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TRADE CONFLICTS AND U.S.-MEXICAN RELATIONS

by

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TRADE CONFLICTS AND U.S.-MEXICAN RELATIONS*

INTRODUCTION

Trends and conflicts in Mexican trade cannot be divorced from the general context of U.S.-Mexico relations. Even Canada, which depends more heavily than Mexico on trade with the U.S. (nearly 70% as opposed to around 66% for Mexico), and which has a much higher level of U.S. direct investment (50% versus 5%-6% of total investment in the country), has escaped the heavy burden of U.S. dominance and history of intervention which Mexicans feel they have suffered. Mexican nationalism and suspicion of U.S. motives rest on a historical awareness of the loss of half the national territory to the U.S. and repeated military incursions in the past century. More recently, Mexico has felt consistently disadvantaged by extreme disparities in political and economic power between the two neighbors. These factors may be little more than historical curiosities to North Americans; however, they represent a living reality to Mexicans. Indeed, they are crucial for any comprehension of the political context within which Mexican decisions concerning trade are made.

Dependence of Mexico upon trade with the U.S., along with geographical contiguity, guarantee that Mexican trade policy is nearly always made with the U.S. in mind. For this reason it is valid to concentrate almost entirely upon U.S.-Mexico trade issues, with only occasional reference to Mexico's other trading partners. Table one shows that the U.S. share of Mexican trade has remained fairly constant over the past

*The opinions, statements of fact, and conclusions of this paper are those of the author alone, they do not necessarily reflect the views of Bankers Trust Co. or its clients.
ten years and in 1979 stood at 62% of imports and 68% of exports. The
dollar volume has increased rapidly, from $2.9 billion in 1970 to $19
billion in 1979. While Mexico is an important trading partner for the
U.S. (third largest in 1980, up from fourth place in 1979), it still
only bought 5.5% of U.S. exports and sold 4.2% of imports in 1979.

The complexity and variety of trade and non-trade transactions
between the U.S. and Mexico also condition the relationship. In most of
these Mexico is also the vulnerable partner. In the area of services,
Mexico received $1.5 billion in 1979 from U.S. tourists, while Mexican
tourists spent only $700 million in the U.S. The boycott of Mexican
tourist resorts after the "anti-Zionism" vote in the U.N. in 1976 is
still resented. U.S. direct investment, while only some 5% of the total
in Mexico, occurs in the most dynamic sectors and is crucial for
economic growth. Mexican fears about the effects of such investment are
discussed below, however an imbalance in the flow of technology should
be mentioned here. Millions of unskilled Mexican workers enter the
U.S., mostly illegally, every year. It is estimated that one-fifth of
Mexican-born workers are employed at least part time in the U.S. and
some estimates of worker remittances exceed $3 billion. Any effort by
the U.S. to stop this flow could seriously endanger the stability of the
Mexican political system. The prosperity of northern Mexico rests
partly on the $3 billion received in 1979 from the U.S. in border com-
cmercial transactions (while $2.5 billion flowed the other way). Drugs
and contraband may constitute a $2-$3 billion business and President
Nixon's "Operation Intercept," in which the border was closed in the
early 1970s, was another reminder of Mexico's vulnerability.
None of the above is to argue that the U.S. does not share in the vulnerabilities of the relationship, but Mexican scholars and officials resist U.S. description of the relationship as "interdependent," because, as they point out, the interdependency is a very lopsided one. At the heart of this inequality lies the fact that the 2,000 miles between Tijuana-San Diego and Brownsville-Matamoros represent the longest land border between an industrialized and developing country in the world. The difference in levels of development, combined with a high and increasing level of interconnection between the two societies, might be expected to lead to tensions under any circumstances. To this must be added Mexico's unique political and economic development model -- so different from that of the U.S. -- and its fierce sense of national pride and desire for national autonomy. These factors produce a wide range of opportunity for misunderstanding and an authentic clash of interests, as well as the basis for policy debate and political struggle within Mexico over trade issues.

Before discussing the development model itself, it must be accepted that development issues, and trade issues in particular, affect the viability of Mexico's political system -- a viability that is never taken for granted in Mexico. Indeed it may be argued that a major distinction between trade debates in the so-called newly industrializing countries and debates in the developed world is that in the former the debate directly affects the outlook for political stability and regime maintenance (not just current administration), while in the latter it usually does not.
Mexico's political system is based on the consolidation of an authentic (albeit middle class) social revolution which transformed Mexican society between 1910 and the early 1930s (though most of the fighting was over by 1920). The Mexican Revolution and its institutionalization has produced a system which, despite its apparent hierarchical characteristics, is centralized and authoritarian. It is, in fact, a delicate balance of ideological tendencies and contending social forces. The hierarchy, the centralization, and the authoritarianism are real, but they exist within a framework of informal rules of the game requiring compromise, veto power for various groups, consensus building, and severe limits to the power of those with authority.

It is difficult to describe briefly the core of the contending ideologies in Mexico, but in short-hand manner they may be seen as the competition between (but also the coexistence of) those who wish to emphasize the middle class and capitalist interests of Madero, Obregon and Carranza, and those who emphasize the interests in social justice of peasants and workers, symbolized by Zapata and Cardenas.

There are two important implications of this Mexican political reality for trade policy. The first is that competing ideologies (not just interests as in the U.S.) co-exist within each Mexican administration: one advocates relatively free trade and increased integration of the economy into the global economic system; the other emphasizes autonomous national development, an increased role for the state and protec-
tion into the foreseeable future (albeit "rationalized" protection).\(^1\)

The second implication for trade policy is that these two ideological tendencies are balanced and, for at least the next decade, they will be linked to a larger balance of forces that is part and parcel of the Mexican political system. To eliminate one or the other would be to significantly alter Mexican society and probably bring an end to 50 years of political stability. Thus, we can expect a constant and unresolved struggle over the next decade within Mexico about, among other things, the issue of free trade.

The way in which competing ideological and policy perspectives are linked to specific trade policies will be discussed below. It should be emphasized that, in spite of these disagreements, Mexico is not a highly polarized society. Mexican presidents do make coherent policy; in the case of trade this is perhaps more coherent than that of most industrialized countries. The elite, while competing at one level, is not fragmented but extremely unified when a policy decision is announced. For example, after the decision to defer entry into GATT little more was heard about the issue publicly.

In the past two years the Lopez Portillo administration has developed a fairly coherent set of economic plans and policies to achieve the goals upon which nearly all political elites agree. Many of these are derived from Mexico's nationalism vis-a-vis the U.S. and from

\(^1\)These two models have recently been characterized by Carlos Tello and his collaborate "the neoliberal project" and "the nationalist project" respectively. See Rolando Cordera and Carlos Tello, Mexico, la disputa por la nación: perspectivas y opciones del desarrollo Mexico City: Siglo Veintiuno, 1981.
the view that as a newly industrializing country Mexico suffers severe trade and other economic disadvantages which petroleum may give it the opportunity to partially redress. Mexico does not have the industrial capacity to compete with the U.S. on an equal basis. It lacks the technology, infrastructure, and cadres of trained technicians to compete except in a few very specific areas. Mexico is also vulnerable to decisions of foreign investors, capital flight (of the kind that forced devaluation in 1976), and the general weakness of the peso vis-a-vis the dollar in the context of free currency convertibility between the two countries. High unemployment and high inflation also make Mexico dependent on other phenomena discussed above, such as labor migration to the U.S. Nearly all Mexican policy-makers agree upon or give lip service to at least the general goals of the Mexican development model. These include:

- To place priority upon decreasing an unemployment and underemployment rate which may be over 40% -- with the need to create 525,000 new jobs every year simply to stay even with the 3%-plus population growth rate; and a related effort to ease what is one of the most inequitable income distribution patterns in Latin America.

- To lay a sophisticated manufacturing export base which will provide jobs and take on the burden of maintaining economic growth as petroleum reserves decline over a twenty-year period.

- To lay a much more solid base for agriculture, both for food self-sufficiency and for export.

