" approach. When the Association of Mexican Bankers issued a statement of self-congratulation, describing themselves as the "saviours" of the economy during the 1976-1977 liquidity squeeze, this must have been seen as encroachment on the government's territory. Soon official spokesmen began explaining that what really kept the country going through the economic and social collapse of 1976 was the country's revolutionary institutions. To underline the point, labour leaders revived one of their standard instruments of pressure, a demand that bank employees be allowed their constitutional right to join trade unions.

This confirms that the Mexican regime still possesses many resources for containing the pretensions of the business elite. The private sector can be kept divided against itself, dependent on official patronage, and liable to sharp retaliation if it steps outside the established framework in political matters. But of course the reason why so many businessmen have been willing to accept these restraints and to operate within the established framework is that, in general, the established framework has worked so well for them, and has proved so permeable to private-sector interests. Even under Echeverría, when an attempt was made to reduce this degree of permeability, all these institutional restraints on business power were operated within a capitalist economic context. In view of that, it may be argued that such narrowly political devices are of no basic importance. However, in countries where they are lacking they can be sorely missed.

The Impact of Oil

There is an alternative line of interpretation, that would also give priority to "economic necessity" as the essence of social explanation and would downplay the political factors I have been stressing. This interpretation would explain the distinctiveness of Mexico's experiences with stabilization very largely as a function of her oil finds. The record can be outlined from the official figures on proven oil reserves. Almost stationary throughout the 1960s, these reserves were put at only 2.8 billion barrels at the end of 1972, by which time Mexico was beginning to be a net importer of hydrocarbons. However, the "Reforma" finds began in May 1972, and discoveries have built up on an accelerating scale ever since. At the end of his presidency, Echeverría admitted to only 6 billion barrels of proven reserves, but much larger figures were widely accepted. López Portillo began his presidency by announcing proven reserves of 11 billion, uprated by 1978 to 20 billion, and on January 1, 1979 upgraded again to 40 billion--the sixth largest proven reserve in the world, after Kuwait. Eventually, it is thought, the total may even rival Saudi Arabia.

Of course this is of huge long-term significance for Mexico, and perhaps even for the world economy. But how much does it explain of the economic record of the 1970s? Without these finds, oil imports would have become a significant active burden on the balance of payments from 1974 onwards, in that respect aggravating Echeverría's problems. On the other hand, because of these finds, his administration greatly expanded this item of public expenditure (PEMEX's investment expenditure rose from $380 million in 1972, to $1,560 million in 1976, to about $3 billion in 1978). So far it is doubtful whether even the net effect on the current balance has been positive (e.g., the 1978 increase in petroleum exports of $0.8 billion was exactly offset by the cost of imported steel tubes for the gasoducto). The short-term effect on the public-sector deficit and the scale of external public indebtedness has been a significant negative. Therefore, the claim that Mexico's economy has already been transformed by the oil prospects rests essentially on the effects on "confidence" and "expectations."

Here, however, questions of political management again become significant intervening variables, clouding the simplicities of any geological or even economic determinism. The first big finds were made in 1972, and many bankers and oilmen had a fair idea of the magnitudes involved before the 1976 financial collapse. Nevertheless, Mexico failed to inspire any degree of foreign confidence: (i) because its government was so secretive about these finds, (ii) because Mexican politics seemed so turbulent and unpredictable, and (iii) because it was thought that the benefits of oil development were very long-term, whilst the problems in the rest of the Mexican economy (which will always account for over 90 percent of total output) were very pressing and intractable. As we now know, the first two of these negatives were transformed into major positives within a very short time after Echeverría's departure. That was achieved because of the political resources made available by the Mexican system. The third reason for withholding confidence from Mexico has not disappeared; it is just perhaps overlooked in the present administratively induced euphoria.

