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The Domestic Determinants of Mexico's Trade Strategy

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Abstract

This working paper examines Mexico's trade policy from the late 1980s to the present. The first section reviews Mexico's trade strategy and revealed preferences, while the second one examines its domestic determinants. Regarding the domestic determinants of trade policy, attention is paid to structural factors (trade partners and comparative advantage), and to actors and institutions (the executive, the legislature, business organizations and civil society actors). The paper finds that Mexico's trade is concentrated in terms of markets, import and export composition, and the number of firms with significant exports, with negative economic and political effects for Mexico. The paper argues that Mexico lacks a coherent trade strategy, and that the institutional setup and the preferences of actors affecting trade policy represent a bias in favor of the status quo. This means that Mexico is ill prepared to maximize the benefits and minimize the costs derived from preference erosion of its preferential trade agreements and from multilateral trade negotiations.

Resumen

En el presente trabajo se hace una revisión de la política comercial de México desde la década de 1980 hasta la actualidad. En la primera sección se presenta la estrategia comercial y las preferencias reveladas, y en la segunda se examinan los determinantes nacionales de dicha estrategia y preferencias. Por lo que toca a los determinantes, se hace particular énfasis en factores estructurales, como los patrones de comercio y las ventajas comparativas, y en instituciones y actores, incluidos los poderes ejecutivo y legislativo, las asociaciones empresariales y los actores de la sociedad civil. Se concluye que hay una gran concentración del comercio de México por lo que se refiere a mercados, composición de las exportaciones e importaciones, y número de empresas que participan de manera significativa en el comercio exterior, y que esta situación conlleva consecuencias negativas tanto en lo económico como en lo político. Asimismo, se argumenta que no existe una estrategia comercial coherente, y que la configuración actual de actores y preferencias en torno a la política comercial representa un sesgo en favor del status quo. Esto significa que México probablemente no está preparado para maximizar los beneficios y minimizar los costos derivados de la erosión de preferencias de sus acuerdos comerciales preferenciales y de las negociaciones comerciales multilaterales.

Introduction

Mexico has been a laggard and a leader in trade policy. It initiated hesitant trade liberalization in the 1970s, only to end up with a closed economy in 1982. As part of macroeconomic liberalization efforts it liberalized its economy on a unilateral basis during the 1980s and joined General Agreement on Tariffs and Trade (GATT) until 1986, making it the newest participant in the multilateral trading system among the countries included in these studies.¹ Starting in the 1990s the country embarked on a series of bilateral and regional trade negotiations, among which the North American Free Trade Agreement (NAFTA, 1994) and the Association Agreement with the European Union (EU, 2000) stand out. As of 2005, Mexico had free trade agreements with 43 countries encompassing the Americas, Europe, the Middle East (Israel) and Asia (Japan).²

It thus appeared that, after being a laggard in trade policy, Mexico had become one of the world leaders in trade and had a clear strategy. However, during the past few years Mexico seems to have lost its sense of direction: Congress has sought a stronger voice in the determination of trade policy, some business groups have asked for a moratorium in the negotiation of free trade agreements, and at the same time the Ministry of the Economy has pursued further unilateral liberalization. Preference erosion and especially Chinese exports are affecting Mexico's participation in the US market while exports to other markets have not grown as much as expected. With the advent of democracy in 2000 trade policymaking has become more pluralistic and likewise more complex; unless and until a broad consensus regarding the basic outlines of trade policy is reached it will not be possible for Mexico to have a coherent trade strategy.

This paper examines the recent evolution of Mexico's trade strategy by providing an overview of the use of tariffs and non-tariff measures, export promotion schemes, and regional and multilateral initiatives (section I). It then addresses the role played by structural and institutional factors in determining Mexico's policies, including trade patterns in terms of markets and composition, domestic political institutions and key economic and political actors (section II). It concludes by highlighting the challenges for the next six years, *i.e.* for the government that will be in power from 2006 to 2012.

¹ This paper will be part of an edited volume comparing case studies of domestic politics and trade policy in MERCOSUR countries, Chile, and Mexico.

² This paper does not attempt to provide a history of Mexico's trade policy. For background on Mexico's trade policy reforms and trade strategies see, *inter alia*, Blanco 1994, Pastor and Wise 1994; Flores, 1998; Ortiz Mena L. N. 2004a; Ortiz Mena L. N. 2004b; and Ortiz Mena L. N. 2005a.

Mexico's Strategies and Revealed Preferences

Given Mexico's significant unilateral liberalization in the 1980s, its participation in the Uruguay Round and especially its active pursuit of free trade agreements since the early 1990s, tariffs are quite low. The bound level most-favored-nation (MFN) tariff is 35%, although applied rates are commonly lower. However, non-tariff barriers remain important, especially the use of anti-dumping (AD) actions.

Export policies focus more on administrative actions, such as sectoral programs comprising, among other measures, unilateral tariff reductions on temporary imports, than on adequate financing of exports.

Import Policies

Tariffs, Import and Export Permits

Mexico's bound tariffs rates are a relatively high 35%. On an MFN basis, the simple average of ad-valorem duties on all goods is 18% (24.5% for agricultural goods and 17.1% for non-agricultural goods). MFN duty free imports were about 10% of all imports in 2001.³ Given Mexico's reliance on trade with free trade agreement (FTA) partners, both the simple average of applied rates and especially trade-weighted averages are much lower.

³<http://stat.wto.org/CountryProfile/WSDBCountryPFView.aspx?Language=E&Country=MX.>, Accessed on October 3, 2005.

Table 1
Mexico's Tariff Structure

<i>Item</i>	<i>1995</i>	<i>2000</i>	<i>2005⁴</i>
M tariff lines	11089	11439	11929
% of controlled M tariff lines ⁵	0.99%	0.99%	0.99%
X tariff lines	5329	5303	11929 ⁶
% of controlled X tariff lines	0.98%	0.99%	1%
Simple average ad valorem M duty	13.7%	16.2%	13.7%
Weighted average ad valorem M duty	2.9%	3%	3.5%

Source: Presidencia de la República, 2005, 351.

Table 1 reflects a great deal of stability during the last ten years regarding Mexico's tariffs, although it is striking that the weighted ad valorem import duty has increased slightly despite the fact that the implementation of FTAs has proceeded apace since January 1994. Countries with which Mexico does not have an FTA do face significant discrimination on an average ad valorem basis, and at any time applied rates can increase to 35%.

Controlled imports and exports constituted approximately 1% of tariff lines during the past decade, although this figure decreased as of November 10, 2005 with the elimination of all temporary import permit requirements. This streamlining will apply, inter alia, to the following sectors: agriculture, chemicals, ceramics, glass, rubber, iron and steel, greases and oils, tuna, clothing, textiles, footwear, wood, kitchen appliances, toys, and bicycles. Import permits will still be required for some final imports, covering 192 tariff lines and some of the following sectors: imported oil derivatives, used tires, used clothing, fructose, used vehicles (49 tariff lines), automobile and truck components, anti-pollution equipment, agricultural items contained in

⁴ Figures for 2005 are estimates calculated in June.

⁵ Tariff lines are classified as free, controlled and prohibited. The original table has "controlled" and "prohibited" tariff lines but here both are added and reported as "controlled."

⁶ The number of X tariff lines increased substantially after 2002 after they were adjusted according to World Customs Organization provisions.