In order to meet these goals the Lopez Portillo administration, during the late 1970s, developed a series of development plans laying out in detail targets and strategies to guide government and private sector activity through the end of his administration in 1982 and beyond. This is the first time a Mexican president has made a systematic effort to set out policy guidelines for his successor. The
planning documents, including a Global Development Plan, some eight sectoral plans, state plans, and the Mexican Food System (SAM), are not of equal importance. One of the sectoral plans, the 1979-1990 National Industrial Development Plan (NIDP), and the slightly more recent 1979-1982 Global Development Plan (GDP) (a compilation of various sectoral targets and strategies), are the two key documents. The Mexican Food System gives substance to the agricultural sections of the GDP.

Both the NIDP and the GDP emphasize employment as a key goal. To achieve this, both target very rapid economic growth rates of 8% per year through the 1980s. Growth is to be export-led; principle exports are petroleum and petroleum derivatives, but increasingly, it is hoped, manufactured exports. An industrial growth rate of 11% is projected by the GDP; this in turn requires a 15%-20% growth in exports through 1982. The 8% overall growth rate is seen as necessary to achieve even a modest growth of 4% in employment, enough to keep slightly ahead of population growth which was 3.6% as late as the mid-1970s. The NIDP deals almost entirely with industry and targets some 83 industries. In particular, high growth rates are planned for oil, petrochemicals, construction, electricity and manufacturing.

There was considerable criticism of the NIDP when it appeared because of the striking gap it projected between industrial and agricultural productivity. The major new addition in the GDP is to bring agriculture back to center stage (without significantly reducing industrial growth targets). The GDP and the Mexican Food System (SAM) foresee an agricultural growth rate more than 4% higher than that projected in the NIDP. A major goal is self-sufficiency in corn and beans by 1982, with
self-sufficiency in other basic foods to be reached during the rest of the decade. Fully 22% of public investment is to go to agriculture from 1980 to 1982, and emphasis will be placed upon related policies in the areas of food prices, credit, packaging, transportation, and tractor production.²

The goals and strategies laid out in the various development plans and in the statements of various government and academic planners and economists may be summarized as follows:

- Increasing employment through rapid growth.
- Increasing labor participation in economic growth through significant increases in real wages.
- Rejuvenating rainfed agriculture and achieving food self-sufficiency through government investment, tax and other incentives, and bureaucratic reforms.
- Diversifying exports away from petroleum and primary materials by increasing domestic manufacturing and by penetrating international markets. Strategies include: using government and private investment; a vast array of tools including incentives, subsidies, and government purchasing policies; and rationalization, but not elimination, of tariff and non-tariff protection.
- Diversifying export markets to reduce dependence on the United States.
- Creating a strong capital goods industry through selective import substitution and measures mentioned above.
- Using petroleum as a fundamental instrument not only to achieve internal economic goals, but as a key tool in international commercial and other negotiations with the U.S. and other industrialized countries.
- Decentralizing the economy by developing major growth poles in regions of the country outside the Mexico City, Monterrey, and Guadalajara regions through government investment and encourage-

ment of more decentralized private investment.

- Using foreign investment policy and regulation of technology transfer as another fundamental instrument to achieve employment, industrialization, and export goals, while maintaining indigenous managerial control over firms with foreign capital participation.

DEBATES AND CONFLICTS OVER THE MEXICAN DEVELOPMENT MODEL

Close analysis of the nine goals and/or strategies in the preceding section reveals a number of unanswered questions of both interpretation and apparent mutual contradiction. Such questions set the agenda for ongoing debate within Mexico on economic and social development in general, and on trade in particular. Many economists note that a growth rate of eight percent per year has and will lead to astronomical rates of inflation, undermining both income distribution and manufacturing export goals (because of an increasingly overvalued peso). Mexico's inflation rate is estimated at nearly 30% for 1981 and may be as high as 40%-45% within a few years. Supply constraints, bottlenecks, and lack of monetary controls insure that rapid growth and high inflation will be closely linked.*

Rapid growth may also destroy the possibility for building a capital goods industry because many of the products which could be manufactured domestically, if demand developed gradually, will have to be imported on a crash basis. In addition, rapid growth may exhaust petroleum reserves faster than anyone expects and may, in the meantime, force Mexico into a mono-export economy. In terms of sectoral growth, it is not precisely clear what the trade-off is between industry and agriculture. The NIDP was drawn up without much emphasis on

*Money supply has grown at 30% annually in recent years.
agriculture, and the SAM and the GDP did not fully integrate planning in all sectors when reemphasizing agriculture. The dominant criticism of all the plans is that they represent a compilation of the differing perspectives of several ministries, but not an integration of these perspectives.

Many of the problems raised above are technical economic questions. Nevertheless, at the heart of these problems lies a political and ideological dilemma about the future structure of Mexican society and its relationship to the U.S. and the international economy. The question can be posed in several ways, but given our concern for trade issues it seems useful to pose it as: Should Mexico pursue a model of independent nationalist development or one of full integration into the international capitalist system? As part of this fundamental debate there are three sub-debates going on in Mexico and are likely to continue through the 1980s. They are: the petroleum debate, the agriculture debate, and the trade debate.

The nationalist/internationalist debate stems directly from the general ideological tendencies and divisions which characterize the Mexican political system. While a description of the debate in such polarized terms grossly oversimplifies the subtleties of Mexican social and political processes it is nevertheless useful to show that there is some clustering of policy preferences in these terms. The idealized nationalist side tends to emphasize: petroleum conservation, diversification of markets away from the U.S., some continued non-tariff protection (anti-GATT), basic foods rather than export agriculture, a relatively large government role in the economy, and heavy expenditure on social
programs. The idealized internationalist side leans toward: high levels of petroleum production, less emphasis on diversification of markets and a closer relationship with the U.S., opening the economy more rapidly to import competition as the best way of developing competitive industries (pro-GATT), the doctrine of comparative advantage in agriculture, reliance on the private sector for most growth, and trickle-down theories of income distribution.

It should be noted that nowhere in policy circles in Mexico (and few places in the private sector) can be found any individual, let alone group, advocating a Chilean, Argentine, or even a Brazilian approach to these issues. Most internationalists and certainly those in the government, accept many of the nationalist precepts. Current policy is a mix of the two themes, leaning toward the nationalist side.

Below, current trade-related policies and debates will be described as an introduction to analysis of trade issues with the United States. We focus mainly on the sub-debates over petroleum and trade; the agriculture debate, perhaps the most difficult and complex, requires extensive discussion of internal social and political structures.

The Petroleum Debate

Mexico now claims some 60 billion barrels of proven oil and gas reserves and 250 billion in possible reserves, which would place it second only to Saudi Arabia. A careful study by the Rand Corporation, however, estimates a 90% probability that Mexico will ultimately produce over 70 billion barrels of petroleum liquids, a 50% probability that it will produce over 90 billion barrels, and a 10% probability that
production will exceed 120 billion barrels. For natural gas the 90%, 50% and 10% estimates respectively are: 130 trillion cubic feet, 170 trillion cubic feet, and 210 trillion cubic feet.  

At present Mexico produces some 2.2 million barrels per day and exports about half of this, of which over 700,000 b/d (70%) goes to the United States. This represents 5.7 percent of U.S. petroleum imports and makes Mexico the 8th largest U.S. supplier. From January to June 1980 Mexico exported an average of 300 million cubic feet per day of natural gas to the U.S. Mexico can be expected to earn nearly $11 billion in foreign exchange from oil and gas exports in 1980. This represents nearly 70% of merchandise exports for that year, up from only 34% in 1977. As the Rand study points out, the key questions for the U.S., and for Mexico, though perhaps for different reasons, are what level will Mexico’s production reach, how much will be exported, and to whom?

With regard to the production platform question, an intense struggle has continued throughout the Lopez Portillo sexenio between the conservationists (most academic economists and intellectuals, some labor groups and the Ministry of National Patrimony and Industrial Development) and the expansionists (some private sector groups, the state oil company PEMEX, and the powerful petroleum workers union). At first it seemed as though the expansionists had won, as production increased

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4Ibid.
rapidly to 2.2 million b/d and rumors of a much higher platform circulated. Then in mid-1980 Lopez Portillo announced a ceiling of 2.7 million b/d through 1982. In November 1980 Minister of National Patrimony, Jose Andres Oteyza, announced that a ceiling of 1.5 million b/d had been placed on exports through 1990 and that no more than half could go to any one country. This move was directed at the large proportions of petroleum exports which go to the U.S. A similar ceiling appears to limit natural gas exports to the U.S. to the 1980 level of 300 million cubic feet per day. The announcement of the latter ceiling says nothing about the presumed 2.7 million b/d ceiling on production by 1982, and suggests by implication that production by 1982 could be as high as 3 million b/d (if half of production is exported).