Conclusion: The Scope and Limits of Mexican Reformism

What constitutes successful "stabilization" of an economy, or effective "adjustment," in the international environment of the late 1970s? Not even Switzerland still aims for zero increase in the overall level of domestic prices, for when, alone among the nations of the world, it did attain that goal, the result was to induce an inward flight of speculative capital so unmanageable that the exchange rate soared out of control and the level of industrial employment became unsustainable. In the countries considered in this workshop, the most ambitious inflation target now imaginable would be 10 percent a year--signifying an exchange rate stable with the U.S. dollar. Other stabilization objectives are equally pragmatic accommodations to an essentially unstable economic setting--e.g., a public-sector deficit that can be financed voluntarily without excessively high interest rates, a disproportionate expansion of the money supply, or unsustainable amounts of foreign borrowing, where the definition of "acceptable" magnitudes is no longer clearcut. The old benchmarks given by exchange-rate fixity and low global inflation have disappeared, leaving far more scope for subjectivity and more reliance on such semi-psychological intangibles as "confidence" in the currency, and "low expectations" of inflation based on "sound" economic management. These terms refer, of course, to the subjective attitudes of wealth-holders, bankers, Fund managers, and the like, who on these questions shape the views of society as a whole. In these matters of "confidence" and "expectations," opinion is weighted on the basis of one-dollar/one-vote, not one-man/one-vote. In the Mexican case, this electorate passed a massive vote of "no confidence" in Echeverría's exchange-rate policies, and expressed the expectation that inflation could easily soar into the stratosphere. Not a surprising verdict, one might say, given the "objective" situation in 1976. In 1978, however, the same electorate expressed unrestricted confidence in the new exchange-rate policy, and effectively voted that, under López Portillo, inflation could be expected to continue to decline. In the short run, such expressions of confidence are themselves self-fulfilling, of course (like the previous expressions of no-confidence), but not in the longer run unless validated by the real economy. The economic indicators themselves had not changed so much between 1976 and 1978 (see the statistical record). A few years ago, most investors would have scorned any claim that Mexico had successfully "stabilized" its economy even though inflation was still moving at close to 20 percent, the money supply was expanding at the fastest rate in 30 years, the foreign debt had risen a third in two years, and the public sector deficit remained above 6 percent of GDP. It is not just the presence of the IMF, or the prospects of oil, that has changed their opinion of what constitutes "successful" economic management (it may be wiser to avoid labelling the present Mexican economy "stabilized"). It is also the observation that by almost any test most other economies are performing much worse than the Mexican economy; and in addition there is the belief that if unforeseen developments occur the Mexican authorities are sufficiently secure, accessible, and responsive to manage the economy along the lines that Fund managers would favour.

To construct the confidence and favourable expectations required for the successful management of a "mixed" economy requires effective and stable political institutions, and a type of political leadership consciously directed towards good relations with the private business constituency. This paper concludes with some comments about the political ingredients required to create such confidence, and what the Mexican case suggests about the scope and limits for "reformism" when operating within the currently existing pattern of economic constraints.

In general, there are important connections between the structure of economic expectations and the management of political power. This point is sometimes overlooked by economists who consider only market forces that might shape expectations. It can be illustrated by reference to the two historically most important "causes" of inflation--war and revolution. Both are uncontrollable political processes in which, for a while, the pressure for public expenditure outruns the resources that can be transferred to the authorities through regular taxation and borrowing. While these processes are in train there can be no rational basis for confidence in the currency, and when this is realised strong inflationary expectations will develop. How are such expectations subsequently broken so that price stability may be restored? Political acts, such as the signing of a peace treaty, the consolidation of a stable post-revolutionary government, and so on, have often powerfully affected inflationary expectations. This is very over-simplified, of course, and such purely political acts may need reinforcing by more technical-looking measures like the strengthening of the central bank, a return to the gold standard, or the implementation of a currency reform. Although such measures may be presented in highly technical terms, and although their technical rationality may be of great importance to their success, they will in fact only work if the society is convinced that the government has the strength and determination to uphold and enforce the reformed economic system, even in the face of unexpected resistance or severe shocks. Therefore, _in extremis_, the basis of economic confidence always rests with (or can be disturbed by) the management of political power.

However in the cases considered in this workshop it was not war, or even full-scale revolution, that undermined the stability of economic expectations. Participants may wish to assess the importance of questions of political management in destabilizing expectations, and--if such factors were significant--why they occurred and how much scope there might have been for minimising them. Finally, once expectations have been destabilized to a serious extent, what are the political preconditions for the re-establishment of a necessary minimum of economic "confidence"?