Economic Complementation Agreements (ECAs), and some items in contained in the Chile-Mexico FTA and the Mexico-Uruguay FTA.

Export permits were eliminated for 7 tariff lines, so as of late 2005 only 19 lines were still subject to such permits; 17 tariff lines pertain to oil derivatives, and 2 to tomatoes.

According to the Ministry of the Economy, the elimination of the aforementioned import and export permits was due to their being obsolete given they were automatically awarded, and in other instances they implied double permit requirements, such as in chemicals used in the pharmaceutical industry, which required both Ministry of the Economy and Ministry of Health authorizations. One ministerial clearing was deemed sufficient.⁷

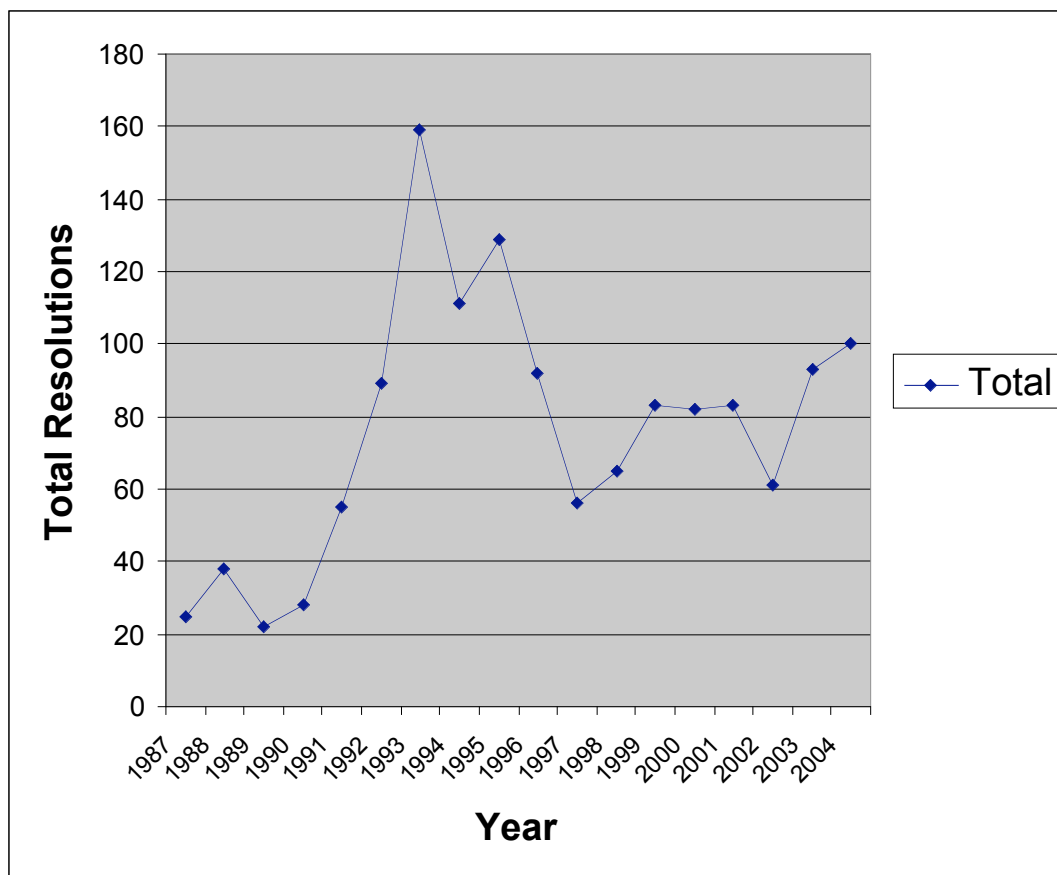
Measures against unfair trade practices

Mexican exports were the frequent target of US AD measures in the 1980s, and during NAFTA negotiations Mexico had as one of its chief aims the elimination or at least curtailment of unwarranted and unilateral AD actions by the US.⁸ In fact, it proposed to eliminate the use of AD actions within the free trade area, and to use competition policy instead. However, since that time Mexico has also become an avid user of AD policies and been loath to do away with that policy instrument in its other FTAs.

⁷ Reforma, "Agiliza Gobierno Comercio Exterior," November 10, 2005, p. 1A (Business Section), and Ministry of the Economy Press Bulletin 145 available at <http://www.economia.gob.mx/?P=125&WrapperElement=link&IdWrapperElement=25> accessed on November 10, 2005.

⁸ Cameron and Tomlin 2000, 45.

Figure 1
Mexico: Number of Yearly AD, CVD and Safeguard Resolutions 1987-2004



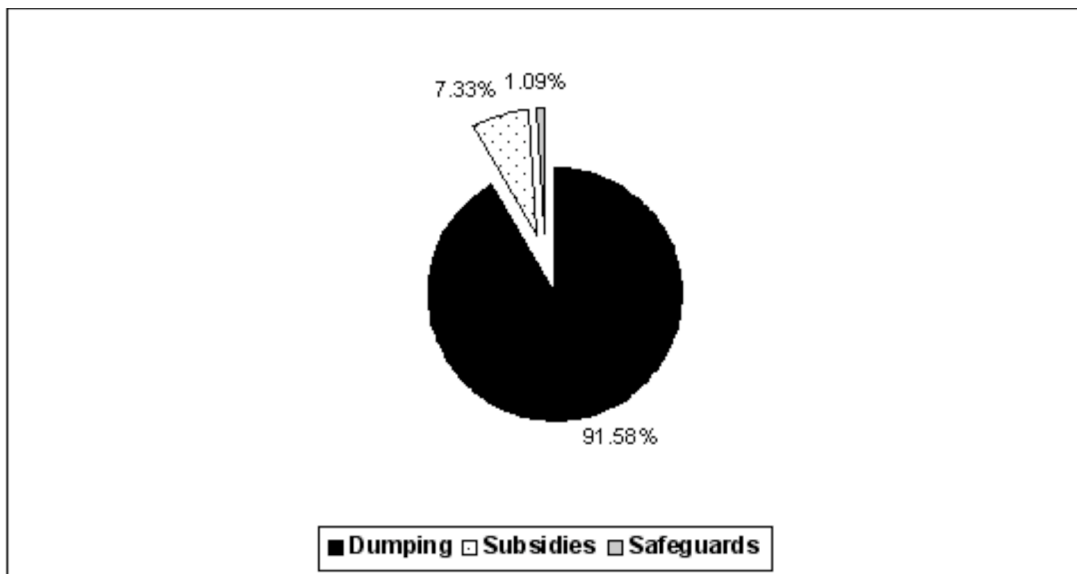
Source: UPCI, 2005, 103.

The number of anti-dumping and countervailing duty (CVD) and safeguard resolutions averaged 59.43 in the years prior to NAFTA (1987 to 1993), while the average was 86.82 for the period 1994-2004.

