

Differing Effects of the Global Financial Crisis: Why Mexico Has Been Harder Hit than Other Large Latin American Countries

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In this article, we argue that the economic and financial crisis that began in Mexico in 2008 has not been primarily caused by the US crisis that began in 2007, as many have argued. As we will show, years of misguided economic policies at the national level have been at the heart of the Mexican crisis. On the one hand, the dominance of foreign banks in the country's financial system and the minimal presence of the public banks have greatly limited the range of counter-cyclical policy options available to authorities. On the other hand, in the face of the crisis, Mexico has continuously applied deflationary Washington Consensus policies that have deepened the economic contraction. This article will focus on Mexico's individual problems, which offer important lessons for other Latin American countries with a shared recent history of Washington Consensus policies.

Keywords: financial crisis, financialisation, Washington consensus, foreign owned banks, overindebtedness, Mexico.

A hypothesis frequently stated by the Mexican economic orthodoxy, the mass media and the country's authorities is that Mexico is an innocent victim of the global economic/financial crisis. After stating that there was no imminent crisis in the wake of the first 'heart attack' of the global financial system, and later that Mexico may only catch 'the sniffles' as the crisis began to unfold after the collapse of investment bank Bear Stearns, those responsible for the country's economic policies have now been forced to accept the gravity of the global financial/economic crisis. However, by diagnosing the crisis as a short-term phenomenon and exogenous to the country's economy, these authorities have justified actions that are deepening an already dramatic decline in the country's economic fortunes. As Mexico makes its way through the historically charged year of 2010, which marks the 200th anniversary of the beginning of the country's war of independence and the 100th anniversary of the start of the Mexican revolution,

increasing unemployment, poverty and social divisions will further add to growing political instability in the country.

The goal of this article is twofold. On the one hand, we seek to establish a correct diagnosis of the Mexican crisis. Contrary to the conventional wisdom that Mexico is an innocent victim of the crisis, we contend that the current crisis more accurately represents the failures of Washington Consensus policies, continuously applied in Mexico for almost 30 years, a record among large Latin American countries. On the other hand, based on this diagnosis, we establish why the purportedly counter-cyclical policies have not only been inadequate for confronting the current crisis, but have actually substantially weakened the country's economy.

The article is divided into seven sections. First, we discuss the general nature of the crisis facing Mexico, which is further developed in the following section, which examines the evolution of Latin American economic structures, with particular emphasis given to the changes in the composition of financial systems under Washington Consensus policies. Then, several elements of the international economic and financial system during the era of financial globalisation are analysed, with particular emphasis given to the role played by foreign-owned banks and the changing structures of large Latin American companies. After considering these larger contexts, the article moves on to focus on Mexico's case in particular. Special emphasis is given to shifts in the country's financial system and the dominance of foreign owned banks as one of the principal causes of the nation's current economic crisis. The highly pro-cyclical official response to the crisis is also analysed. Finally, we conclude with some considerations of Mexico's immediate future, including the pitfalls of foreign bank dominance during times of high economic uncertainty.

Endogenous or Exogenous Crisis?

At face value, the argument that much of the developing world, and Mexico in particular, is an innocent victim of the global crisis is a seductive one. The financial crisis did indeed begin in the shadow banking system of the United States, and it did subsequently reverberate throughout the world. Yet it is also true that some countries have maintained economic structures that are highly dependent on, and vulnerable to, the conditions of worldwide trade and finance. In Latin America, all major economies have suffered from severe shocks as a result of their reliance on foreign capital during the last few decades. This phenomenon manifested itself in Mexico in the 1980s, 1990s, and the early years of this century, each time with devastating results. In the era of financial globalisation, financial crises have been a prevalent factor throughout the developing world (IMF, 1998; Laeven and Valencia, 2008). Given that the dangers of strong reliance on foreign capital have been well known for years, can a government claim to be an innocent victim when this reliance causes a crisis? If a person plays with a bee and the bee stings them, can that person blame the bee? This question will be addressed throughout this text.

As stated, our hypothesis is that the current crisis in Mexico represents the limits of the neoliberal economic model, which is based on policies of export-led growth, trade and financial opening, external financing and a reduced role of the state in economic activities, all under conditions of financial domination. A fundamental part of this economic model, which has been implemented in differing degrees in most developing countries, is the systemic replacement of publicly owned banks by foreign-owned ones,

Table 1. Year on Year Percentage Change in GDP, 2009

World	-0.6
Advanced economies	-3.2
Emerging and developing economies	2.4
Western hemisphere	-1.8
Argentina	0.9
Brazil	-0.2
Mexico	-6.5

Source: IMF (2010) World Economic Outlook, Table A4.

a tendency that has led to a shift in the structures of domestic and foreign indebtedness in developing countries.