The softening of the world oil market in the Spring and Summer of 1981 changed the terms of the debate between expansionists and conservationists somewhat but has not affected basic positions. The conservationists resisted lowering oil prices while the expansionists, led by former PEMEX Director Diaz Serrano, supported this virtually inevitable move. Two price reductions later, in the Winter of 1982, Mexico has had to ignore quotas on imports to the U.S. with its (previously inconceivable) agreement to sell to the U.S. strategic petroleum reserve and will probably have to step up petroleum production to meet both internal demand and loss in projected foreign exchange revenue resulting from lower prices. Nevertheless, the pragmatism of the Mexican response to lower oil prices does not signal any reduction in the basic differences between the expansionists and the conservationists. The U.S. now has a stronger hand temporarily in negotiating over petroleum issues with Mexico. Should the U.S. choose to overplay that hand, it will simply
strengthen the arguments of the nationalists in the future.

The dangers of significantly increased hydrocarbon production involve early exhaustion of reserves and inability of the economy to absorb export revenues. Two prominent Mexican economists have laid out a conservationist and nationalist perspective for regulating petroleum production using the following criteria:

- Maintenance of reserves. Some suggest that Mexico could eventually produce in excess of 7 million b/d. Another conservationist economist has calculated that with reserves at 70 billion barrels and growth at 8% per annum, Mexico would reach the point of 15 years of reserves at existing production rates by 1986 and with 70 billion barrels by the mid-1990s -- all much sooner than anyone is currently expecting.

- Production only of what the economy can absorb. This involves first keeping down inflation rates and making sure that all dollars coming into the economy are transformed into internal investment, since oil prices are likely to rise faster than interest rates. Secondly, petroleum income should create a permanent source of wealth -- not simply bail Mexico out of balance of payments crises as has happened to date. Third, petroleum production rates should be geared to efficient possibilities for opening the economy to foreign trade -- but not allowing Mexico to fall into the trap of dependence on capital goods and technology imports. For example, one calculation suggests that between 1979 and 1986 48% of all investment by PEMEX would require goods not made in Mexico, thus transferring abroad much of the benefit of oil industry development.

- Use of petroleum to negotiate trade agreements. This means negotiating other Mexican exports to the U.S. in exchange for petroleum, and negotiating coinvestment and technology

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6 Confidential interview, Mexico City, March 1981.

7 Laura Randall, op. cit., p. 8.
transfer agreements with other industrialized countries.

- Maintaining world market equilibrium. Mexico has not joined OPEC for reasons of national autonomy, good relations with the U.S., and the fact that it can receive the benefits of OPEC without joining. Nevertheless, at export levels of 2-3 million b/day, it will have a significant impact on the world market. It can be expected to act to maintain price levels and generally go along with OPEC production rate policy.

The second question about petroleum policy is how much will be exported? The ceiling on exports of 1.5 billion b/d will undoubtedly hold through 1982 but cannot bind Lopez Portillo's successor. The issues discussed above concerning the absorptive capacity of the economy, economic growth policy, and impact on the world market will affect this decision as well.

On the third question, to whom will the exports go, rests much of the debate between the nationalists and the internationalists. As the November announcement suggests, much of the debate will involve relations with the United States. In the first place, Mexico hopes to use petroleum as its most important bargaining chip in commercial and other (e.g., labor migration) negotiations with the U.S. In addition, by signing petroleum agreements with other countries, as it has already done with Japan, Spain, and Canada, Mexico expects to receive benefits in terms of transfer of technology and foreign investment that it might not otherwise receive.

Second, and perhaps more importantly, Mexico has nationalist and national security reasons for wishing to diversify petroleum exports away from the U.S. The nationalization of the petroleum industry in 1938 by President Cardenas is a major symbol of the Mexican Revolution -- made even more important because most of the industry was owned by
U.S. citizens. All Mexican presidents must be especially sensitive to the charge that they are delivering Mexico’s oil back into U.S. hands. In addition, there is fear that should the U.S. become too dependent on Mexican oil interruption of the flow could lead to a national security threat from the U.S. Such fears have been intensified by incidents such as Energy Secretary Schlesinger’s refusal to approve the natural gas price negotiated between Mexico and U.S. companies in 1979, and a January 1980 complaint by the Carter administration against Mexican price hikes followed by the discovery a few weeks later that the U.S. was selling oil to Japan on the spot market at an even higher price. 8

Petroleum production and export policy is thus important in terms of domestic consumption and growth issues, and also as a factor in determining what kind of a deal Mexico is able to negotiate for itself in international trade. Yet playing "the oil card" conflicts somewhat with valid concerns of the conservationists and it is not clear that Mexico can both use oil conservatively and as a lever for international concessions to the extent that advocates of both lines imply. The political sensitivity of these issues is illustrated by the rather opaque character of public announcements and the use of rumor to float trial balloons. The 1980 announcement of the 1.5 million b/d export ceiling beyond 1982, when the current administration cannot possibly enforce it, is a case in point, and confuses outside observers (and presumably the Mexican public) about whether it is a conservationist or an expansionist

The key to Mexican export policy is a vast array of subsidies and incentives to promote industrial exports. These include certificates of fiscal promotion, reduced rates for electricity and gas, and preferential loan rates. In addition, implementation of the foreign investment law is geared to promotion of exports (see below), and in certain industries, such as automobiles and pharmaceuticals, special requirements for export are traded off against production licenses or local content requirements. While the Mexican NIDP and GDP recognize that Mexican exports to the U.S. will depend on fluctuations in the U.S. economy, policy makers hope to guarantee exports against extreme fluctuations in U.S. income levels and U.S. protection by negotiating bilateral agreements to guarantee markets, and by diversification of trading partners.

Success of the diversification policy appears limited. Despite efforts by various Mexican presidents, the U.S. share of Mexican trade is not very different from what it was over 20 years ago. President Echeverría (1970-1976) also put major emphasis on diversification of capital and technology flows, yet this percentage from the U.S. actually increased during his administration. An area where further diversification may be possible, in spite of Echeverría's experience, is that of technology and service contracts. The Japanese already have significant involvement in steel and pipeline technology, and the French and Canadians may have an increasing role in nuclear development.
Some of the industries targeted in the NIDP for higher export goals include:

- Those where the limiting factor is supply, not demand, such as mining.
- Those which add value to local raw materials or process basic industrial inputs such as secondary petrochemicals, chemicals, metal products, agroindustry and fertilizer.
- Traditional exports that have reduced output because of lack of investment or competitive capacity such as textiles.
- Those that require large scale demand and thus depend on foreign markets such as capital goods.
- Sectors that have generated a trade deficit because of control by foreign companies, such as the automotive industry, pharmaceuticals, rubber, and some chemicals.

All the targets mentioned are goals, not reality. At present, nearly 100% of production goes to meet domestic demands and industrial export has been labeled "marginal" by at least one U.S. economist. It is true that the list of Mexico's top export earners has shifted from primary agricultural and mining products in 1965 (sugar, coffee, cotton, lead, copper and zinc) to a somewhat more varied list, including processed goods (petroleum, coffee, frozen shrimp, chemical products, cotton, automotive vehicles, parts and components, electrical and electromechanical machinery and equipment, tomatoes, fresh vegetables and cattle on the hoof). However, trends in exports showed increases in 1978-79 greater than the 43.3% overall increase in exports only in extractive industries like crude petroleum and chemicals (with agriculture at +18.3% still considerably higher than transformation industries at +11.2%). The big gainers between January-June 1979 and 1980 with

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total exports up 76.4%, are petroleum derivates (+559.0%), crude oil (+190.2%), metallic and non-metallic minerals (+91.5%) and tomatoes (+24.5%).