As shown in Figure 2 (below), AD is the trade instrument that Mexico uses most frequently to protect domestic industries; Chinese exports have been the most frequent target of AD actions (Figure 3). In fact, Mexico was the last country to grant its acquiescence to China's entry to the World Trade Organization (WTO), and as part of China's Accession Protocol it secured an agreement whereby it would be able to maintain AD actions against a host of

Chinese exports until 2007, without China being able to bring the matter under the WTO's Dispute Settlement Understanding.⁹

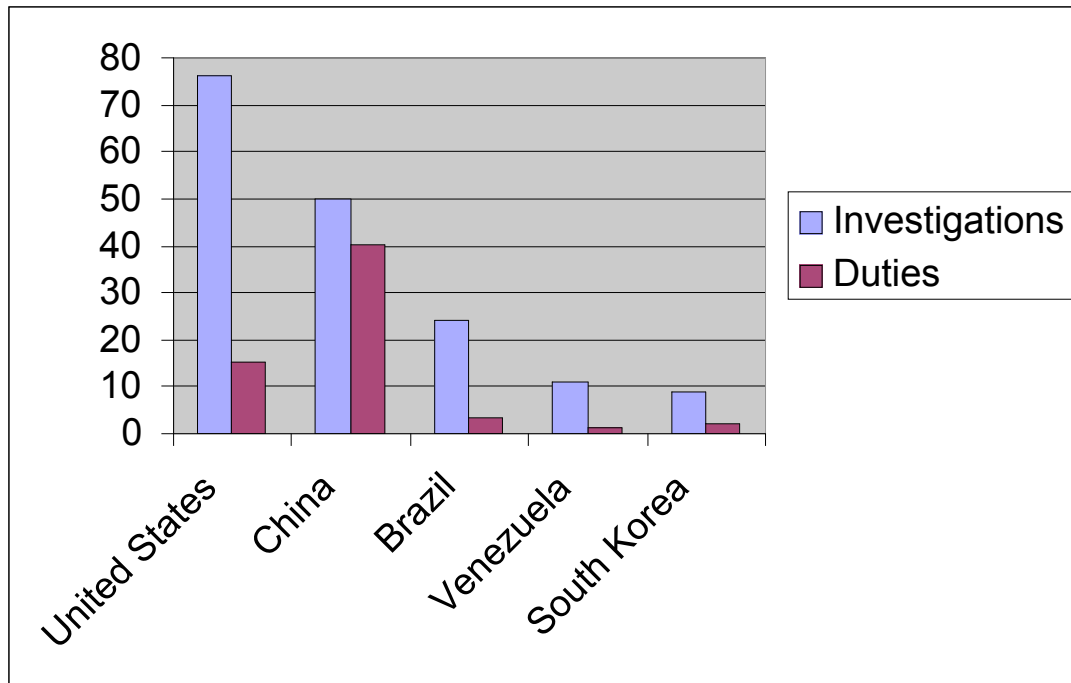
Figure 2
Mexico: Share of AD, CVD, and Safeguard Resolutions 1987-1994



Source: UPCI, 2005, 104.

⁹ See World Trade Organization 2001, Annex 7. The other countries allowed to maintain restrictions on imports from China are Argentina, the European Communities, Hungary, Poland and Turkey.

Figure 3
Mexico: Investigations and AD / CVD Duties by Country 1987-1994
(Top Five Countries)



Source: UPCI, 2005, 112.

As can be seen in Figure 3, the US is by far the country that has faced the most investigations by Mexican authorities, but the incidence of actual imposition of duties is relatively low 18%. In contrast, China has faced 50 investigations, but faced 37 duties (a 74% incidence rate). Five sectors account for more than 90% of all duties imposed between 1987 and 1994, and Chinese exports figure prominently in them.¹⁰

¹⁰ See UPCI, 2005, 115-123.

Table 2
Mexico: Duties in Force by Sector 1987-1994
(Percentage of Duties in Force)

<i>Sector</i>	Percentage of total duties
I. Basic Metal Industries	23.63
II. Chemical substances, oil products, rubber products and plastic	27.16
III. Fabrics, clothes and leather industry	9.88
IV. Metal products, machinery and equipment	2.47
V. Agriculture, forestry and fisheries	12.35
VI. Other manufacturing industries	17.28
VII. Lumber products	1.23

Source: UPCI 2005, 114.

While Mexico rarely uses CVD actions and safeguards even less so, regarding China it reached an agreement, approved by the WTO in mid 2005, whereby it would continue imposing safeguards against a number of Chinese exports until 2013.¹¹

Export Policies

Mexico has several policies to promote exports; chief among them are maquila, PITEX¹² and sectoral programs. Export financing has been limited and cumbersome, given onerous guarantee requirements, for at least the past decade.

Export Promotion

Maquila (in-bond processing), an export promotion strategy based on duty rebates and preferential tax treatment, started in the mid 1960s and still remains an important trade policy instrument. For firms to benefit from the maquila regime, they must export no less than 10% of total sales.¹³

¹¹ <http://www.economia.gob.mx/pics/p/p104/230805.pdf>, accessed on October 10, 2005.

¹² PITEX is the Temporary Import Program for the Production of Export Goods.

¹³ Or \$500,000 USD.

Approximately 45% of total exports in 2004 derived from the maquila sector,¹⁴ although it is on the wane at least temporarily. It reached a peak in 2001 with 3,630 units giving employment to 1.2 million people, but by 2003 the number of units had decreased by 21.21% and employment by 11.41%. Some of the decrease is attributed to the US recession (which is the market for 98% of maquila exports), to changes in Mexican tax laws (which ended the tax exemption to maquiladoras in 2001 —although it was reinstated in 2004), to greater competition from China, the Caribbean and Central America, and to the relatively strong peso.¹⁵

NAFTA also generated changes to the maquila regime: it extended duty free treatment to all North American components, whether or not destined for maquilas, and in 2001 it ended duty drawbacks on non-NAFTA components, adversely affecting many Asian firms.¹⁶ The government has since responded by unilaterally reducing tariffs on a number of items.¹⁷

The other long-standing export promotion program is PITEEX. Under PITEEX, the duty-free temporary import of inputs is allowed, but under a more restricted regime than maquiladoras.¹⁸ At least 30% of the annual sales of PITEEX companies must be exported, and the regime also allows for the import of machinery, spare parts, and laboratory and measurement equipment which will not be re-exported but is used in the production process of export goods. By 2004 there were 3,013 maquila programs and 3,516 PITEEX programs, whose exports accounted for 87% of total manufacturing exports.¹⁹

Another program, ECEX (Foreign Trade Enterprises), supports the marketing of Mexican products in international markets through the identification of demand for certain products, promotion campaigns and clustering the offer of several small producers. To qualify, firms must export at least \$250,000 USD annually and use the inputs of three national producers at a minimum. Its impact is marginal compared to maquila and PITEEX: in 2004 there were 400 ECEX enterprises, with total exports of \$4.2 billion USD, while maquila and PITEEX exported \$137 billion USD that same year.²⁰

ALTEX (Highly Exporting Firms), established in 1990, provides for a streamlining of administrative burdens imposed by the government for firms linked to foreign markets. Such firms also have access to SICA, the Commercial Intelligence System operated by the Ministry of the Economy, which provides information on export opportunities.

¹⁴ Presidencia de la República, 2005, 344.

¹⁵ Hufbauer and Schott 2005, 48-49.

¹⁶ *Id.*

¹⁷ See the paragraphs on sectoral programs (PROSECs) below.

¹⁸ Maquiladoras are allowed to undertake a wider array of activities than PITEEX firms, and are thus able to import finished and semi-finished products, unlike PITEEX firms. For greater information on the difference between the maquila and PITEEX regimes, see *North American Free Trade & Investment Report*, 2005, v. 1, pp. 5-8.

