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*Unequal Partners: The United States and Mexico*

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The book on the United States and Mexico with the title listed above was launched on April 12 at the Center for Strategic and International Studies. I trace how each country's policy was made toward the other -- one country dominant economically, and the other dependent on the other for its market and as a destination to which its nationals flee to seek greater opportunity. The fact that the two countries are neighbors makes the relationship more than one of asymmetry -- this is true of most countries with respect to the United States -- but a reality that adds dependence and dominance to the equation. Other pairs of countries in which asymmetry of neighbors led over an extended period to dominance-dependence relationships included Germany/Poland and Japan/South Korea.

The book's discussion traces the pattern of mutual policymaking in six areas: trade; investment and finance; narcotics; energy; migration; and the border. The objective of the book is to demonstrate that policy-making from a dependency-dominance perspective leads the two countries more toward talking past one another rather than understanding each other. I argue that the more the two countries relate to each other as sovereign equals -- despite the economic inequality -- the more both will benefit. Discussion as sovereign equals already has taken place in some activities such as trade and investment, is moving in that direction at the border, but interaction remains much as it has been for decades in dealing with narcotics, migration, and energy.

Mexico practiced import substitution for much of the post World War II period, derived development benefit from this for a while, but retained this policy of keeping out foreign (read U.S.) goods long beyond its useful life. Consequently, there was little give-and-take on trade issues between the two countries. Why try to discuss trade policy when the Mexican authorities felt there was nothing to discuss? The change came in 1982 when the Mexican economy collapsed and the authorities quickly recognized what its economists had been saying for more than a decade, that Mexican trade policy was short-sighted in not exploiting the U.S. market, something that required reciprocity by allowing more U.S. goods to enter Mexico. Mexico, in 1984, joined the General Agreement on Tariffs and Trade, the global trading organization that Mexico had refused to join a few years earlier. The change

in trade policy went further when Mexican President Carlos Salinas de Gortari proposed what later became the North American Free Trade Agreement (NAFTA). The United States welcomed these changes in Mexican trade policy.

Similarly with respect to direct U.S. investment: the relevant legislation dating from the 1970s was based on promoting domestic investment while limiting foreign direct investment (FDI). Modest amounts of U.S. FDI were made, but the terms and conditions of proposed investments were subjected to negotiation to determine if they benefited Mexico. This was a perfect setup for bribery--permission generally would not be granted without a payoff. Mexico decided that projects could be financed more cheaply by borrowing from foreign sources rather than increasing FDI because even though the debt had to be serviced and repaid, an endless stream of dividends to foreign investors would not be necessary.

The economic problems of 1982 were precipitated by a debt crisis -- the Mexican authorities came to Washington to ask the International Monetary Fund and the U.S. government to delay debt repayments. Policy was rapidly changed, and FDI was actively sought. Just as Mexico's imports and exports grew after import substitution was jettisoned, so too did FDI into Mexico after the policy was changed. FDI into Mexico grew further after NAFTA went into effect. To stop the bribery associated with negotiated approval, Mexico made investment approval automatic unless there were specific problems that needed to be addressed. Thus, there were two 180° policy shifts after 1982.

In 1991-92, the Mexican government decided to sell the banks that it had nationalized ten years earlier, and it wanted to get as much as it could from this reprivatization. And it got high prices. The weighted average bid-to-book ratio was 3.04, compared to a ratio of 1.89 when the United States sold financial institutions in the 1980s. Foreign banks were not allowed to compete in these auctions--only Mexican investors could. Many of the banks were sold to persons and groups with little banking experience. Payments for the purchases came in some cases from money borrowed from the same banks. Bank lending at high interest rates soared as buyers sought to recoup their outlays to acquire the banks, but deposits into the banks lagged. By 1995, it was

clear that the government had to rescue the reprivatized banks—at a cost of at least 15 percent of Mexico’s gross domestic product. In early 1995, the government removed restrictions on foreign ownership of Mexican banks—something it had refused to do in the reprivatization process and when negotiating the banking provisions of NAFTA. Today, all large banks in Mexico save one (Banorte) are foreign owned. Again, a 180° turn in economic policy.