One simple theory which used to be very popular was that the existence of powerful and irresponsible labour organisations had prevented weak Latin American governments from containing cost pressures, correcting sectoral distortions, or controlling their budget outlays. However, now that we can observe various cases where labour organisations have been physically crushed or tamed for a number of years, we find that inflationary expectations have not generally responded to the extent predicted by this theory. One hypothesis to explain these disappointing results is that, as a consequence of the effort to destroy the labour movement, those social groups most hostile to the left (including the repressive apparatus, and various financial interests) have acquired as much influence over the budget, and as much capacity to create allocative distortions, as the labour sector ever enjoyed even at its most assertive.

My interpretation of the role played by the Mexican labour movement would also suggest that in some circumstances the existence of a powerful and disciplined intermediary between government and workers may offer important opportunities for political negotiations that will (for a critical year or two) reduce labour pressure and thus facilitate the restoration of confidence in the currency.

More generally, it would seem that throughout Latin America there has built up a degree of distrust of the political steadfastness of the economic managers. In these circumstances, the variable that seems to influence economic expectations more powerfully than any other is the free-market rate of exchange with the dollar. For example, so long as Echeverría succeeded in maintaining the conviction that the Mexican peso would not be devalued during his term of office, he enjoyed a certain margin of maneuver in the selection of his domestic policies, and Mexican economic expectations remained "unreasonably" stable. When his political authority began to wane, towards the end of his term of office, confidence in his pledge of exchange-rate stability declined as well, and once he was forced to withdraw support from the currency his popular credibility (and therefore his capacity for political negotiation) was totally destroyed. In the Mexican political cycle, however, a tremendous new surge of political confidence occurs with absolute punctuality every six years. López Portillo has kept the dollar freely convertible at an almost unvarying rate since February 1977, and this has recreated a certain margin of maneuver within which the Mexican authorities can select their domestic priorities. It has also conferred the inestimable advantage--at least for the time being--of an "unreasonably" stable climate of economic expectations. There has been a rather direct correlation between the stability of Mexican economic expectations and the country's six-year presidential cycle.

On these arguments, the Mexican system of economic management is likely to emerge quite favourably in any comparisons with other Latin American countries, for the same reasons that the Mexican political system looks comparatively attractive. But then it must be said that, in terms of economic performance (with the exception of Brazil), we are comparing Mexico with distinctly unsuccessful countries; and in terms of the stability and responsiveness of political institutions, only Jamaica offers the Mexicans any significant competition. In any case, the relatively favourable elements this paper has identified in the Mexican political system obviously cannot be transferred to other countries. Furthermore, many Mexicans would say that their country still faces such grave and intractable social problems that there are no grounds for complacency that the misfortunes of others can be warded off at home. It is in this context that any comments on the relative success of the Mexican "reformism"[23] must be situated.

Workshop participants were asked to consider the extent to which major disequilibria could be corrected within a reasonable period of time while minimizing the accompanying damage to a country's social and political fabric. By softening the usual criteria of effective "stabilization," and introducing the more imprecise and subjective idea of "inspiring confidence," Mexico's recent successes in correcting the disequilibria of 1976 can be put in the most favourable light. However, as argued above, the need to maintain private-sector confidence limits quite narrowly the alternatives available within this overall framework of Mexican "reformism." Private wealth-holders may accept the Mexican political formula so long as it is managed with great restraint, and slanted in their favour. But the moment there is doubt about the fulfillment of those conditions, their influence begins to swing against any degree of "reformism." Given the social conditions of contemporary Mexico, it may require a constant effort to persuade them that their interests would not be better served by a pro-business dictatorship. How much scope does that leave for "preserving the country's social and political fabric"?