¹⁹ Subsecretaría de Industria y Comercio, 2005.

²⁰ Subsecretaría de Industria y Comercio 2005. In fact, ECEX exports decreased by 21.14% from 2001 to 2004.

In addition, Mexican firms that provide inputs for maquila, PITEEX, the auto sector,²¹ and ECEX may qualify as PRONEX (National Providers) and receive preferential fiscal treatment.

Sectoral Promotion Programs (PROSECs) were introduced in 2002. They allow the import of certain inputs with preferential (reduced) import duties if they are used in the following industries: capital goods, coffee, footwear, chocolates and candies, electric and electronics, photography, automobiles and their parts, toys and sports equipment, wood, rubber and plastic manufactures, agricultural machinery, mining and metallurgy, furniture, paper and cardboard, pharma-chemicals, medications, medical equipment, chemical, iron and steel industry, textiles and clothing, and transportation.²²

PROSEC is an aggressive program used to foster exports, largely through the unilateral reduction of tariffs, given the commitments undertaken in NAFTA to phase out duty drawbacks. Several duty reductions have taken place since 2002, which benefited firms using imported inputs, but have predictably upset some local producers.²³

In short, the most important export promotion programs are maquila, PITEEX, and, more recently, PROSEC although an array of other instruments is used. The use of local inputs has not picked up despite different attempts to do so.²⁴

Export Financing

The Mexican financial crisis of late 1994-1995 put the financial system under severe stress. Bank lending was radically curtailed, including that of Mexican Foreign Trade Bank (BANCOMEXT).²⁵

BANCOMEXT provided \$5.4 billion USD of financing in 2004, which is an increase of 21.8% over the 2000 figure, but a reduction of 17% when compared to the financing awarded in 2002. Approximately 40% of the resources are destined to manufacturing and services, and 38% to the agricultural sector.²⁶

According to Arnulfo R. Gómez -a former high ranking BANCOMEXT official, who was in charge of the Bank's FTA Department during the 1990s- there was no adequate strategy to make the most out of Mexico's FTAs, so that the

²¹ To qualify for preferential treatment regarding the auto sector, the auto firms must have a safe harbor (depósito legal).

²² The preferential tariffs covered for each sector can be consulted at: http://www.economia-snci.gob.mx/sic_sistemas/prosec/arma_prosec.php In addition, there is an "other" category that includes tariff lines applying to several other industries.

²³ In 2004 further liberalization measures were implemented as part of the Ministry of the Economy's "Regulatory Improvement Program," so it seems that trade policy is now being conducted under the guise of regulatory improvements.

²⁴ Refer to the section on international trade negotiations for more information.

²⁵ Hernández and Villagómez, 2001.

²⁶ Presidencia de la República, 2005, 177.

Bank's actions were in the end the result of large firms' trade and investment decisions.²⁷

The Bank's resources were not used for the technological updating of national industries, and trade promotion was largely based on the Bank's representatives abroad's submission of 25 monthly "demands" for Mexican goods, which resulted in simulations and absurd "demands" merely in order to fulfill the quota.

International trade negotiations

The most salient aspect of Mexico's foreign trade policy is its regional strategy. Since the early 1990s, Mexico has been very active negotiating free trade agreements, and by 2005 had FTAs with 43 countries. Notwithstanding its "collection" of FTAs, its trade has remained very concentrated in terms of export markets, export structure and number of firms accounting for total exports.

Mexico's Regional Trade Strategy

Mexico started its regional strategy in earnest with NAFTA. Although it had been a member of the Latin American Free Trade Association (LAFTA) and is still a member of the Latin American Integration Association (LAIA), the regional deals of significance started with NAFTA.

²⁷ Interview with Arnulfo R. Gómez, former BANCOMEXT official and Professor of International Trade at Universidad Anáhuac del Sur, Mexico City, November 4, 2005. The example he mentioned is the demand for caviar from BANCOMEXT's representative in Paris, when it is well known that Mexico is not a producer of caviar!

Table 3
Mexico's Free Trade Agreements

<i>Name of Agreement</i>	<i>Partners</i>	<i>Entry into force</i>
NAFTA	Canada, United States	January 1, 1994
G-3 FTA	Colombia, Venezuela	January 1, 1995
Mexico-Costa Rica FTA	Costa Rica	January 1, 1995
Mexico-Bolivia FTA	Bolivia	January 1, 1995
Mexico-Nicaragua FTA	Nicaragua	July 1, 1998
Mexico-Chile FTA	Chile	August 1, 1999
Mexico-EU Association Agreement	European Union	July 1, 2000
Mexico-Israel FTA	Israel	July 1, 2000 (goods); March 1, 2001 (services)
Northern Triangle FTA	El Salvador, Honduras, Guatemala	March 15, 2001 (El Salvador, Guatemala); June 1, 2001 (Honduras)
Mexico-EFTA FTA	Iceland, Liechtenstein, Norway, Switzerland	July 1, 2001
Mexico-Uruguay FTA	Uruguay	July 15, 2004
Mexico-Japan Agreement for the Strengthening of the Economic Partnership	Japan	April 1, 2005

Source: Presidencia de la República, 2005, 171 and

<http://www.economia.gob.mx/index.jsp?P=2113#>, accessed on August 19, 2005.

In addition to these far-reaching agreements, most of which cover trade in goods, agriculture, services and investment,²⁸ Mexico has subscribed some Economic Complementation Agreements under the aegis of LAIA. The most significant ones are the Argentina-Mexico ECA, which entered into force on April 2, 2002; an ECA with Brazil, which entered into force on May 2, 2003; and an ECA with MERCOSUR, which was published in Mexico's Daily Register

²⁸ For a comparison of the scope and coverage of Mexico's FTAs, see Ortiz Mena L. N. 2005b.

(*Diario Oficial de la Federación*) on May 13, 2003, but which is still not in force, pending Paraguayan ratification.²⁹

Although the government presents these agreements as an instrument to diversify markets, they respond to different logics.³⁰ NAFTA was Mexico's "second best" response in attempting to attract foreign investment through secure market access to developed countries in the early 1990s. Its true preference had been to forge close trade and investment links with the European Union, but was not successful in its overtures given that the attention was geared toward the former Eastern European countries. Likewise, there was no original "North American" vision; Mexico first sought a bilateral FTA with the US and then Canada joined the negotiations fearing trade and investment diversion.

Mexico steadfastly pursued its objective to secure a special economic partnership with the EU and finally secured it in 2000. It also sought an FTA with Japan, largely to attract Japanese investment, throughout the 1990s. It was only able to attain that goal in April, 2005.

These agreements are aimed at attracting foreign investment through secure market access to the world's most important markets. The Latin American agreements are more reactive than proactive and respond at least partly to Latin American countries' protests over alleged violations of LAIA provisions, under which Mexico would have been forced to unilaterally grant its LAIA partners the same preferences it had granted to Canada and the US. Mexico was loath to do this, and instead offered to negotiate FTAs with interested parties. Smaller Latin American countries accepted the approach, but Argentina and Brazil refused to follow suit.³¹

In early 2004, Mexico took a more proactive stance toward MERCOSUR and asked to be admitted as a full member. This generated a great deal of confusion, for MERCOSUR had been envisaged as having an overriding geographic (and geopolitical) logic in which Mexico had no place. Also, given that it strives to be a common market, its members will eventually have a common external tariff (CET), so bilateral FTAs would have to be adjusted to accommodate to the CET. The matter was clarified when in April 2004 Mexico participated in the XXVI Meeting of the MERCOSUR Common Market Council and Summit of MERCOSUR presidents and asked to become an Associate Member, which did not require a CET but merely an FTA with each MERCOSUR member. Mexico has an FTA with Uruguay, but the conclusion of an FTA with Brazil looks unlikely at least in the short and medium term given Brazilian

²⁹ Presidencia de la República, 2005, 171 and http://www.sice.oas.org/Trade/mex_s.ASP, accessed on October 18, 2005.