**Import Policy and Protection**

In the past five years Mexico has attempted to move from a policy of import substitution of consumer goods to a policy of selective import substitution of capital goods and a concentration on export promotion of most manufactured goods. The by-word has been "rationalizing" protection, rather than moving to free trade. Until 1976 Mexico had a high tariff structure, but more importantly had strict quotas on most of the 7000 items on the tariff schedule. In addition, import permits were granted not by a centralized executive agency, but by what one Mexican government official called a "mafia" of sector-specific import committees formed by local domestic manufacturers. Each committee was constituted by local manufacturers and passed on each import license on a case-by-case basis. This led to ample opportunity not only for severe protectionism but also for virtual extortion. Often cases would arise where local manufacturers on the import committee turned down an import, claiming that they manufactured the product domestically. This would turn out to be untrue, and in order to get the license passed the importer might have to agree to buy a certain amount of the local product even if it were inappropriate. Certain items, such as automobiles, could not be imported under any circumstances.

From the perspective of the mid-1970s, Mexico has come a long way in "rationalizing" protection. Policy has moved to selective tariffs and quotas plus the subsidies and incentives mentioned in the previous
section, and local content requirements in areas like autos, auto parts, and pharmaceuticals. As of December 1979, only 1,729 items on the tariff schedule were subject to prior permit, though these still represent 55% of imports by volume and 60% by value. In many areas, such as durable consumer goods, quantitative import restrictions have been replaced by technical/bureaucratic judgements within the Ministry of Commerce, thus decisions are significantly more centralized. Mexico has not used non-tariff restrictions of the kind used in some industrialized countries, such as environmental or labeling laws or other kinds of standardization requirements.

Entry into the GATT and associated protocols (discussed later) would eventually produce an even more significant reduction of both tariffs and non-tariff restrictions; however, as discussed below, Mexico is at present unwilling to take this step toward implementing a free trade philosophy. Indeed there are signs that not only do powerful forces reject the ideology of free trade as propounded in GATT, but that even the current steps may go too far for certain groups. The next phase of liberalization (Phase II) was to introduce a two-year procedure starting in 1981 to remove import restrictions on all but 700 items on the tariff schedule. There are signs, however, that affected industries are calling in political IOUs, and either the procedure will be delayed or the number of items affected will be less than anticipated. In a few cases, such as beer and hi-fi equipment, quantitative restrictions have been re-imposed when foreign competition led to domestic complaints. In addition to the obvious interests of the protected industries, the maintenance of protection in such areas is justified ideologically by the argument in some governmental and academic circles that it is not in
the national interest to spend foreign exchange on luxury imports, regardless of whether a domestic market willing to pay high prices exists. The latter view is not without opponents in Mexico, but it does create a coincidence of interests between nationalist and statist officials, and intellectuals and elements of the private sector harmed by imports of consumer goods.

The Exchange Rate

The Mexican peso has traditionally been pegged to the U.S. dollar. Its value is mainly affected by relative inflation rates between the two countries and Mexico's trade deficit with the U.S. Pressure on the peso stems from the mutual free convertibility of the two currencies and the lack of any other restrictions on currency flows. The dollarization of the Mexican economy has made monetary restrictions difficult for Mexican authorities to implement.

With high and probably increasing inflation in Mexico (the rate was about 30% in 1980, over 28% in 1980, and probably considerably higher -- and perhaps up to 40%-45% -- in the late 1980s) the peso is increasingly overvalued. A number of factors work against devaluation, however. One observer notes that a projection of 30 pesos to the dollar by 1985 (the rate in January 1982 is now 22-23/dollar) would accommodate only half the anticipated change between Mexican and U.S. cost levels.° Petroleum exports make devaluation unnecessary in balance of payment terms and

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devaluation would produce even higher inflation rates since so much of Mexico's food, capital goods, and consumer goods are imported. In particular, given high levels of basic food imports, devaluation (without even more massive subsidies) would be especially hard on the poor.

Without devaluation, however, Mexican industrial exports will be squeezed between rapidly rising domestic costs and the sluggish exchange rate. At even a 25-30% inflation rate (the minimum that can be expected under present policies), in two years the cost relations will change more than profit margins. The implication appears to be that to increase earnings from manufactured exports, Mexico must either reduce inflation or devalue in the short run and increase productivity in the manufacturing sector in the long run. However, this squeeze may not be felt by the industries themselves, since overvaluation of the peso provides subsidized imported inputs for many industries which can be combined with production subsidies to reduce the pain of import competition for the final product.

Thus, like the situation for import quota protection, it is in the interest of certain manufacturing industries to maintain an overvalued peso. Like that situation, the nationalist ideology of some government and intellectual circles coincides with these interests somewhat. Traditionally it is an element of national pride for Mexican presidents not to devalue the peso. No Mexican president in the past several decades has devalued unless the outflow of funds into dollar accounts or abroad has been so great as to threaten the ability of the central bank to sup-

11Laura Randall, op. cit., p. 15.
port the peso. Immediately before the 1976 devaluation Mexico suffered capital flight of several hundred million dollars per day. While it may not be impossible, it will be very difficult politically for a Mexican president to devalue and to maintain his nationalist credentials in the absence of a balance of payments crisis. The Lopez Portillo administration appears to have opted for a series of mini-adjustments of only a few percentage points per year, which are not expected to resolve the problem of non-competitive manufactured exports.

Foreign Investment and Technology Transfer

The tension in Mexico between the ideologies of capitalism/internationalism and social justice-oriented nationalism with roots in the Mexican Revolution have always made the relationship between the state and private sector, and particularly the role of foreign investment (mostly U.S.), a politically sensitive one. While the private sector has been powerful both politically and economically, it has never had a legitimate place in the revolutionary coalition. There is not the degree of interpenetration of political and economic elites in Mexico that exists in most capitalist countries, and there is an undercurrent of hostility and suspicion between business and government that is not fully submerged even under an administration as favorable to the private sector as Lopez Portillo's.

The role of foreign investment is affected by both this underlying suspicion and by Mexican nationalism vis-a-vis the U.S. During the early 1970s, the concern of Mexican nationalists regarding the presence of foreign capital in key sectors led to the passage of several laws regulating foreign investment. The 1973 Law on Foreign Investment
expanded the requirements for Mexicanization of all enterprises, limiting virtually all new investment to 49% foreign equity and, in some crucial sectors, considerably less. The Transfer of Technology Law in the same year set limits to the amount that could be paid in royalties for foreign technology, as well as limiting the kind of technology that could be transferred. The two laws established commissions for overseeing foreign investment and technology, and for implementing the legislation in the national interest. A third and very controversial piece of legislation, the Law on Patents and Trademarks, restricted the rights of patent holders and required that within a certain period all foreign trademarks must be associated with domestic brands and so indicated in the packaging of all products. The latter provision was not implemented under Echeverría and has been so unpopular among multinational trademark holders that the López Portillo government has postponed it on a year-to-year basis.

U.S. direct investment in Mexico has declined from 81% of all direct foreign investment in 1970 to 70% in 1980. However, in terms of new investment in 1980, U.S. share was back up to 83%; total new direct foreign investment in 1980 was $1.2 billion, of which the U.S. accounted for $1 billion. Direct U.S. investment totals only 4% of total national investment in Mexico and 9% of private investment. Nevertheless, it tends to be in the most dynamic, capital intensive, and high-technology sectors of the economy, and nearly 90% is in manufacturing. The argument of the nationalists is that this gives U.S. and other foreign capital a control of economic activity way beyond its actual percentage participation. The legislation described above was therefore designed to limit the autonomy of foreign capital, assuring that foreign capital
would act to further the goals of government planners. Among these goals are: providing increased employment, investing in areas outside Mexico City, increasing usage of domestically manufactured inputs, and promoting exports.

There has been some shift in priorities for foreign investors under the Lopez Portillo administration. In technology transfer the emphasis has gone from keeping royalty payments low, to a de-emphasis on price as long as the technology allows penetration of international markets and/or the adaptation to Mexican market conditions, and helps substitute for imports. With regard to foreign investment, generally the post-petroleum boom attitude is that foreign investment is not so important for the capital it provides, but rather for the technology or expertise it brings and the increased capacity it provides (existing foreign market positions, for example) to increase Mexico's manufactured exports.