Although this phenomenon is present in a large part of the developing world, there are nevertheless countries with different experiences and countries that stray from the model. In the context of Latin America, in recent years Argentina has been a leader in the region with regard to recovering its economic sovereignty in terms of monetary, fiscal and credit policies. Other South American countries have made significant advances towards determining their own economic trajectory. Mexico represents the opposite extreme. Due largely to the drastic changes in the composition of the country's financial system over recent decades, the global financial/economic crisis has affected Mexico with particular force (see Table 1), rendering the sustainability of the country's economic model highly uncertain in the near term.

The Financial Structure of the Export-Led Growth Model

Washington Consensus policies, established and maintained by US banks and international financial institutions such as the International Monetary Fund (IMF), with the backing of significant segments of Latin American business and banking groups, led to fundamental changes in the economic structures of the region. The most striking result of approximately three decades of structural reforms has been the loss of economic sovereignty in a large part of the region. The 'independence' of central banks in the majority of the countries of the region highlights the distancing of monetary policy from the needs of national economies. At the same time, the commitment to eliminating fiscal deficits, particularly in times of crisis, represents a total abdication of fiscal policy and the elimination of the role of public spending as a guarantor of private sector profits in all of the countries in the region. Furthermore, the transformation of financial systems dominated by publicly-owned banks into systems characterised by the systemic presence of foreign-owned banks excludes any possibility of a coherent national credit policy. Given the serious limitations in the development of bank credit in national currencies, double monetary circuits arise in which large companies finance themselves in international markets and in foreign currencies. The slow yet steady loss of the publicly owned banks has been a constant in the last decades in Latin America, as can be seen in Figure 1.

In Mexico, the development bank Nacional Financiera, which was one of the principal driving forces behind the 'Mexican miracle', was relegated to second-tier functions as part of the financial reforms implemented at the end of the 1980s. In Argentina, the national development bank was shuttered in the mid 1990s, and its

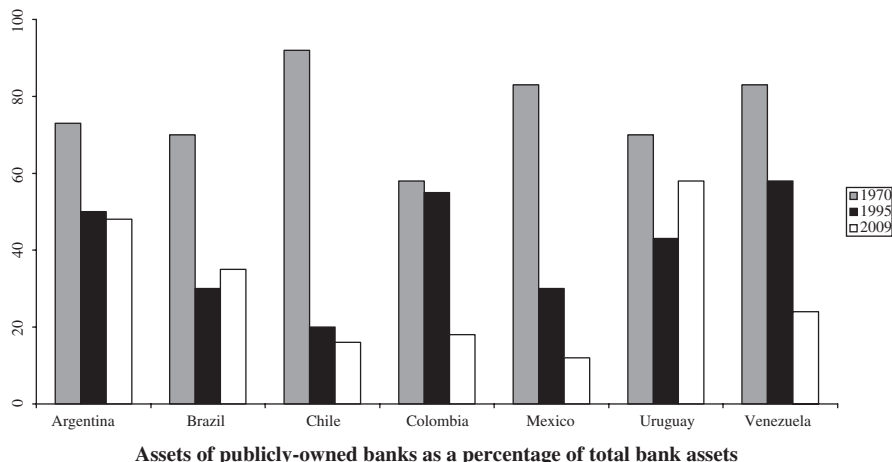


Figure 1. Publicly-Owned Banks in Latin America. Source: LaPorta, Rafael, Lopez de Silanes and Florencio and Shleifer, Andrei (2002). For 2009, Authors' Estimates Based on *América Economía* (2009a), and Central Banks' Information.

system of publicly owned provincial banks was privatised largely as a result of the banking crisis of 1995. Yet the Argentine publicly owned banks proved to be the most anti-cyclical agents of the financial system during the country's banking crisis of 2001–2002. The same is true in the case of Uruguay during its 2002 crisis. Within Latin America, the largest national publicly owned bank is in Brazil, even though several large public banks at the state level have been privatised. The Banco Nacional de Desenvolvimento Econômico e Social and the Banco do Brasil still play fundamental roles in Brazil, one of the few countries in Latin America not to have suffered a significant banking crisis in recent decades.

The results of Washington Consensus policies on financial structures in Latin America have been clear. On the one hand, trade and financial opening have offered significant profits for the expansive transnational corporations (TNCs) in the region, particularly in strategic sectors that were previously dominated by national states, such as hydrocarbon exploitation, the generation and distribution of electricity, telephony, commercial banking, airports, ports, railroads and infrastructure in general. On the other hand, during this period of trade and financial opening, there has been an overwhelming and undeniable trend towards recurrent financial crises, stagnant economic growth, decline in salaries, falling formal official employment with high and growing levels of under-employment and informal employment in the region.