³⁰ For instance, the table that reports these agreements in president Fox's 5th State of the Union Address (Informe) has the heading "Instruments to Facilitate Market Diversification" (Instrumentos de Concertación para Facilitar la Diversificación de Mercados). Presidencia de la República, 2005, 171.

³¹ Ortiz Mena L. N. 2004b.

preferences to maintain protection for some of its industrial sectors, and Mexican resistance to opening up its agricultural sector (especially agribusiness) to Brazilian competition.³²

In November 2003 Economics Minister, Canales, announced that Mexico would sign no more FTAs in the foreseeable future, declaring a “moratorium” on FTAs, and stating that it would suspend ongoing negotiations with Korea, Argentina and Panama.³³ The reasons for this stance will be examined further in Section II of this paper, but suffice to say that the official stance is contradictory, insofar as in November 2005 President Fox stood out as a staunch supporter of the Free Trade Area of the Americas (FTAA) and insisted on the benefits of striking regional trade agreements.³⁴

Mexico's Multilateral Trade Strategy

Mexico's participation in the multilateral trading system has paled with that of its regional strategy, although lately it has become more salient and it is likely that the importance of multilateralism for Mexico will increase. The WTO's importance for Mexico is on the rise for several reasons. Firstly, the scope and coverage of the multilateral trading system has increased and Mexico will start to feel the effects of multilateral undertakings, whereas in the past the breadth and depth of issue area coverage of its regional trade agreements in general surpassed those of the multilateral trading system.³⁵ Mexico will not be able to opt out of the WTO except at a high cost and, notwithstanding current difficulties facing the Doha negotiation agenda, multilateral trade negotiations will continue apace. As an attractive market for many countries in terms of trade in goods and services, Mexico will continue to receive requests for improved market access.

Secondly, not only will Mexico have to bear the burden of WTO membership; it also has offensive aims that can only be attained in that forum. It has very good access to the market of its FTA partners, but with regional trade agreements continuing to expand and multilateral trade negotiations proceeding onwards, albeit at a slow pace, Mexico is experiencing preference erosion. It will have to strive for improved market access; the renegotiation of FTAs is politically extremely difficult, while gaining concessions at the multilateral level is more feasible –even if they are attained on an MFN and not a preferential basis.

Thirdly, there are several issues that can best, and perhaps only, be pursued via WTO negotiations, such as improved market access for services

³² Ortiz Mena L. N. and Sennes, 2005.

³³ <http://www.esmas.com/noticierostelevisa/mexico/325931.html>, accessed on August 19, 2005. In addition, there is a binational working group whose aim is to assess the feasibility of a Mexico-New Zealand FTA.

³⁴ See “Declara Fox su amor a países del MERCOSUR”, *Reforma*, November 6, 2005. Available at: <http://busquedas.gruporeforma.com/utilerias/imdservicios3W.DLL?JSearchformatS&file=MEX/REFORM01/00663/00663274.htm&palabra=fox%20mar%20del%20plata&sitereforma>, accessed on November 8, 2005.

³⁵ Ortiz Mena L. N., 2005b.

(under the aegis of the General Agreement on Trade in Services-GATS), the elimination of export subsidies and a radical reduction of domestic support for agriculture, a modification of US AD legislation and settling disputes.³⁶

The WTO's relevance for Mexico, from both an offensive and a defensive perspective, contrasts with the cavalier attitude that Mexico showed toward the GATT. It balked at joining in 1979 after accession negotiations had concluded, and joined until 1986. It participated in the Uruguay Round, but given its deep integration with the US economy through NAFTA, the effects of multilateral commitments in Mexico were negligible.³⁷

It has since become more active in the multilateral trading system and hosted the Fifth WTO Ministerial at Cancun in September 2003. Although the meeting ended in abject failure, it reflected a more proactive stance by Mexico, as did its participation as a member of the G-20 grouping, which seeks an elimination of export subsidies and a radical reduction of domestic support (production subsidies) for agriculture.

Not only has Mexico's activism increased, but the effects of multilateral commitments have started to be felt. For instance, in 2004 a WTO panel issued a report on a Mexico-US dispute over access to Mexico's telecommunications market (which was in fact the first dispute over GATS commitments to be heard at the WTO). In anticipation of the ruling, the largest Mexican telephone company, TELMEX, which had been accused of anti-competitive behavior, started adjusting its interconnection rates.³⁸

At the Sixth WTO Ministerial, held in Hong Kong in December 2005, Mexico restated its aim, as a member of the G-20, to eliminate export subsidies and curtail domestic support for agriculture. Regarding industrial products, Mexico seeks flexibility for developing countries but without watering down ambitious goals to establish low bound tariffs. It also seeks vastly improved market access regarding trade in services.³⁹

Should the FTA moratorium stay in place and the FTAA stall, at least multilateral trade negotiations will continue. This means that Mexico has little option but to pay greater attention to multilateral developments, no matter which political party is in power.

The next section provides an overview of the trade patterns and composition resulting from the trade strategy outlined in the section.

The domestic sources of Mexico's strategy and revealed preferences

³⁶ All of Mexico's FTAs have a dispute settlement mechanism, but in some instances it has opted to settle a dispute using the WTO's Dispute Settlement Understanding. For instance, it has been the plaintiff in four cases, all of them involving the US as defendant (DeMateo, 2006).

³⁷ For an overview of Mexico's participation in the multilateral trading system see Ortiz Mena L. N., 2005a.

³⁸ For an overview of the Mexico-US telecom dispute, see Ortiz Mena L. N. and Rodríguez, 2005.

³⁹ Subsecretaría de Negociaciones Comerciales Internacionales, 2005.

The main challenge and opportunity for Mexico has been, and continues to be, its condition as neighbor to the US. Its foreign economic policy has, as reference point, how it is able to deal with the US; everything else is a function of the nature of its interaction with its Northern neighbor, be it a search for greater reliance on the domestic market, an attempt at trade and investment diversification, or a deepening of ties to the North, trying to make the most out of a geographic situation that cannot be altered and a disparity in power and wealth that is difficult to mitigate.