A fourth precipitous change occurred at the end of 1994 when the central bank found itself with scant foreign reserves because they had been used to prop up the value of the peso. President Salinas chose not to devalue the peso during his term in office. Instead, the authorities sold tesobonos—peso debt with a dollar guarantee. When the holders of the tesobonos, both Mexican and foreign, tried to cash them in, the Mexican authorities realized that they had no way to maintain a fixed exchange rate with meager foreign reserves and no way to roll over the tesobono debt. The decision was made to allow the peso to float.

The key aspect of bilateral narcotics interaction was the U.S. refusal to take any responsibility for drug shipments from Mexico for consumption by users in the United States. The United States instituted a policy in the mid-1980s of decertifying countries judged as not cooperating in combating narcotraffic; the penalty for lack of certification was cessation of U.S. direct aid and U.S. opposition to loans to these countries by multilateral development banks, such as the World Bank. Mexico was never decertified, but every year there was a minor drama as the list of delinquent countries was drawn up. In 1965, inspections of vehicles crossing the border had been intensified in what was called Operation Intercept, deliberately delaying the movement of Mexican exports in order to send the message that Mexico would be punished for lack of full cooperation in dealing with drug shipments to the United States. This was repeated in 1985. It was not until March 2009, during her first official visit to Mexico as Secretary of State, that Hillary Clinton conceded what was abundantly evident to everybody outside the U.S. government that the “insatiable [U.S.] demand for illegal drugs fuels the drug trade.”

The struggle among large drug marketing organizations for greater access to the lucrative U.S. drug market, worth somewhere between about \$20 and \$40 billion dollars a year, has led to an estimated 20,000 murders in Mexico over the past three years. Most of those killed have been drug dealers, but victims also included government officials, police, and innocent bystanders. There was speculation from U.S. sources that Mexico was becoming a “failed state” because of its inability to maintain domestic order. This is overstatement; Mexico’s murder rate is lower than in most Latin American countries despite the killings in the states from which drugs are exported. Under the Mérida Initiative, antinarcotics cooperation between the two countries has become significant. Nevertheless, the cooperative “war” on drugs has thus far been a costly failure.

There are now upwards of 12 million unauthorized immigrants in the United States, about 60 percent of them Mexicans. Most of them have come to the United States for economic reasons—to augment their incomes and be able to send remittances to

families back home. Many came because U.S. legislation deliberately omitted any reliable way for employers to knowingly identify the immigration status of those who seek work. This was seen, both in the United States and Mexico, as an implicit invitation to Mexicans to seek work across the border. There is now a somewhat more reliable way for employers to identify the immigration status of job seeker -- but U.S. policy to deal with the millions of unauthorized immigrants already in the country has not yet been determined.

The Mexican constitution prohibits private equity investment in oil and natural gas exploration and development; this E&D is the exclusive preserve of the national oil monopoly, Petróleos Mexicanos, known as Pemex. The government has sought to encourage E&D through service contracts, but there has been little interest in these by qualified oil companies. Pemex has been unable to find enough new resources to compensate for current oil and gas production. In addition, Pemex has scant skills in drilling in the deep waters of its portion of the Gulf of Mexico. Consequently, oil reserves now amount to only about eight years of production at current levels. In addition, production is declining in Mexico’s largest oil field, Cantarell. Conceivably, Mexico will cease to be an oil exporter during the next decade; it is already a large importer of natural gas and oil products. About 40 percent of the federal budget has been funded by skimming from the gross revenue of Pemex, and this source of funding is likely to be at risk. Allowing joint ventures with independent oil companies could improve Mexico’s chances of finding more oil, but changing the current structure would be difficult because of the resource nationalism that has been stimulated in schools and speeches ever since the 1938 expropriation of the assets of foreign oil companies.

Mexico has shown that it can change long-standing economic policy when a crisis demonstrates its faults, but —like many countries—has not shown a similar ability to change policy before a crisis erupts. Trade, investment, banking and exchange-rate policies are examples of crisis-driven changes. The current example of the inability to change policy in anticipation of a crisis is in energy.

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