The major conflict within Mexico concerning the role of foreign investors and trade is, on the one hand, recognition that multinational companies do and will play a major part in improving Mexico's export capacity and, on the other hand, the suspicion in some government circles that such investors may disproportionately influence the direction of economic and social development. It is true that MNCs account for 25% more exports than their share of production in Mexico, and it is estimated that around half of trade takes place between subsidiaries and parent MNCs. Foreign companies investing in Mexico are thus likely to play an increasingly larger role in Mexican trade with the U.S. and elsewhere. On the other hand, foreign companies do not accept many of
Mexico's nationalist objectives and often resist and seek to avoid Mexicanization, the trademarks law, decentralization of industry outside Mexico City, and a larger role for the Mexican state in the economy. In addition, the MNCs resent much of the rhetoric and open suspicion voiced in Mexico over the role of foreign investors. Mexican policy toward foreign investment is likely to continue to exhibit an ambivalence between encouragement of foreign investment as a major part of its export-led growth policies, and suspicion of foreign investment as potentially disruptive of a socially-oriented and independent development model.

The Agriculture Debate

Agriculture is likely to be the single most important social, political and policy area for Mexico in the 1980s and 1990s. Doing justice to the social, political, and economic complexities of this sector would lead us too far afield for the present discussion of the direct and immediate implications of agriculture for Mexico-U.S. trade policies.

The rural areas are Mexico's political Achilles Heel. Rural underemployment may be as high as 60%, and despite the fact that there exist a vast number of peasant associations, and that the official party bases one of its three official sectors on peasant representation, peasants have never really been incorporated into the political system to the extent that skilled labor has. Instead, the government has used tactics of divide-and-rule, cooptation, bribery, and outright repression to keep the peasantry -- those who benefit least from the regime -- passive and divided. The most significant device for maintaining social control in the countryside is land reform and the ejido system.
After the consolidation of the Mexican Revolution and into the 1930s, Mexico embarked on a major land reform program by expropriating large estates from private owners and turning over these and some government-owned land to peasants for their use. The land is divided into units called ejidos. Most are farmed collectively but all are owned by the state and cannot be sold, yet can be passed down to heirs. Approximately half the cultivable land in Mexico is under the ejido system, while the other half is owned by private individuals. Some of these private owners are small farmers and differ little from the ejido farmers, but a few -- and these control the bulk of the irrigated land -- are owned or otherwise controlled by large-scale producers. These large farmers are economically and (because of ties to the state and national governments) often politically dominant in the regions where they farm. They are concentrated in the northern states of Sinaloa and Sonora, tend to produce for export, farm mostly irrigated land, have access to credit and agricultural inputs unavailable to ejido farmers and other small producers. The latter tend to farm in rainfed areas with attendant uncertainties of weather, and to produce subsistence crops and basic foodstuffs such as corn and beans.

During the past 10-15 years, Mexico has had to import large quantities of grain and other basic foods while exporting crops like winter vegetables, cotton, and coffee. In recent years the presumed "comparative advantage" of this strategy has turned against Mexico, and some observers believe that by 1990 food imports will eat up over half of petroleum revenues, totally overwhelming agricultural export revenues. These and other considerations have led the Lopez Portillo government to
re-emphasize the production of basic foodstuffs through the Mexican Food System (SAM). SAM proposes to revitalize the rainfed areas and to make changes in credit availability, agricultural pricing, and other key policies which will increase the productivity of those who grow basic foods, i.e., ejido and other small-scale farmers.

The problems with this approach are numerous, but for our purposes the key one is the implicit conflict between agriculture for export and agriculture for internal consumption. While SAM claims to be interested in increasing production of basic foods but not in reducing exports, many agricultural experts note that it is very unlikely that both hopes can be realized. In other words, it is very unlikely that the rapidly growing Mexican population can be fed solely from rainfed agriculture. This goes to the heart of the debate over the Mexican development model. Will policy emphasize basic food self-sufficiency, small farmers, and employment through labor intensive agriculture, or will there by a continuation of policies which support export agriculture, rural dependence on imports and exploitive distribution and marketing systems, large and privileged farmers, and unemployment in rural areas because of mechanization and other capital-intensive methods? The argument is clearly much more complex than stated above, and the above formulation leans toward those who oppose an emphasis on export agriculture. Nevertheless, the issue represents a real choice and one which will be very politically sensitive to make -- if it can be made at all. Indeed, if attempts were made to actually carry out a food self-sufficiency policy, the political ramifications in terms of power shifts among social groups
in the rural areas might well be equivalent to a second Mexican Revo-

lution.

In terms of trade relations between the U.S. and Mexico, three
related issues are or will be the focus of conflict. The first is a
general one and may be formulated as Mexico's fear of "the food weapon." If Mexico becomes permanently dependent on basic food imports from the
U.S., then, according to this view, the U.S. will be able to exert undue
pressure on Mexico for all kinds of trade and other concessions by sim-
ply withholding grain. 12

A second issue is the equivalent of the first with regard to Mexi-
can food imports into the U.S. This will be discussed more fully in the
section on specific products but, put simply, Mexican exports of winter
vegetables, for example, are seen as extremely vulnerable to non-tariff
barriers -- such as anti-dumping petitions and suits -- initiated by
protectionist groups within the U.S.

The third issue relates to agricultural development and the entry
into GATT. Mexican opponents of GATT argue that while the U.S. pro-
tects its agriculture through non-tariff barriers such as anti-dumping
legislation, Mexico's policies to stimulate agricultural production
through subsidies and incentives run afoul of the GATT regulations.
This issue will be discussed in more detail below.

12Steven E. Sanderson. "Florida Tomatoes, U.S.-Mexican Relations
and the International Division of Labor." Paper prepared for the
Latin American Studies Association Meetings, Bloomington, Indiana,
October 1980, pp. 33-34.
Ideologies, Institutions and Interests

We have discussed the differences in historical experience and models of development which form the background to trade conflicts between Mexico and the U.S. At a somewhat less abstract level, there are ideologies and perceptions of government officials and key opinion leaders, institutional decision-making processes, and perceived national interests at variance between the two countries.

The difference in perceptions is linked to a broader ideological distinction which, stated in oversimplified form, is: In the U.S. the reliance on the free market, and therefore free trade, is the only available ideology (whatever the deviations in practice), while in Mexico the state is regarded as the only mechanism which can guarantee the desired balance between social justice and economic growth. The general view in the U.S. is that Mexican protection will inevitably produce inefficiency, while the Mexican argument is that a planned mix of protection and competition is the only way to lay an industrial export base. A former U.S. Department of Treasury official has rather neatly phrased the corresponding difference in institutional practice as between Mexico City planners dealing in targets and Washington lawyers dealing in rules.13 These differences, for example, are at the heart of much of the debate over Mexico’s entry into GATT.

Centralization in Mexico versus decentralization in the U.S. is

13 Hufbauer, et. al., op. cit., p. 141.
another aspect of the decision-making process which affects the trade
debate. The U.S. is politically incapable of targeting only certain
selected industries for export promotion, while this is the basis of the
Mexican NIDP. In the area of protection, as noted above, Mexico has
recently moved toward a more centralized system for managing protection.
The U.S., in contrast, has maintained or even expanded a decentralized
system of implementing such non-tariff barriers as anti-dumping and
countervailing duties provisions. In the 1979 Trade Agreements Act, for
example, considerable discretion over the control and timing of these
protectionist tools is removed from the executive branch and passed to
the courts -- thus placing protectionist initiative more in the hands of
U.S. domestic industry affected by import competition. Because of
these and other differences in perspective and processes of institu-
tional decision-making, the two countries, often correctly, perceive
their objective interests to be in conflict. This is generally recog-
nized more clearly in Mexico than in the U.S.