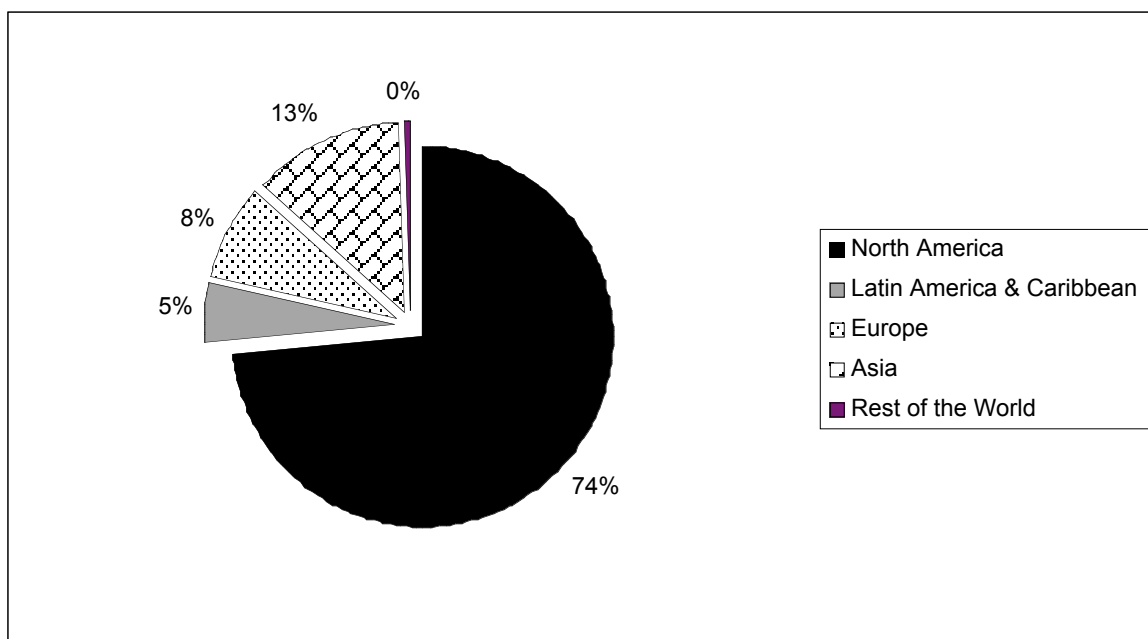
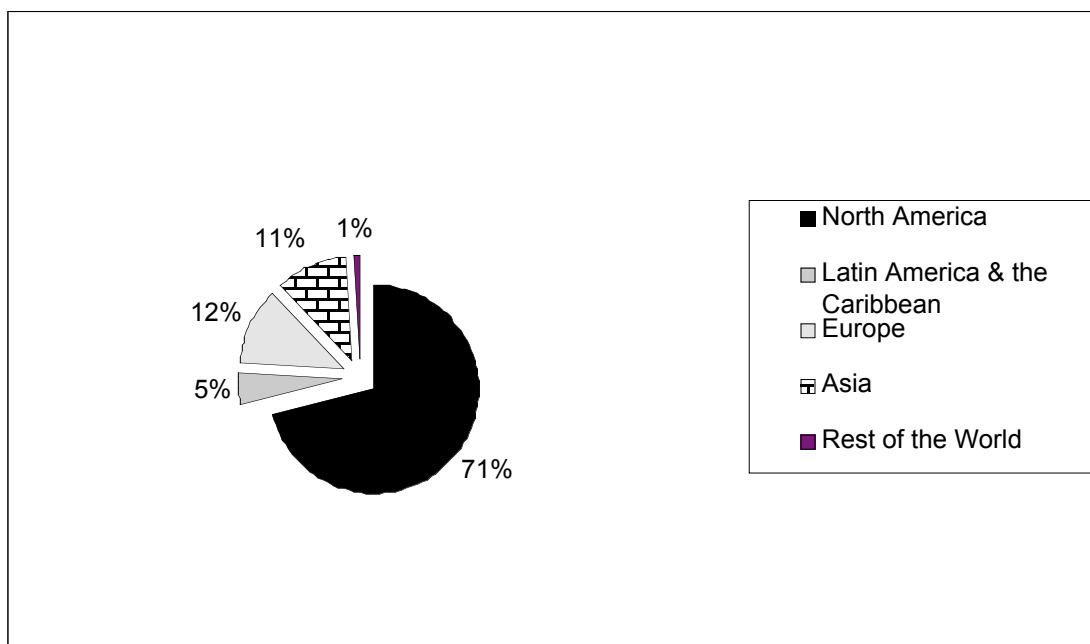
While, by definition the geographic situation cannot be altered and power disparity has been high since at least middle of the 19th century, when Mexico lost about half of its territory to the US, the actors taking part in the formulation of trade policy, as well as the process itself, have been changing since the 1990s. The greatest challenge at present is to find a new consensus -at least in its broad outline –on Mexico's place in the world political economy and how to make the best out of its structural opportunities and limitations in terms of foreign economic policy.

Structural factors

Main trade partners

Mexico's trade remains extremely concentrated despite the plethora of FTAs it has negotiated. Assessing trade on a regional dimension, it is clear that patterns have shifted only slightly since before the entry into force of NAFTA to the present. Mexico is in fact more concentrated in the North American region at present than it was before it embarked on NAFTA and the other FTAs, and the participation of Europe has actually decreased despite the 2000 Association Agreement with the EU. The decrease in Europe's participation has been accompanied by an increase in Asia's share of Mexico's trade.

Figure 4
Share of Mexico's Trade by Region, 1993 and 2004

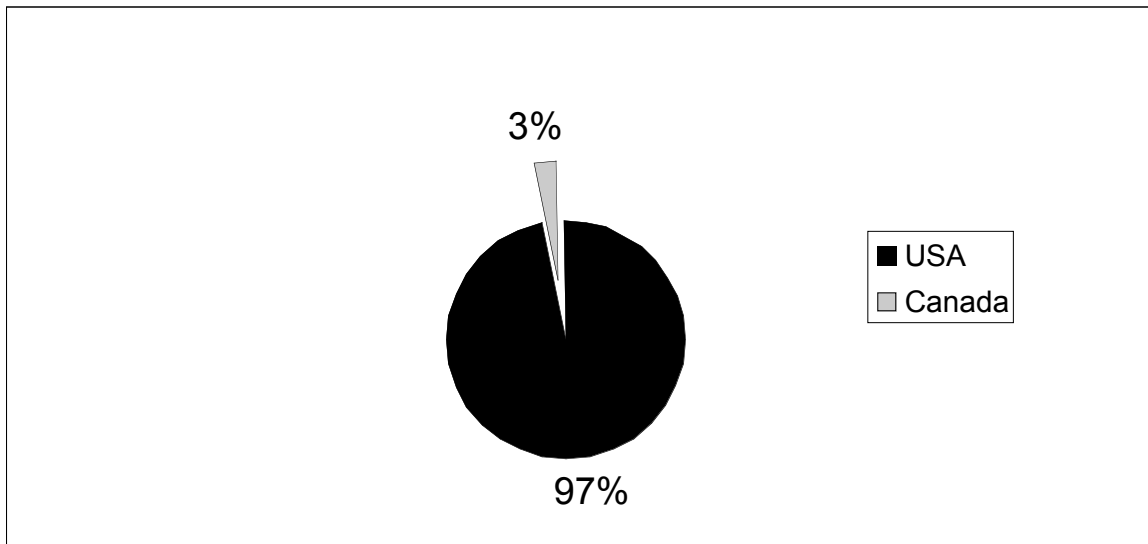


Source: Presidencia de la República 2005, 173.

If Mexico's trade is concentrated by region, it is also concentrated within each region. The most dramatic example is NAFTA, where 97% of its trade is with the US. One might say that this is not surprising, given the size of the US

economy and its physical proximity to Mexico, but the fact is that trade with Canada has not taken off as much as had been expected or desired.