The "social fabric" metaphor was chosen to be deliberately vague because different workshop participants will start from different assumptions about the sources of social conflict and social cohesion. My personal approach would be to distinguish between three senses in which economic-stabilization processes might "damage the social fabric": (1) The economic-resources base of the social fabric might be eroded or undermined. There are signs that this may have happened in the Uruguayan stabilization (although the decline of the Uruguayan economy has a long history), and in Chile. It is clearly feared in Jamaica and Peru, but has been successfully avoided in Mexico. (2) The political and legal framework for non-violent conflict resolution may be impaired, resulting in more naked struggles for power, and more pitiless treatment of the powerless. This is the "southern cone" experience, perhaps most striking because until recently those countries lived under remarkably sophisticated and apparently resilient political institutions. Jamaica still struggles to preserve institutions of the more civilized kind, although their credibility is being eroded by the economic strains. Mexico, of course, has suffered acutely from violent struggles for power over many decades, and has gradually developed its institutional framework to overcome that legacy. Mexico's leaders have been willing to pay a considerable price in terms of "sound" economic management to preserve that institutional system, and understandably so. I have explained the disequilibria experience under Echeverría substantially in terms of the need to "re-legitimise" these institutions after 1968, a task in which I consider him (despite everything) quite successful. This is a priority that remains of first concern to his successors. (3) Despite an expanding resource base and effective political institutions, stabilization policies may produce such unacceptable distributive effects that grave long-term social damage results. On this count, Mexican society is not so well-favoured. Internal inequalities are already so great, demographic pressures are already so fierce, and the underlying structural problems (agriculture, water supply, pollution, etc.) have already built up so far that almost no margin remains for distractions or mistakes. However mild the recession of 1977 may look to outside observers, it added to problems of youth unemployment that were in any case accumulating at an unprecedented rate. The list of other socially damaging consequences of Mexican inflation and the resulting stabilization would take a long time to enumerate.

In summary, therefore, although Mexico's "reformism" emerged more successfully from these trials than it was reasonable to hope, substantial underlying damage to the social fabric was sustained, and the resilience of the political system will be tested to the limits by the social problems still confronted by the world's most populous hispanic republic.

STATISTICAL RECORD

	1970	1971	1972	1973	1974	1975	1976	1977	1978
Annual Percentage Increase:									
National consumer price index	5.0	5.4	5.0	12.1	23.7	15.0	15.8	29.1	17.4
Mexico City wholesale price index	6.0	3.7	2.8	15.7	22.5	10.5	22.2	41.2	15.8
Money Supply (Dec/Dec)	10.5	8.3	21.2	24.2	22.0	21.3	30.9	26.6	31.7
Real GDP	6.9	3.4	7.3	7.6	5.9	4.1	1.7	3.2	6.6
Percentage of GDP consisting of:									
Consolidated public sector deficit	1.9	2.5	4.5	6.0	6.3	8.6	9.6	7.5	6.4
Gross fixed investment	19.7	18.0	19.1	20.4	21.3	22.4	21.9	20.3	(22+)
Current account deficit	2.8	2.8	1.9	2.4	3.9	5.3	4.0	2.0	3.0
Balance of Payments data (in billion dollars):									
Current account (- is deficit)	-0.9	-0.7	-0.8	-1.2	-2.6	-3.7	-3.0	-1.6	-2.5
Errors and omissions (- is outflow)	+0.5	+0.2	+0.2	-0.4	-0.1	-0.5	-2.5	-0.5	+0.1
Net external public debt (end year)	4.3	4.5	5.1	7.1	10.0	14.4	19.6	22.9	26.3
Merchandise imports	2.3	2.3	2.7	3.8	6.1	6.6	6.0	5.8	8.1
Merchandise exports	1.3	1.4	1.7	2.1	2.9	2.9	3.3	4.5	5.8
(of which) petroleum exports	-	-	0.1	0.2	0.3	0.4	0.6	1.0	1.8
Peso/Dollar rate (annual average)	12.5	12.5	12.5	12.5	12.5	12.5	15.4	22.6	22.7
Legally recognised strikes (year to Aug)	n.a.	36	30	57	452	104	102	173	n.a.

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[1]See my article reviewing recent literature on "The Politics of Inflation" in Political Studies (Oxford), forthcoming 1979.

[2]The last three of these contentions are argued more fully in my paper on "The Economic Policies of the Echeverría Sexenio: What Went Wrong and Why?" delivered at the Latin American Studies Association meeting in Pittsburgh, April 1979. See also Soledad Loaeza, "La Política del Rumor--Mexico, Noviembre-Diciembre de 1976," in Las Crisis en el Sistema Político Mexicano (1928-77) (El Colegio de Mexico), 1977.

[3]Redvers Opie, "The Achievements of the Mexican Economy in 1969, and Future Prospects," CAMCO, Mexico City, March 1970, p. 11.