Each country tends to label the other's trade policies as motivated
by "politics." In the most extreme cases, the U.S. use of the word for
Mexico tends to mean "irrational and/or paranoid," while the Mexican
formulation vis-a-vis the U.S. means "Machiavellian." In the U.S., the
issues most commonly mentioned are Mexico's deferral of entry into GATT
and Mexico's insistence on an independent petroleum production/export
policy. These are seen as motivated by a somewhat irrational view of
U.S. intentions toward Mexico. In Mexico the issues mentioned are the
motives behind the Generalized System of Preferences, GATT, and U.S.
interest in Mexican petroleum. The GSP is seen not as an effort to aid
developing countries but as a tactic to undercut the unity of the
UNCTAD/Group of 77 nations. GATT is often seen not as a multilateral trade agreement but as a multilateral "cover" for a series of bilateral agreements between key world economic powers. The most negative Mexican interpretation of U.S. motives regarding petroleum is that the U.S. regards Mexico as "an oilwell."

It should be emphasized that these are the most conflictive interpretations of these issues. Most policy-makers recognize that the issues are more complex and that, to the extent that real interests do conflict, mutually satisfactory compromises may be negotiated. Because both sides know that these interpretations are the opening round in a prolonged negotiating process, both are at pains to define the terms of the negotiation in a way most favorable to themselves. In this sense both are taking a rational view. In the following examples of specific Mexico-U.S. trade issues, it should be noted that at one level the debate concerns the substance of the issue, at another level the debate is over the tactical and strategic advantages or disadvantages for Mexico vis-a-vis the U.S.

The Generalized System of Preferences (GSP)

While the GSP (Title V of the 1974 Trade Act) is generally seen by the U.S. as highly advantageous to Mexico, many Mexican commentators point to its deficiencies, both substantive and political. Mexico was the principal Latin American beneficiary of GSP in 1979, exporting $546 million to the U.S. under its provisions (up from $245 million in 1976). This represented 6% of Mexico's total 1979 exports.

Some Mexican commentators point out that, in comparison to Mexico's
needs, the GSP is extremely inadequate. 14 Five weaknesses mentioned by del Castillo are: 1) Textiles are excluded from GS, 2) There are unrealistically low competitive need limits which, along with other exceptions, reduced Mexico's actual exports in relation to potential by 75%, 3) Certain agricultural products are excluded, 4) There is vagueness and administrative discretion written into the law which allows many items to be barred by customs officials at the border for "administrative reasons," and 5) There are beginning to be moves to "graduate" Mexico from GSP for certain products. The latter two points are sometimes interpreted in Mexico as politically motivated in order to influence Mexico to make decisions in line with U.S. trade policy (such as joining GATT). The overall substantive objection is that the GSP forces Mexico to export moderate amounts instead of large amounts of products in precisely those areas where its comparative advantage is greatest. Indeed, Mexico has shifted some exports to sections 806.30 and 807 of the Tariff Code (those relating to in-bond industries) because these do not have restrictive ceilings. The disadvantage under the latter sections is that local Mexican components cannot be imported duty-free into the U.S.

In addition to the substantive objections, the GS is seen in some circles in Mexico as motivated by the desire to divide the developing countries between the so-called Newly Industrializing Countries (NICs) like Mexico, which would benefit considerably from the GS, and other

LDCs, which would not. The GSP, under this interpretation, is part of an OECD strategy to prevent Third World unity, to scuttle UNCTAD efforts, and to split the group of 77.

**Protectionism in the U.S.**

A Mexican concern related to the above discussion is that the U.S., while calling for an end to protection in Mexico, practices protection on its own terms. The 1974 and 1979 Trade Acts in the U.S. provide a number of non-tariff tools for alleviating the impact of foreign competition which have or may bring the U.S. and Mexico into conflict in specific areas. The 1979 Trade Act did more than simply codify fair trade rules because, as we have noted above, it gives more control to the U.S. private sector, through the courts, over the timing and selection of protection issues. The most publicized case of conflict was the petition by Florida tomato growers to have the Commerce Department find that Mexican growers were dumping (selling below cost) winter tomatoes on the U.S. market. Though the Commerce Department found in favor of the Mexicans, i.e., no dumping, the Florida growers now had the right to file suit in customs court and have in fact done so. Some U.S. officials expect further suits over winter vegetables and such products as ammonia, of which Mexico is the largest exporter to the U.S.

In addition to anti-dumping legislation, a number of protectionist tools may be used against Mexican exports. These include: countervailing duties, unfair trade practices, and import relief action provisions. A countervailing duties suit has already been filed against Mexican imports by a company representing the leather apparel industry; an
unfair trade practices suit was thought to be in the works with respect to Mexican auto parts exports; and import relief action may still be applied to Mexican auto exports because of local content and export performance requirements for the auto industry in Mexico. In addition, specific pieces of U.S. legislation protect U.S. industry against Mexican imports in key products where Mexico has a comparative advantage. These include textiles (the Multifiber Agreement), cheese, and shoes.

Finally, the issue of unskilled labor migration from Mexico must be mentioned here. While Mexico is not unambivalent about the costs and benefits of Mexican migration to the U.S., it is pointed out that the unwillingness of the U.S. to allow the free flow of labor across the border contradicts the free market/free trade ideology which the U.S. uses to argue the need for a dismantling of Mexican protectionist and other barriers to the free flow of U.S. goods and capital across the border.

The GATT

With the possible exception of petroleum and the "Tomato War," Mexico's announcement in mid-1980, after many months of negotiation and debate, that it would defer entry into the GATT, has caused more concern in the U.S. than any other trade-related issue. While the issue does not constitute a direct conflict, it is certainly true that U.S. private sector organizations and the U.S. Government, had been making major efforts for over a year to induce Mexico to join.

The GATT issue points up most clearly the two levels of trade conflict between Mexico and the U.S.: substance and strategy. In the final
analysis, the U.S. emphasized the immediate substantive advantages for Mexico of joining, while Mexican opponents of GATT emphasized strategic disadvantages. It should be pointed out that the GATT decision was hotly debated within Mexico, and there is every indication that President Lopez Portillo himself favored entry into GATT.

Puzzlement in the U.S. over the Mexican decision is partly based on the fact that, as one U.S. Treasury Department official noted, Mexico negotiated the best GATT entry protocol ever negotiated. Mexico is the largest U.S. trading partner not in GATT, and U.S. officials emphasize the importance of developing a framework to negotiate trade issues quietly, to avoid having each potentially conflictual issue or product become politicized and damage the overall relationship. In addition, one aspect of the favorable entry protocol was that Mexico had a long grace period (in some cases up to twelve years) to adjust its tariff and non-tariff trade policies to the requirements of GATT.

Some U.S. officials feel that even more important than joining GATT itself would be the signing by Mexico of the associated Subsidy and Countervailing Measures Agreement. This agreement covers the main issue between the two countries regarding imports of Mexican products into the U.S.: the fact that Mexican export policy is based on subsidies and incentives to encourage domestic industry, while U.S. anti-dumping and countervailing duties legislation are designed precisely to counteract such a policy. The U.S. argument is first, that if Mexico does not sign the Subsidy and Countervailing Measures Agreement, U.S. industry will not have to show injury (a difficult procedure) in order to have countervailing duties applies against Mexican products; and second, that
there will be no framework for negotiating the politically damaging conflicts that are likely to ensue in specific product areas. Several U.S. officials stated that Mexican opponents of GATT apparently believed (as a result for example, of the Commerce Department finding of "no dumping" in the tomato case) that the U.S. executive branch, whatever the rhetoric, would never actually apply countervailing measures against Mexican goods for fear of damaging U.S.-Mexico relations and losing access to Mexican petroleum exports. In the view of these same U.S. officials, however, this calculation was mistaken because of the decreased discretion given the executive branch by the 1979 Trade Act. They foresaw a number of trade conflicts as potentially quite damaging to U.S.-Mexico relations as a result of court cases out of the control of the State Department, Commerce Department, or even the White House. Such conflicts could damage the possibility of further progress even in the area of bilateral U.S.-Mexico trade agreements.

This brief description of the U.S. perspective reveals that a number of threads discussed in previous sections of the paper reappear in the GATT decision: the U.S. view that eventually Mexico must move toward a free trade orientation; the Washington preference for general rules; the emphasis on a decentralized trade policy-making process; and the hint that the Mexicans are miscalculating their own true interests.