Figure 5
Mexico's Trade with NAFTA Partners, 2004

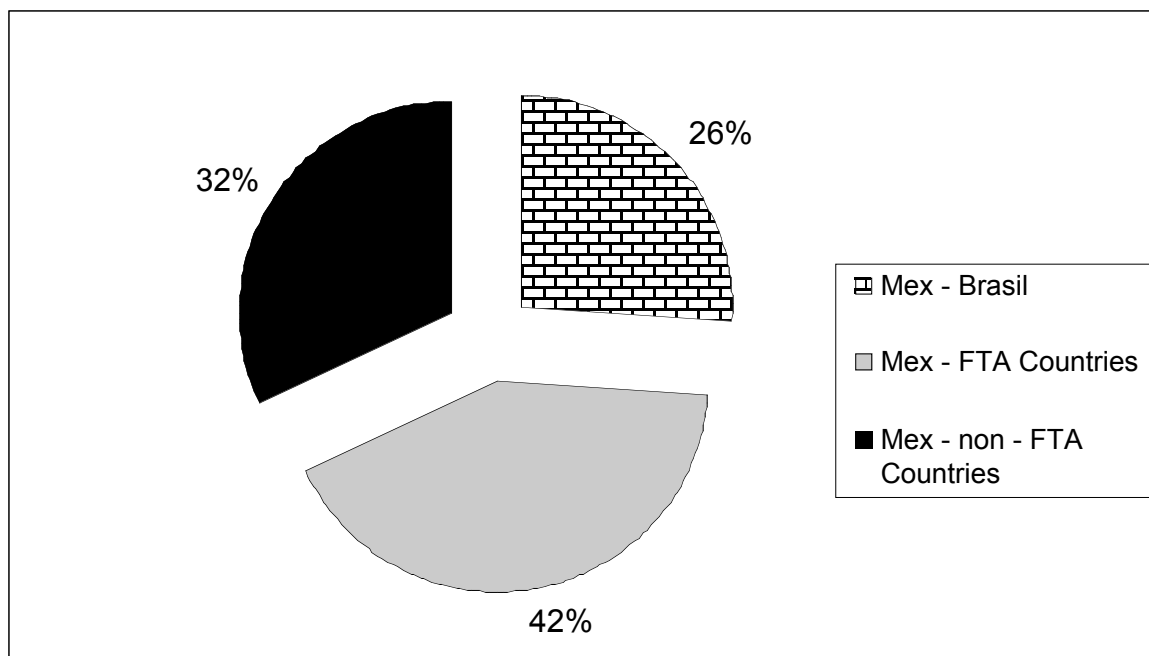


Source: Presidencia de la República, 2005, 173.

Mexico's trade with Latin America, which comprises only 5% of its total trade, is not taken up in large part by countries with which it has FTAs. In fact, 58% of its trade is with countries with which it does not have an FTA, and Brazil looms large within them.⁴⁰

⁴⁰ Brazil is listed and counted separately although it is part of the countries with which Mexico does not have an FTA.

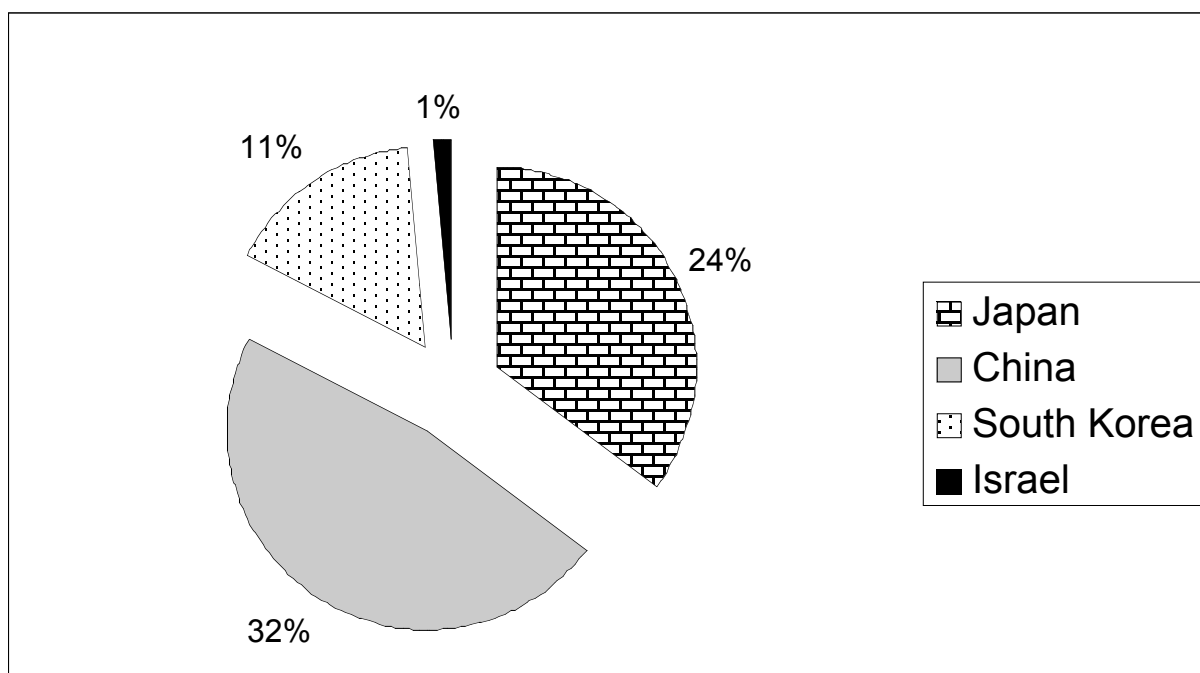
Figure 6
Mexico's Trade with Latin America, 2004



Source: Presidencia de la República 2005, 173.

Regarding Mexico's trade with Asia, it has ballooned with China despite having serious trade frictions and the imposition of numerous AD duties against Chinese imports.

Figure 7
Mexico's Trade with Asia



Source: Presidencia de la República, 2005, 173.