[4]E.V.K. FitzGerald takes this line in "Stabilisation Policy in Mexico," in R. Thorp and L. Whitehead, eds., Inflation and Stabilisation in Latin America (London: Macmillan, forthcoming).

[5]See "The Economic Policies of the Echeverría Sexenio," op. cit.

[6]Rene Villarreal, El Desequilibrio Externo en La Industrialización de Mexico (Mexico City: Fondo de Cultura Económica, 1976), p. 202.

[7]Confidential text subsequently leaked in El Heraldo (Mexico City), November 21, 1977.

[8]This text was also leaked to El Heraldo (ibid.) and has been retranslated here.

[9]Ibid. It is interesting to contrast the postures of the two sides in 1976 with their relative positions in 1954. The Mexican authorities had then decided on a 31 percent parity change to head off a movement of speculative capital that might otherwise have wiped out their free reserves. The IMF was concerned that this devaluation was proposed at such short notice, and considered that the proposed parity change might be too large. Several members of the Board asked the Mexicans to consider a less severe devaluation, or the reversion to a floating rate (as in 1948). But the Mexican spokesman pointed out that in the special conditions of his country the usual remedy for short-term capital outflows (the imposition of exchange controls) was impractical, and insisted that nothing less than the 31 percent devaluation would suffice. It had to be large enough to provoke a backflow of capital, and to meet the country's needs for some years hence. The U.S. representative warned of possible retaliation by his country if unfair competition resulted from the devalution, and in general the Directors expressed a similar concern, but finally the Fund concurred with the Mexican proposal, recognising that no alternative was open. J. Keith Horsefield, The International Monetary Fund 1945-65 (Washington, D.C., 1966), Vol. II, pp. 106-107 and pp. 379-380.

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[10]Thus, for example, according to one Jamaican official involved in the February 1978 negotiations with the Fund: "They never told us specifically what policies we had to follow to qualify. All they would say was 'You show me what you want to do and I'll tell you if it's correct.' By the end we were pleading with them, 'Please just impose your conditions and be done with it.' But they said Jamaica had to make up its own mind." The Guardian (London), September 6, 1978.

[11]El Heraldo, op. cit.

[12]Ibid.

[13]The memorandum stated that "despite the widespread impression in Mexico that wages and related benefits are a secondary factor, because they amount to only one third of national income, wage inflation would appear to be the proximate cause of Mexico's loss of competitiveness. . . . After a long period of wage restraint labour costs rose rapidly from 1972 onwards. Since then minimum wages doubled, labour contract increases came to almost two thirds . . . whilst by historical standards the increase in labour productivity has been low . . . and it will be useless to expect the necessary reduction in government expenditure as a share of GNP without restraint on wage increases. After all, the wage bill under budgetary control amounts to about one quarter of Mexico's total labour income." (My emphasis).

By contrast Carlos Tello argues that, "taking 1970-6 as a whole there was virtually no change in real wage levels. If we take into account growing under- and unemployment it is very likely that the average real income of the working class (or the share of wages in total income) fell over those years." "La Economia Echeverrista" Nexos (Mexico City) Year 1, No. 11, November 1978, p. 9. (Unless the wage element in total costs had risen, it would be very misleading to describe nominal wage rises as "the proximate cause" of lost competitiveness).

In order to sort out these polemics it would be necessary to distinguish between three very different issues: (i) what happened to average real take-home pay per regularly employed worker, (ii) what happened to aggregate labour costs as a share of GDP, and (iii) whether the expansion of public expenditure as a proportion of GDP was attributable to the rise in remuneration per public employee, or the increased numbers on the public sector payroll, or to an expansion in other types of public spending. My tentative impression is that the pre-tax income of the most successful union members (oil-workers and mineworkers) rose substantially faster than money per capita GDP 1970-1976, and then fell back significantly in 1977. After tax the improvement per worker would be quite modest even here. The least successful union members (railway employees) must have faced a substantial decline in real take-home pay over this period. Intermediate categories of workers were only modestly ahead even at the peak of their success (1974). The wage component of public expenditure rose far faster than this, however, because of the huge increase in the numbers employed (e.g., a 70 percent rise in the number of primary teachers).