A final aspect of the U.S. view that has not been mentioned becomes important as we discuss the Mexican view: the U.S. preference for a multilateral rather than a bilateral format for negotiating trade issues with Mexico.

The basis of Mexico's opposition to entry into GATT may be divided
into those arguments which refer to Mexico’s strategic negotiating position vis-a-vis the industrialized world, especially the United States, and arguments which refer to the specific aspects of the entry protocol.

Three related points underlie the strategic argument:

- Entry into GATT, regardless of specific exceptions negotiated for Mexico, implies accepting the rules of the international trade game laid down by the U.S. and Europe. Mexican entry into GATT means at least tacit acceptance of a free trade ideology and the gradual elimination of protection, regardless of how much domestic policy-makers feel it is inappropriate in specific cases.

- The multilateral context for negotiating trade issues puts Mexico at a disadvantage vis-a-vis the U.S., its major and overwhelming trading partner. For the first time in history the U.S. needs trade with Mexico as much as or more than Mexico needs trade with the U.S. This is true not only because of U.S. petroleum needs, but also because, with the oil boom, the internal Mexican market will expand rapidly and provide the opportunity for the U.S. to expand exports which are increasingly crucial to maintaining the value of the dollar and financing its other trade deficits.

- The format of GATT is both too broad and too narrow. It is too broad because it really does not address the key areas where the developed countries exercise protection against exports from the developing countries. Mexican opponents to GATT argue that, in reality, crucial products are negotiated on a bilateral basis; for example, U.S.-Japan agreements on color TV sets, and agreements with other countries on steel, shoes, boat construction, textiles and other products. These bilateral agreements come precisely in the areas where developing countries, including Mexico, have a competitive edge. The format of GATT is considered too narrow because, like the GSP, it is seen as partly a political effort to split the Newly Industrializing Countries from other LDCs, and thus derail the Group of 77. Unlike the UNCTAD proposals, GATT does not deal with issues of structural changes in the international trade system, such as regulating world markets and the use of international capital.

With reference to the specific content of the GATT and Mexico’s entry protocol (which even the opponents accept as a relatively favorable one), three other points are worth mentioning:

- The rules and the spirit of GATT affect not so much current Mexican policy but projected future policies. While GATT and its associated tariff code agreements foresee the gradual...
elimination of tools like quantitative controls, subsidies and public sector purchases, Mexican planners foresee the imposition or withdrawal of such measures as the situation warrants into the foreseeable future. In other words, a quota might be lifted for a product and then reimposed in a few years. The GATT would prevent such freedom without extensive consultation and trade-offs on a case-by-case basis.

- Mexico can rationalize its system of protection without entry into GATT.

- Entry into GATT would prevent Mexico from playing its "oil card." GATT does not recognize the freedom to restrict trade in non-renewable resources unless this is accompanied by internal production/consumption restrictions. The Mexican view is that this not only restricts national sovereignty in an unacceptable way, but also prevents the use of petroleum agreements as a selective tool to receive special commercial preferences.

We have mentioned that the decision by Mexico to defer entry into GATT--occasioned both a difference of opinion with the U.S. and a major debate within Mexico. While Lopez Portillo is believed to have favored entry into GATT, he took no active public role in the debate. Instead, an unusual political process took place within Mexico. The President encouraged a protracted public debate on the issue and apparently abided by the result. This is probably a result of the fact that the left -- those who support a more nationalist development model -- lined up against GATT, and because of a number of other decisions, such as increases in the petroleum production platform, for which the government was already under fire for tipping the political balance too far toward capitalist internationalism. Thus, in the ongoing internal debate over the development model in Mexico, the GATT became an important substantive and symbolic issue. While Lopez Portillo defined the rules of the debate by prohibiting cabinet ministers from taking an active role, the line-up was much as might be expected. The Ministry of National Patrimony and Industry and groups like the Colegio Nacional de Economistas
opposed entry. In addition, some small and medium-sized firms opposed entry, as did the Ministry of Agriculture (representing some import-sensitive farmers). The Ministry of Commerce and the large industrial groups, especially those linked to multinational companies, supported entry, as did various conservative economists. In this sense the GATT decision was at the center of the most important permanent policy issue in Mexico over the past 40 years in Mexico: capitalist internationalism vs. statist nationalism.

INDUSTRY - SPECIFIC ISSUES IN U.S.-MEXICO TRADE RELATIONS

The following cases are a brief sampling of the product areas where many of the trade issues discussed in the previous sections have been or probably will be played out.

Tomatoes/Winter Vegetables

In 1979 and 1980 the most publicly visible trade conflict between Mexico and the U.S. involved a petition by Florida Tomato growers that the Treasury Department (and subsequently the Commerce Department) find that Mexican growers of winter tomatoes were dumping their produce on the U.S. market. The issue is important because it illustrates the conflict between the decentralized forces of U.S. protectionism and the efforts by the U.S. executive branch to contain these forces in the interest of improving U.S.-Mexico relations. It is also important because it involves an area -- agricultural exports -- which earns a large amount of export revenue for Mexico (fruits and vegetables were valued at over $500 million in 1979) and where other issues of this kind may arise; for example, with regard to other fruits and vegetables,
hides and skins, and pork. The issue was a complex one and illustrated a pattern which is likely to show up increasingly in U.S.-Mexico trade relations. It was less a conflict between the U.S. and Mexico than it was a conflict between coalitions extending across national boundaries. It pitted Florida tomato growers against an international coalition of Mexican producers in Sinaloa and Sonora and U.S. distributors in Arizona and elsewhere in the Southwest. The role of the U.S. executive branch was that of attempting to balance the outcome between maintaining harmonious relations with Mexico and avoiding the wrath of Florida growers in an election year.

The Automobile Industry

In 1977, the Mexican government issued an auto decree designed to achieve a balance in exchange earnings on automotive vehicles and auto parts. It replaced a policy of requiring the mostly foreign-owned auto companies to meet a 60% local content requirement. Instead, the 1977 decree introduced a package offering tax, credit, and capital goods import incentives to attract further investment and the option of either meeting a 75% local content requirement by 1981 or trading this off against increased exports (usually to the parent company in the U.S., Germany or Japan). In addition, price controls were relaxed for the domestic market. For this and other reasons, Mexico benefited from massive new investments in 1979-80 on the part of the U.S. big three plus Volkswagen and Nissan.

15 Steven E. Sanderson, op. cit.
While Mexican goals of balanced trade in the auto industry by 1985 are probably overly optimistic, the size of the investment by the U.S. companies suggests that by mid-decade Mexican exports of auto parts to the U.S. may be well above the 1979 figure of 2% of parts imported into the U.S. Potential conflict centers around the complaint by U.S. auto-workers that Mexican policy, and the auto companies' response, is exporting needed jobs from the U.S. to Mexico. According to U.S. trade officials, this may be an area where Import Relief Action provisions may be applied. These officials also note the possibility that similar policies in Mexico might be applied to petrochemicals, textiles, and steel. The issue of job exports from the U.S. has also been raised for some time by the in-bond industry (maquiladora) program, which grew from $3 million in value added in 1966 to over a $1 billion in 1979. Autos and the other product areas mentioned here exhibit a somewhat similar pattern to winter vegetables in that the conflict promises to be between international coalitions, in this case U.S. labor (and perhaps some domestic manufacturers) versus the Mexican government (at least implicitly) and multinational companies.

