The Mexican Economy Since the Tequila Crisis

On December 1, Mexico's first nonruling party president in more than seven decades will take office. Vicente Fox Quesada, a member of the center-right National Action Party, will face a host of challenges in the areas of banking and finance, worker and capital productivity, and taxation.

Much has been made of Mexico's rapid growth since the so-called Tequila Crisis of 1995. In the last five years, Mexican industrial production growth has outstripped that of any other major Western Hemisphere country, including Argentina, Brazil, Chile and the United States.

But the principal engine of this growth has been exports. Mexican consumption growth has significantly trailed production growth. In addition, small and medium-sized nonexporting firms have seen far less expansion than the big exporters. The lags in domestic consumption and in expansion by the smaller nonexporting firms have similar roots. The large export firms have access to foreign credit, while Mexican consumers and small to medium-sized producers must rely on credit from Mexican banks—and these banks have cut back on their lending. While bank loan activity has had its ups and downs since the Tequila Crisis, the real value of bank loans has generally been down, especially since 1998 (*Chart 1*).

Vicente Fox has proposed financial programs to address credit availability for small to medium-sized firms. For one, he suggests a Grameen-style bank to provide credit to small borrowers. The first Grameen bank, located in Bangladesh, represented a highly successful approach to lending for very small business operations. Fox developed his own brand of Grameen banking in his home state of Guanajuato and hopes to take his operation national.

Although many Americans have heard of Mexico's high growth over the last five years, fewer realize that Mexico has experienced very little economic expansion per person over the last two decades. Between 1981 and 1999, total Mexican GDP per capita grew only 6.8 percent—not per year, but over the entire period. During the same time frame, U.S. income per capita rose 48 percent.

To further complicate matters, Mexican income distribution has become increasingly uneven over the last 15 years. Income disparity in Mexico exceeds that of the United States as well as Ecuador, El Salvador and Bolivia. Thus, Mexico's challenge is not only to raise real income per capita but also to create opportunities so that its poorest share in the increase. If that is not possible, political pressures may militate against the very measures Fox believes are most likely to increase income per capita.

An important aspect of creating a basis for growth in income per capita is raising education levels. Compared with industrial countries, some Asian tigers and even Brazil and Chile, Mexico's average education level is low. Similar comparisons can be made with other social indicators. Mexico's infant mortality, for example, is markedly higher than that in Argentina and Chile, not to mention Korea, France and the United States.

Fox believes he can make labor and capital more productive by investing in education and infrastructure and increasing social spending. He wants to broaden tax coverage by bringing Mexico's large informal sector into the taxpaying fold. This would allow the government to increase spending without further taxing the formal sector, which currently bears the fiscal burden.

So far, Mexico's new administration looks as if it will emphasize government's relationship to the public more as a channel for investment in human skills, capacities and infrastructure than as a medium for income redistribution or other populist measures.

—William C. Gruben

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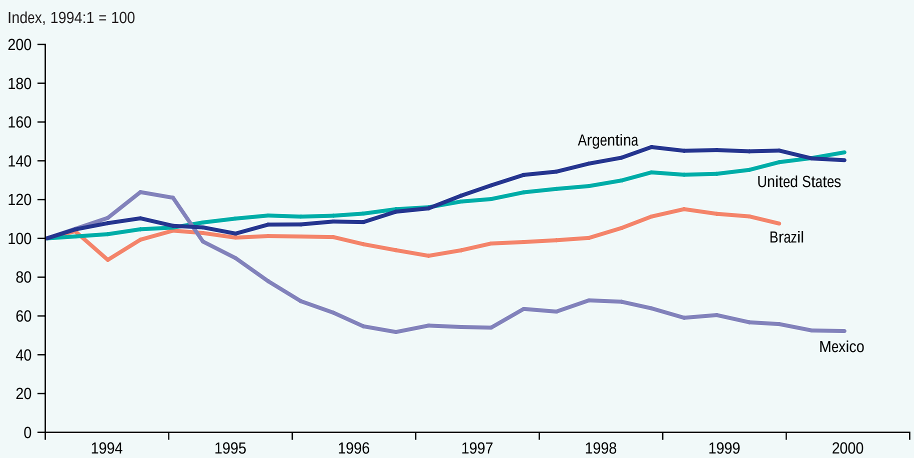
Chart 1

Mexican Bank Lending Falls

(Real commercial bank loans to the private sector, deflated with CPI)



SOURCE: International Monetary Fund, *International Financial Statistics*.