On a more specific level, the participation and/or dominance of TNCs in non-financial sectors of the economy has not met its principal promise of greater levels of investment, nor has the greatly increased presence of international banks fulfilled its promises of increased savings and greater access to affordable and steady financing in the region. In the non-financial sector, combined public and private investment in infrastructure barely reaches 3 per cent of Gross Domestic Product (GDP) in the region, a level far lower than that of the 1980s. Investment in infrastructure has fallen significantly short of what is needed to accommodate the region's growth. A recently published study by the World Bank clearly states that for the region to maintain competitiveness with

respect to East Asia and other regions, investment in infrastructure would have to double. According to the study, in order to lift Latin America and the Caribbean to the level of coverage of South Korea in a period of twenty years or to simply maintain the pace of China, infrastructure investment in the order of 4–6 per cent of GDP would be necessary (Fay and Morrison, 2005), a far cry from present levels in the region.

Far from the stated goals and predicted outcome of the widespread participation of TNCs in non-financial sectors, the most relevant result of TNC participation in the region has been growing capital flight in the form of repatriated earnings, intra-firm transactions, royalty payments, interest, assets sales, etc. In Mexico's case, between 1982 and 2008, interest paid on public and private debt plus TNC profits grew from over US\$6 billion per year to over US\$25 billion per year (Banco de México, 2010). Yet at the same time the coefficient of investment has not risen, as the lion's share of the resources that enter the region have been put towards the acquisition of existing assets. The impact of foreign direct investment (FDI) on the levels of investment is therefore greatly reduced (Vidal, 2001, 2005).

The opening up of regional economies to foreign financial conglomerates has had similar results. Savings rates have fallen throughout the region (Kucynsky, 2003), while bank financing has continuously fallen. During the 1990s, when global banks made their strongest push into the region, bank financing to the non-financial private sector in the region's three largest economies, Argentina, Brazil and Mexico, averaged 17.7, 35.6 and 23 per cent, respectively. During the first seven years of the 2000s, these levels dropped to 14.8, 29.7 and 15.5 per cent (World Bank, 2008).

The Global Consolidation of the Economic Cycle

However, while the largest TNCs and financial conglomerates were increasing their dominance in Latin America and other regions, the same firms and the economies of their home countries were also experiencing profound internal changes, as explored by Guttmann (2009). The financialisation of the US economy has implied the hollowing-out of companies with worldwide coverage such as Citigroup, General Electric and General Motors. At the same time, the financial globalisation led by the United States generated increasing disequilibria in the United States. As stated by D'Arista, the displacement of a large part of the country's productive activity to other countries, together with the growing level of US household debt, created an unsustainable economic situation for the country (D'Arista, 2005), even considering the enormous benefits that controlling the world's hegemonic currency and possessing the deepest and widest financial system in the world grants the United States.

Before its collapse, the era of financial/economic globalisation had arrived at a fairly clear division between the economic functions of the United States and the rest of the world. This relationship, referred to by some as the 'Bretton Woods II' system, signifies that the United States consumes what the world produces, and that the savings or financial resources of the world are placed in financial assets denominated in dollars. By being the financial centre of the world and by holding the hegemonic currency, the United States finds itself in the position of being able to issue financial assets or promissory notes (dollars) for its purchases, while the rest of the world has to produce in order to consume. To buy a product made in China or Mexico, a dollar only has to be printed in the United States, while in China or Mexico something must be produced

to obtain the dollars necessary for the purchase. However, once the Chinese or Mexican product is sold, neither of those countries uses the dollars in their internal markets for fear of monetary punishment, particularly inflation. For this reason, surplus-producing countries sterilise a large part of their capital inflows through the purchase of US dollar-based financial assets. Therefore, dollars printed in the United States are exported to the world through the US current account deficit and later return to the country via the country's capital account (Liu, 2002).

After years of implacable advances through the productive and financial interests of a relatively small number of TNCs based in an even smaller number of countries, an important integration with national economies throughout the world was achieved. For a variety of reasons, some Latin American countries have tied themselves more to the fortunes of these firms and their home country's economies, manifested through the handing over of strategic economic sectors, the expansion of export sectors and increased financial dependency on the United States. It is precisely the countries that have most integrated themselves into this economic model, either in terms of their productive structures or in terms of their financial systems, that have been the most affected by the current crisis. At the same time, other countries have maintained a greater degree of economic sovereignty, or in some cases even recovered what they had ceded in terms of economic self-sufficiency. In Latin America, the case of Argentina is particularly noteworthy.

As such, the hypothesis that countries whose economies were structured to export their products to the United States, to transform their economic surpluses into dollar-based assets, or to pump financial resources out of their country through foreign banks, are innocent victims of the crisis is not valid. In Mexico, the decisions made by the economic groups who have commanded the nation's capital accumulation for years have increasingly strained the domestic economy, while at the same time increasing dependency on foreign actors. As such, even though the crisis did first appear in the United States, in Mexico it has come to reflect the economic model's limitations.