**Pharmaceuticals**

The pharmaceutical industry illustrates what is seen by the Mexican Government as essentially a conflict between Mexican nationalism and the practices of some multinational companies. Current political processes are the culmination of at least a ten year effort by Mexican nationalists to have foreign firms manufacture pharmaceuticals from primary products in Mexico, rather than simply marketing them there. Over 85% of the market is controlled by foreign firms. Pharmaceutical companies
have been a major target of the left because they are seen as charging higher prices than if they were integrated domestically, and because the area is considered vital for national self-sufficiency (second only to food). Pharmaceuticals, because of their relationship to health care for the poor, are central to the social justice component of Mexican nationalist ideology. Most pharmaceutical companies have strongly resisted efforts by at least two Mexican presidents to make them integrate their operations. In 1980 the government decided that the right to produce and market pharmaceuticals would be auctioned. Bidders would be required to export, to incorporate local primary materials, to limit payments for technology transfer, and to reduce foreign equity from the current average of 85% to 49% or below. Import ceilings on raw materials as well as export targets were set. While this product area is characterized more by domestic conflict than those described above, it has clear implications for trade and the way that, particularly from the Mexican perspective, trade issues shade imperceptibly into issues of world market structure and the movement of international capital -- issues which are not addressed by GATT and other OECD-initiated multilateral trade agreements. In addition, the issue illustrates what is perhaps an earlier stage in the relationship between the Mexican government and MNCs than is represented by the auto industry. Automotive policy was quite conflictual during the mid-1970s. The 1977 auto decree has shifted the basis of the conflict from one between certain Mexican government officials and foreign auto companies, to one between an alliance between the Mexican government and MNCs versus manufacturing and labor groups in the U.S.
**Petrochemicals**

The petrochemical industry is one of the major export growth industries targeted by both the National Industrial Development Plan and the Global Development Plan. According to projections in these plans, growth of secondary petrochemical exports will be 19% per year in the early 1980s. Fertilizer export growth is projected at 10% per year. This level of growth is based on subsidized energy inputs. The obvious market is the U.S. and if the targets are met, imports from Mexico might be high enough so that injury to domestic manufacturers could be shown. U.S. trade officials predict that this is an area where unfair trade practices and relief action provisions in U.S. law may be invoked — possibly leading to conflict between the U.S. and Mexico.

**CONCLUSIONS**

The next five years in U.S.-Mexico trade relations will bring potential conflict in many of the areas we have mentioned. The way these are resolved will, of course, depend primarily upon the course of overall U.S.-Mexico relations. Petroleum need not be a major area of conflict if the U.S. does not press Mexico to adopt any particular production or export policies. There are signs that this is beginning to be understood in the U.S. The issue most likely to trigger conflict is not directly related to either oil, trade, or even to Mexico, but rather the possibility of U.S. intervention in Central America. If the U.S. becomes overly or publicly concerned either about Mexico's role in support of the left in Central America, or about the security of Mexican petroleum in the event of increasing revolutionary activity in Guatemala, El Salvador and Honduras, then relations with Mexico will
deteriorate along a broad spectrum.

In the area of trade, the two most likely areas of conflict are, first, continued U.S. protection in areas where Mexico already has comparative advantage -- textiles, shoes, certain agricultural commodities, and certain other labor-intensive industries. The "tomato war" was resolved temporarily in favor of the Mexican producers, but the issue is in the courts and might not only be reversed, but might also lead to further petitions and suits over similar products. Second, if Mexico's Industrial Development and Global Development plans approach their targets for the mid-1980s, there may be increased usage of non-tariff barriers (countervailing duties, etc.) against Mexican exports which benefit from subsidy and incentive programs in Mexico (including energy subsidies). Some Mexican officials apparently believe that these issues will be resolved in Mexico's favor -- and events so far bear out this belief -- but decreasing U.S. executive discretion and increased Mexican exports of auto parts, petrochemicals, steel, and capital goods could trigger a severe negative response in the U.S. One factor which may render these issues moot is the strong possibility that in spite of export targets in Mexican plans, internal bottlenecks, increasing inflation, and rising domestic consumption will reduce Mexico's capacity to export these products in the near term.

In addition to potential conflict, there will undoubtedly be considerable mutual adaptation. The area where this is most likely is bilateral agreements on trade. We have seen that Mexico deferred entry into GATT in part because the multilateral character of GATT did not fit Mexico's current strategic objectives. The Reagan Administration may
decide that a series of bilateral agreements is the only way in which potential trade conflicts can be resolved given Mexico's decision. Areas in which such agreements might be expected in the near future include: petrochemicals, manufactures from in-bond industries (Mexican exports), food and food packaging and processing material, transportation and storage goods, and services and technology transfer. In addition to a U.S. move toward bilateral and industry-specific agreements, Mexico may be expected to feel the need to move toward legislation similar to that of other developed countries, with laws on anti-dumping and assistance to industries affected by foreign trade, thereby supplementing or substituting for current quantitative import restrictions.

In addition to conflict and adaptation, the future of Mexico-U.S. trade relationships will be characterized by increasing integration and increasing complexity of alliances and conflicts. Mexico rejects an idea often mentioned by business and other circles in the U.S., i.e., a North American Common Market. This is seen as either a veiled attempt to acquire Mexican oil and gas, or at best as leading to a process which will merge the Mexican development model with that of the U.S. Nevertheless, even without any formal agreements, the process of integration is taking place and is likely to continue. Bilateral agreements will further the process, as will increased U.S. investment in Mexico's auto industry, expansion of the in-bond industry program, and continued labor migration. Some see the move toward a de facto common market in the possible expansion of the free zone and overland smuggling of gasoline north and of cheaper U.S. goods south. To this can be added the growing dollarization of the Mexican monetary system.
Integration brings new alliances and cleavages which cut across international boundaries. Some authors view this in the context of a new international division of labor.\textsuperscript{16} Whatever the theoretical construct, it is clear from our discussion of tomatoes, auto parts, in-bond industries and other areas that trade conflict will not be simply between Mexico and the U.S., but between more complex international alliances of capital, labor, consumers and governments in both countries. This will feed directly into the policy debate within Mexico about the most appropriate development model.

Mexico and North-South Trade Issues

To some extent, Mexican trade issues vis-a-vis the U.S. are atypical of the general run of such issues. Mexico's oil, its physical proximity to the U.S., its historical relationship to the U.S., and its rather unique political system and internal balance of political forces make it an unusual case. On the other hand, Mexico shares (sometimes in an aggravated form) much of the perspective of "the South" because of its level of industrial development, its extreme social inequalities, its large population of rural poor, and its areas of comparative trade advantage (primary materials and labor intensive industries). It therefore seems appropriate to conclude with three observations concerning the role of trade issues and conflicts in the Mexican social and political system, and the manner in which these contrast with the situation in the industrialized world.

\textsuperscript{16} Ibid.
First, trade policy and trade issues are at the center of the political debate in Mexico. Far from being a residue of other policy, trade issues are viewed as representing crucial choices about the direction of Mexican political, social, and economic development. The petroleum debate, the agriculture debate, and the GATT debate are only the most obvious examples of such centrality.

Second, and closely related to the above, unlike in developed capitalist countries, there is an ideological alternative to free trade in Mexico. The model of statist nationalism and its associated commitment to social justice and its view of private capital as almost a necessary evil, often incline the state to reject free trade as a goal. There is lively disagreement on this issue within Mexico, but it is not a question of how much protection is possible under an essentially open system. Rather, it is a debate in which the ideology of free trade must compete with a more statist alternative.

Third, and most importantly, a possible reason why trade is at the center of the policy debate, and why free trade is not an unchallenged ideology, is the fact that social inequality is a life-or-death matter to the regime. Because the Mexican political system is "post-revolutionary," and built upon a delicate balance of forces, the regime must constantly preside over the social equality debate. Some developing countries, such as Brazil in the 1960s, Argentina and Chile can submerge this debate for a time under repressive military authoritarianism; that, however, is unlikely to be the end of the story.

In a society like Mexico, where social inequality (unlike the developed world) is an immediate and explosive issue for the survival of
the political system, protection, subsidies, and a variety of state interventions in the economy are crucial to the arsenal of weapons by which the state maintains social order. In this sense protection is the cost of maintaining social inequality. A free trade policy would be literally revolutionary in its implications. It will be interesting to observe in this regard whether the Southern Cone countries will be able to avoid these revolutionary implications by means of military authoritarianism. Asian societies such as Taiwan, and, to a lesser extent, Korea, have embraced a policy of free trade and open economy only after first traveling the route of revolutionary reform to reduce social inequality. Mexican society is extremely unequal and, while authoritarian in some ways, is also open to influences from a wide variety of social forces. Mexico therefore illustrates perhaps most clearly the dilemma shared by many of the newly industrializing countries: how to maintain political stability while moving toward export-led growth without a radical restructuring of society.
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