The Financialisation of Latin American TNCs

The form in which financial groups' and corporations' financial gains have been constituted is at the centre of the origin and development of the crisis, in the United States as well as in Europe and Latin America. Finance-dominated capitalism, constituting a regime of accumulation dominated by finance, has been in steady advance for years. This classification does not refer only to the transfer of wealth through new forms of finance, such as derivative markets, which are fed by the treasuries of many TNCs, as well as investment funds, banks and investment banks, when these still existed; it also refers to the merger and acquisitions that have predominated over investments made to increase or create new productive capacities. This point has already been made, both to characterise FDI and its growth in recent years, as well as to explain privatisation processes (Vidal, 2001, 2008, 2009). Finance-dominated capitalism, among other aspects, also relates to the ability of corporations to finance themselves through sales of stock, treasury operations, the issuance of debt and various forms of securitisation.

In an economy in which many large corporations are self-funding, the importance of shareholders and foreign investment funds grows, as does the financialisation of the management of the firm (Plihon, 2003). Corporations have modified the composition

of their shareholders, with a growing influence of investment funds and other financial companies. As Guttman highlights in his characterisation of finance-led capitalism ‘the rapid growth of these so-called institutional investors over the last quarter of a century has turned them into the principal shareholders of large firms across the globe. They often use their ownership rights to impose a financial logic rooted in quarterly per-share earnings as defining measure of performance’ (Guttman, 2009: 22). The directors of firms often employ aggressive management of treasuries, including the issuing of debt in multiple types of paper, the monetisation of assets, inventories, future sales, and as Serfati emphasises, even intangible assets (Serfati, 2009). By merger and acquisition growth, assets can be rationalised and used as a base to generate new income.

Financialisation has evolved within corporations in the US, Europe, Asia and Latin America as a means to increase profits. Mexican-based corporations that have obeyed this logic include Cemex, Televisa, Gruma, Vitro, Grupo Alfa, Modelo, Comercial Mexicana; the Brazilian-based corporations Vale, Votorantim, Gerdau, Sadia and Odebrecht also fall into this category. Other large corporations based in Argentina, Chile and other Latin American countries can be added to the list, as well as several state-owned enterprises in the region. Maintaining the profitability of these companies and their capacity to meet debt obligations in foreign currency has for years represented a constant and significant problem for countries in the region.

Yet with the onset of the crisis, the withdrawal investment funds’ positions and the contraction of several financial markets has created strong credit rationing toward large Latin-American corporations that finance themselves in external markets (*América Economía*, 2009b; BIS, 2009). This fundamental element of the crisis has arisen from the dynamic of profit formation within large corporations based in Latin America. The need for foreign currencies increases with the operations of TNCs, investment funds, pension funds and hedge funds in the region. It is in this context that the diverse relationships between Latin American countries and other countries and regions of the world, as well as the differences between the composition of financial systems, become particularly relevant.

Foreign-owned Banks and the Fallacy of the Importation of the Global Crisis

Mexico’s entrusting of its economic destiny to the ebbs and flows of its neighbour to the north has always been a risky strategy. While the US economy was in expansion, the dismantling of the Mexican domestic economy eliminated any possibility of sustained growth and more plentiful and better paid employment. As much as the US economy may have continued growing, neither the relinquishing of the national system of payments to foreign actors, nor the growing dependence on crude oil exports and the remittances of workers employed in the United States, nor the dependency on the US market, both for imports and exports, would have offered greater economic gains for Mexico.

However, the negative effects of the gradual hollowing-out of the Mexican economy are minimal in comparison to the economic losses, particularly in employment, that the collapse of the US economy has caused, and will continue to cause, in Mexico, which is highly dependent on its neighbour in areas as basic as its supply of food, credit, and employment (both directly and indirectly).

From the mid 1990s to the early 2000s, large global financial consortia have made strong inroads in Latin America. While many hailed the possible benefits of the widespread participation of the foreign-owned banks, even the greatest defenders of their activity, such as the IMF, have warned about the possibility of importing a financial crisis through foreign-owned banks (IMF, 2007: 114). According to the IMF, if there is a financial crisis in the home country of an international bank, foreign branches or subsidiaries could be affected. If one international bank has foreign entities of sufficient size, or if a number of international banks are in crisis in their home countries, a financial crisis could arise in a country that would otherwise not have experienced one.

The loss of the national banking system in Mexico has led to the development of the crisis in two ways: the first takes a similar form to the IMF’s warning, while the transmission of the other arises from the external debts of Mexican companies. In both cases, Mexico offers an important cautionary tale for other countries in the region. With more than 80 per cent of the banking system in foreign hands (as measured by assets) the country’s banking system is more globalised than that of any other large economy. During the years of the foreign owned banks’ domination, all Mexican firms have suffered a notable credit rationing.

As can be seen in Figure 2, in the months that immediately preceded the global financial shock of the bankruptcy of Lehman Brothers in September of 2008, the financing of all sizes of national firms was highly dependent on suppliers, while the commercial banks operating in the country provided a relatively small amount of credit. However, there is a notable difference between the financing of small and medium enterprises (SMEs) and that of the largest companies. As Figure 2 shows, the

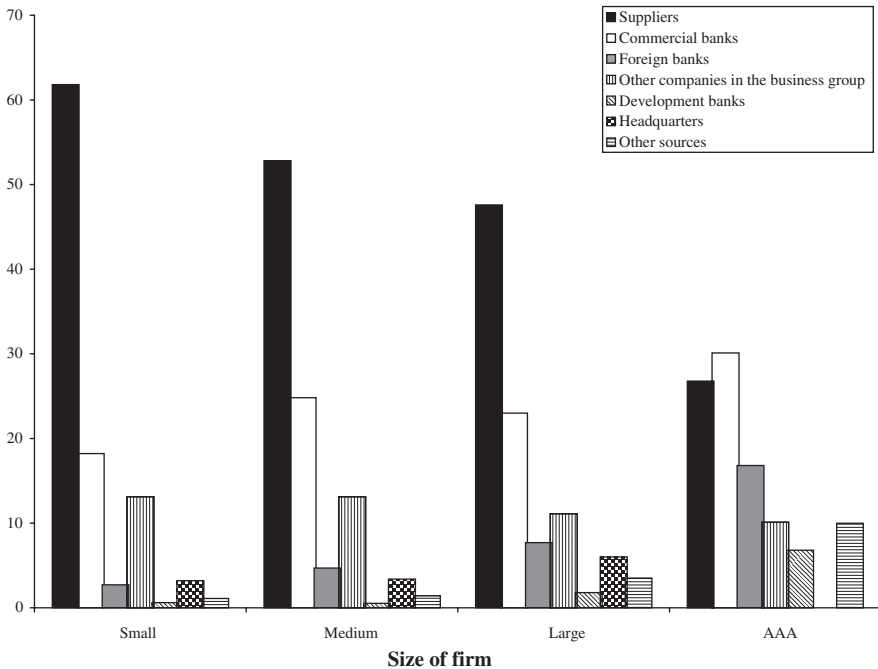


Figure 2. Sources of Financing for Privately-Owned Mexican Firms. (Banco de México, 2009a).

larger the firm, the lower the participation of suppliers and the greater the financing from commercial banks operating in the country, banks operating outside the country, capital markets (under the heading of 'other liabilities') and from development banks.

Therefore, unlike the vast majority of national firms, the largest companies have the option of financing themselves in international and national financial markets through the issuing of stocks, bonds and other credit contracts. In recent years, these forms of financing have been less expensive and more accessible than credit from national banks, for two reasons in particular. On the one hand, foreign-owned banks operating in the country have not increased levels of credit to national firms since the crisis of 1994–1995.

In fact, in the fourth quarter of 1994, Mexican banks allotted 19.7 per cent of GDP to commercial and industrial activities, while in the fourth quarter of 2008, this figure had shrunk to 8.9 per cent of GDP (CNBV, 1994 and 2008). Furthermore, due to the fact that international banks operating in Mexico in many cases charged higher interest rates than their own headquarters in foreign companies, many large companies opted to finance activities directly through headquarter banks.

On the other hand, during this period of financial asset price inflation, international interest rates were at historically low levels. As such, there was a correlation of forces that favoured a growing external debt level amongst the largest Mexican firms. The combination of the rationing of credit to all Mexican firms and the lower interest rates offered by external sources of credit led to a structural change in the financing of the large national firms. Another fundamental change in this aspect has been the incursion by several of the largest national corporations into the derivatives market as a part of the general strategy to increase earnings through financial speculation, a substantive aspect of the accumulation of capital under financial dominance, as already stated.

The collapse of the business model centred around structured finance and the fall of several of the largest global banks confirmed the fact that financial globalisation always had its limits, while at the same time the protection that industrialised countries have granted to their national companies has deflated the myth of a separation between the state and firm that the promoters of globalisation had defended for decades (Guillén, 2007). European and North American countries have been able to channel large quantities of resources towards their national companies through fiscal deficits for many years. During the current crisis, these deficits have grown in dramatic fashion.

Restrictive Internal Policies and External over-Indebtedness

In the face of a deep and prolonged crisis, the response of the Mexican authorities is reminiscent of that taken by their Argentine counterparts in the years leading to the country's banking crisis of 2001–2002, the punctuating moment of the country's long-term economic collapse. In both cases, national authorities attempted to ward off the collapse of Washington Consensus economic models by consolidating fiscal balances. However, in moments of increasing economic strain, such policies are highly pro-cyclical, and are incapable of meeting their core objective of servicing external debt obligations.

In the case of Mexico, a clear dynamic is emerging in which the government is cutting spending and increasing taxes, while at the same time subsidising the external positions of large private sector companies and drastically reducing the capacities of state-owned companies. While the policies are incoherent as an anti-cyclical strategy, they are perfectly consistent with the Washington Consensus model that favours the financial interests of international banks and a small national elite over all other considerations. In the case of Mexico, these interests determine the desire to privatise the few remaining sectors of the economy in which the state still maintains a strong presence, particularly the energy sector.

The protection of the national elite has manifested itself in direct and indirect forms. The most direct form has been the bailout of large privately owned firms by state-owned banks. On the one hand, the central bank (Banco de México) spent more than US\$30 billion between October of 2008 and October 2009, representing around a third of the international reserves at the beginning of this period (Banco de México, 2009b), in large part to guarantee the payment of these companies' debts. On the other hand, state-run banks Nafin and Bancomext also extended a credit line of US\$50 billion to guarantee external debt payments of eight of Mexico's largest privately owned companies (*El Economista*, 2009). Companies such as Cemex, Vitro, Comercial Mexicana, Gruma and Soriana have benefited from these programmes.

As mentioned, large national companies maintained credit lines with the headquarters of international banks, yet, in the wake of the bankruptcy of Lehman Brothers, credit lines were cut and maturing debts were not rolled over. In addition, many large companies also held large derivative positions with international banks. As a result of the approximately 30 per cent devaluation caused in large part by the very actions of the Banco de México to bail out large domestic firms and their international creditors, bets on the stability of the peso quickly soured. While many companies were affected, it quickly became apparent that the situation of Comercial Mexicana (Wal-Mart's main competitor in Mexico) was the most dire, with the company facing imminent bankruptcy had it not been bailed out by the government.

With the easing of the international financial crisis from March through to the end of 2009, such measures have allowed many of Mexico's largest companies to renegotiate debts and stay in operation. If another sharp correction occurs in international markets, it is unlikely that Mexico will be able to bail out its largest companies again. Under the next most likely possibility that international credit markets muddle along for years on a slowly downwards trend, the debt taken on to bail out privately held companies may well come to represent a tipping point for the Mexican economy, as the debt will be compensated for by decreased fiscal spending and higher taxes, which will lead to further economic contraction and therefore higher debt premiums. Such a downward spiral was clearly witnessed in Argentina.

In the face of a protracted and deep crisis, the true beneficiaries of the bailout will be international creditors, not the large Mexican companies, and much less the overall Mexican economy. Although granted a temporary reprieve, large Mexican companies are still far from guaranteed stable financing from abroad, and domestic credit is still largely unavailable. In the initial moments of the crisis, the bailing out of these companies has directly led to a notable increase in foreign debt, a significant devaluation of the peso, the disappearance of approximately a third of the country's foreign exchange reserves and the extension of US\$47 billion credit line from the IMF, in addition to an emergency US\$30 billion Fed credit swap granted in the weeks following the Lehman Brothers bankruptcy.

Mexico's Public Finance Policies in the Crisis: More Taxes, Less Expenditure and Privatisations

Instead of initiating changes in the structure of public and private sector debts in response to the drastic changes in global finance, authorities have placed all of their chips on a one-time guarantee of private sector external debt. The money spent on this bet could have been invested in new refineries to diminish the country's dependence on imported gasoline, or to capitalise a strong public bank that could finance the future of large and small Mexican companies.

Yet, as mentioned, this wager by the authorities does not only carry opportunity costs. In an attempt to guarantee the servicing of foreign private debt, the government has reduced spending in key economic areas while increasing the tax burden for large sectors of society. As of the end of the first half of 2010, budgeted government spending had fallen (year on year, in real terms) as follows: the Secretary of Agriculture by 21.6 per cent, the Secretary of Public Education by 2.6 per cent, the Secretary of Labor and Social Security by 17 per cent and the Secretary of Energy by 87.4 per cent (Secretaría de Hacienda y Crédito Público [SHCP], 2010a). At the aggregate level of government spending, during this period current expenditures fell 1.9 and capital expenditures fell 4.1 (SHCP, 2010b).

Effective as of 2009, the government implemented a new flat-rate business tax (the IETU), a new tax for bank deposits made in cash, and taxes on gambling and lotteries (SHCP, 2008). In addition, value added tax was increased from 15 to 16 per cent, effective as of the beginning of 2010 (Diario Oficial de la Federación, 2009) while key energy prices (particularly gasoline), determined in large part by the government, have continued to rise throughout 2010 (SHCP, 2009a). Yet this fiscal consolidation has been undertaken with a simultaneous protection and advancement of the country's most powerful economic actors, at a great cost to the overall economy.

Mexico has traditionally had among the lowest fiscal pressures in Latin America. In 2008, Brazil collected taxes equivalent to 26.7 per cent of GDP, close to European standards, while the regional average was 17 per cent. In 2008, fiscal pressure in Mexico was 8.1 per cent, far below that of many Central American and Caribbean countries (ECLAC, 2009). This figure is due in large part to the fact that the country's largest companies contribute less than 2 per cent of their earnings to taxation, according to recent statements by the Undersecretary of the Treasury, Alejandro Werner (*La Jornada*, 2009). While a value added tax has been in place for years, the small middle-class currently shoulders around half of the country's tax burden. Unless large businesses pay more taxes, it will be difficult for fiscal revenues to balance out greater levels of external debt.

The dynamic of unbalanced tax receipts and pro-cyclical fiscal policy has been relatively commonplace throughout Latin America in times of crisis. Yet in Mexico's case, this pro-cyclical dynamic is also coupled with the Mexican government's desire to privatise the country's energy sector, which has led to extremely pro-cyclical action on behalf of the national government. The most dramatic example of such behaviour was the shuttering of the state-owned electricity company Luz y Fuerza by federal military police on 10 October, directly eliminating approximately 44,000 jobs, yet opening a large electrical grid for voice, video and data transmission to private exploitation.

The constant bleeding of resources from the state-owned petroleum monopoly Petroleos Mexicanos (Pemex) offers a parallel situation. Years of scant investment,

high levels of external debt, 'endoprivatisation' (Vicher, 2009) and over-exploitation of oil fields has left Pemex in a highly weakened state, with crude production falling precipitously, even as energy prices enjoy a limited rebound. The decision to over-exploit proven reserves while simultaneously starving the company of funds to invest towards greater refinery and exploration capacities represents a conscious effort by successive governments to discredit the viability of the company as a reason for its privatisation. Once again, the desire to privatise Pemex runs completely counter to the interests of the national economy as a whole, as the company provides approximately 40 per cent of all government revenue. Yet unlike other oil exporting nations, the size of the past oil boom has not been put to any apparent good use in Mexico. While the government's dependence on oil revenues has distorted Mexico's tributary system, no significant domestic investments have been made, the rainy-day oil surplus fund has been largely spent, the largest oil fields have been over-exploited and a lack of investment in Pemex means that company can no longer meet the country's refinery needs. Mexico now imports approximately a third of refined gasoline, weakening the country's trade balance and passing over opportunities for domestic employment and profit in the petroleum transformation processes.

At the same time, it is noteworthy that Pemex cannot find competitive financing in the Mexican internal market. Estimated as being the eleventh largest integrated *company* in the world (Pemex, 2009), Pemex, like its peers in the private sector, has financed itself in foreign markets for the reasons already mentioned. It has also entered heavily into derivatives markets, with mixed results. As a public entity, public finances explicitly guarantee the external debt of Pemex, which has the relative certainty of being rescued by the government if need be. But on the other hand, the external financial position of the government could be drastically weakened if a more tenuous debt situation arises in relation to Pemex.

The high levels of external debt of the public sector was one of the principal factors behind the crises of 1982 and 1994–1995. Even though private external debt flashed the first warning signs during the current crisis, the situation of external public debt is also highly worrying. Public internal debt was at US\$313.7 billion in September 2009, while in the same month external public debt was just over US\$91 billion (SHCP, 2009b). Total net federal public sector debt as a percentage of GDP grew by 75 per cent from December 2007 to September 2009 (SHCP, 2009c: 77). However, it is worth noting that as a result of financial innovation and the pervasiveness of derivatives, the line between external and internal debt has blurred considerably. Meanwhile, the total liabilities of the investment projects with a deferred impact on the budget, in relation to Pemex, had risen to US\$43.5 billion by the end of 2008 (SHCP, 2009d: 87). In a continually complicated international context, a repetition of past Mexican public finance crises continues to be a strong possibility.

However, the current and growing crisis in public finances marks an important difference with past crises, in which external debt financed some form of economic expansion. The large-scale investments in the oil sector during the mid and late 1970s and the speculative boom at the beginning of the 1990s represented strategic bets by the respective governments that soured and resulted in crises. The current public and private external high levels of debt do not stem from any type of growth strategy (as poorly planned as they may be) for the national economy. On the contrary, they represent a complete lack of economic strategy and the total abdication of internal credit policies. Even though certain national companies have undoubtedly been able to expand their international operations, the national economy has experienced an economic cycle

of stagnation followed by collapse, as opposed to a more traditional cycle of boom and bust.

However, as stated, in these initial moments of the crisis, private external debt, which in the second half of 2008 reached approximately US\$67 billion (SHCP, 2009e), has been the weakest link in Mexico's financial structure. The unconditional guarantee that the government has offered to the largest private-owned national companies and their foreign creditors has blurred the line between private and public debt. While the guarantees for Pemex are explicit, the recent government decisions signal that it is also willing to sacrifice the well-being of public finances in order to rescue private enterprises.

Foreign-Owned Banks: Pro-cyclical Agents during Moments of Financial Crisis

As argued, the dominance of foreign-owned banks in Mexico opens up the possibilities for a financial crisis in two ways. The first, already briefly examined, results from the obligation of large public and private companies to seek finance in international markets. The other, which will be analysed in this section, relates to the possibility that in moments of crisis, the interests of foreign-owned banks can diverge from the interests of a national economy to the point that the interests of the foreign-owned banks provoke a crisis, or deepen one already in progress in the host country.

The most conventional form for the development of a crisis provoked by foreign-owned banks follows the basic schematic of the IMF, already presented, and comes close to the situation that has been playing out with Citigroup and its local subsidiary Banamex. In this scenario, there is a banking crisis in the United States, created in part by Citigroup, whose balances have been greatly weakened. In dire straits, the headquarters adopts a defensive position. On the one hand, national and international credit lines are reduced, while on the other hand, and following the same logic, the headquarters seeks to repatriate as much capital as possible that had previously been spread throughout the world in previous moments of expansion.

For their foreign subsidiaries, such as Banamex, this dynamic involves a reduction in credit and a rise in the funds repatriated to headquarters. Even though these actions strengthen the financial position of the headquarters, they reduce financing in the host country and decelerate the local economy. But in addition, these operations require foreign currency. In these early moments of the crisis, Mexico has now seen the consequences of both the reduction of credit lines and the repatriation of capital. In addition to the large-scale capital outflows seen in Mexico after the collapse of Lehman Brothers, bank credit issued to Mexican society, starting from a very low point, registered a year on year fall of over 6 per cent as of August of 2009 (SHCP, 2009f: 34).

The same banks that today dominate Mexico's financial system, when confronting a highly uncertain panorama during the Argentine banking crisis of 2001–2002 protected the interests of their headquarter banks at all costs, abandoning local branches and subsidiaries, completely closing credit lines and increasing earnings through derivative operations in order to repatriate large sums of dollars to their headquarters (Marshall, 2008). Even though similar behaviour has yet to present itself in Mexico, it represents

one of the greatest risks to the country's economy in the case of the probable deepening of the financial crisis.

Financial structures take time to change. The transfer of the Mexican banking system to foreign actors has left public and private finances in a state of elevated external vulnerability, precisely at a time when the home countries of foreign banks operating in Mexico have entered into a deep and prolonged crisis. As difficult as it will be to modify the external positions of private companies, it will be much more complicated to 'Mexicanise' the country's banking sector, particularly in moments of crisis when foreign banks control the ever-scarcer supply of dollars. During the Argentine crisis, the foreign banks, backed by the governments of their home countries as well as the World Bank and the IMF, utilised their economic power, increased by the crisis, to cut off the flow of dollars into the country in an attempt to expand their presence in the local market and to impose the dollar as the national currency. Due in large part to the presence of a strong national publicly owned bank, and in spite of the grave crisis provoked in no small part by the foreign-owned banks operating in the country, the Argentine government was able to resist their offensive (Marshall, 2008).

Despite the fact that the country's capability to finance itself in international financial markets was severely restricted, the Argentine government was able to channel growing amounts of credit into the strengthening of the country's publicly owned companies and their SMEs through the publicly owned banks. As such, through the recovery of the country's credit policy, denominated in Argentine pesos, national investment was lifted, the participation of national companies in the domestic economy grew, and the country was able to maintain sustained levels of employment and economic growth uncommon to the region. As seen in Figure 1, the age of financial globalisation has corresponded to a period in which state-owned banks in Latin America have been gradually dismantled, opening up spaces for the subsequent entry and domination of international banks. Recent decades have represented a golden age for the largest global financial consortia, while for Latin American countries, these years have witnessed repeated financial crises in the context of economic stagnation, and falling wages and growing income disparity.

Conclusions

Mexico currently finds itself mired in what appears to be an intractable financial and economic crisis that is likely to last into the coming years. More than any other Latin American country, Mexico has hitched its wagon to the fortunes of the United States in terms of trade and employment, while in financial terms, it has left itself extremely exposed to the volatility of international credit markets and the interests of foreign banks operating in the country. As a result, Mexico has been particularly hard hit by the first stages of the global crisis. While aggregate GDP figures must be taken with a pinch of salt, the fact that Mexico's GDP shrank by 6.7 per cent during 2009, while Argentina and Brazil's economies grew by 0.7 and 0.3 per cent respectively, is indeed telling (ECLAC, 2010). As has been noted by organisations such as the World Bank, approximately half of all people thrown into poverty in Latin America as a result of the global crisis are in Mexico (World Bank, 2009). The Mexican government's response to the crisis, based more on protecting and expanding the positions of a small elite than on protecting employment, has significantly aggravated a crisis that was of its own creation. The identification and analysis of the differences between the

Mexican experience and those of other Latin American countries in the face of the current global crisis is of utmost importance, and begs for further research into the area.

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Effects of the Global Financial Crisis: Mexico

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