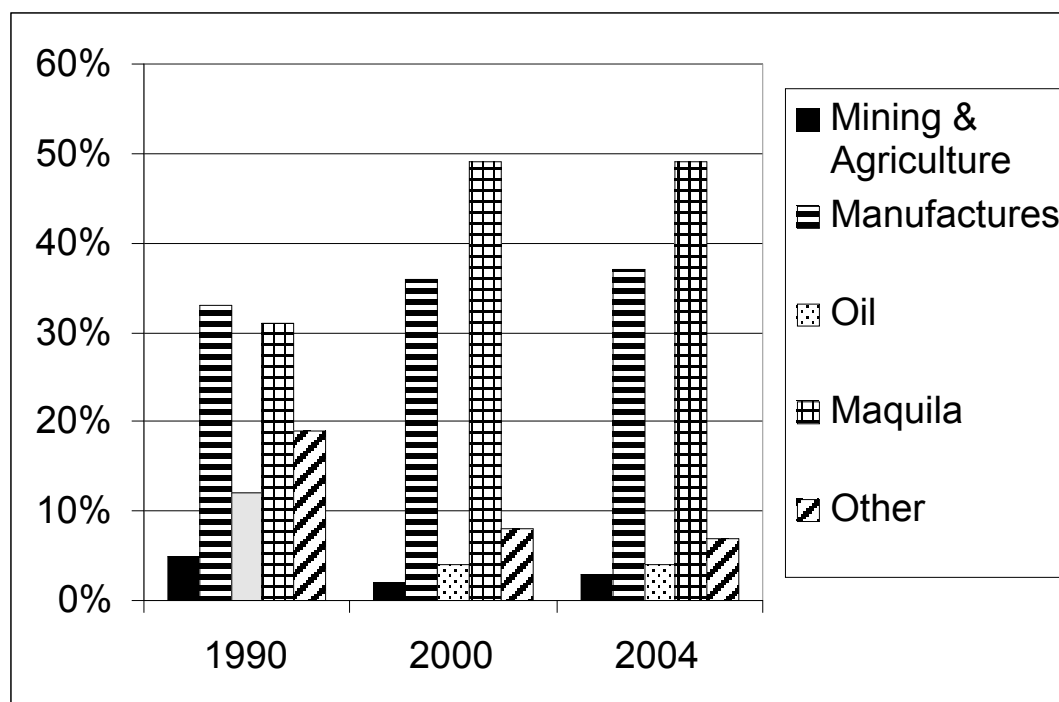
In short, Mexico's trade is still largely dependent on the US, no matter what other FTAs it has subscribed; and outside its trade concentration with the US, its largest shares of trade with other regions are with countries with which it does not have an FTA: Brazil and China.⁴¹

Main exports and imports

Mexico is not dependent on oil exports, as it was during the late 1970s and early 1990; in 2004 they accounted for only about 5% of total exports despite high oil prices. Mining and agriculture account for a small share of exports and have not picked up, at least in relative terms, since 1990. The most noteworthy increase is the share of maquila exports, which by 2000 accounted for approximately _ of total exports.

⁴¹ Mexico has an FTA with EU and EFTA, so Europe is already encompassed by preferential trade agreements. The Japan-Mexico agreement is quite recent, so its effects have still to be experienced.

Figure 8
Mexico: Share of Exports of Goods and Services by Sector
1990, 2000, and 2004



Source: Presidencia de la República, 2005, 339-340.

Exports are very concentrated, with only six sectors accounting for 30% of total exports.

Table 4
Export Composition by Main Products (billions of USD)

Product	1995	2003
All products	79.5	164.9
Autos and parts	18.1	18.4
Electronics	11.3	15.9
Oil	9.3	10.2
Computers	2.2	6.1
Diverse machinery	3.5	6.0
Textiles and clothing	4.6	5.3

Source: Unger, 2005.

Imports are also highly concentrated, as shown in Table 4 (the top six sectors account for 32% of total imports), and both the main imports and main exports have remained virtually the same since the mid 1990s. Furthermore, there is a high degree of correlation between the types of exports and imports, indicating the importance of intra-industrial and intra-firm trade and the participation of foreign firms -and foreign capital- in Mexico's trade.

While in 2001 Mexico's main exporter was PEMEX, the national oil company, the other top ten exporters were General Motors, Daimler Chrysler, Volkswagen, CEMEX,⁴² IBM, Ford, Hewlett-Packard, Visteon⁴³ and General Electric.⁴⁴

Table 5
Import Composition by Main Products (billions USD)

<i>Product</i>	<i>1995</i>	<i>2003</i>
All products	72.5	170.5
Electronics	22.5	22.2
Autos and parts	7.4	11.6
Plastics	5.3	6.3
Diverse machinery	6.6	6.0
Computers	3.0	5.7
Textiles and clothing	2.4	3.5

Source: Unger, 2005.

The composition of trade has thus remained very stable despite a marked increase in the value of trade. Likewise, the sensitivity of imports with respect to exports is extremely high.⁴⁵

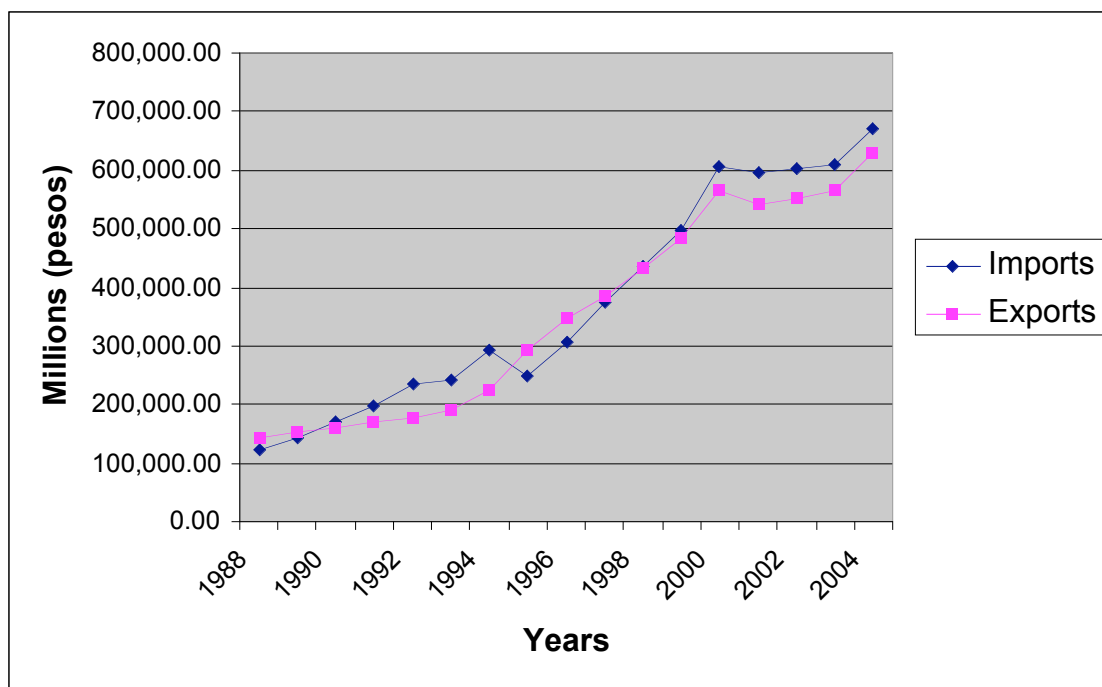
⁴² CEMEX is Cementos de México, a private cement company that is one of the leading cement producers worldwide.

⁴³ Visteon is a producer of air conditioning systems and electronic accessories for automobiles. See <http://www.visteon.com/products/automotive/index.shtml> Accessed on November 8, 2005.

⁴⁴ Unger, 2005.

⁴⁵ In simple terms, between 1991 and 2002 for every unit change in imports there was a 0.917 unit change in exports. See Unger, 2005.

Figure 9
Mexico: Exports and Imports 1988-2004 (millions of 1993 pesos)



Source: Presidencia de la República, 2005, 190-191.

A particularly salient challenge is that posed by China, given Mexico's reliance on the US market and the relatively stable composition of trade. China is affecting Mexico's export performance through two related mechanisms: direct export competition and price effects. Regarding export competition, the export similarity index (ESI) between China and Mexico for the world market increased from 36.9% in 1995 to 42.8% in 2001; out of the top 20 products that accounted for the increase in the ESI, 16 were related to information technology,⁴⁶ whose production in Mexico is largely based in the maquila sector.

Not only is China competing with Mexico for market share in the same products; given China's export value of some products, it is increasingly becoming a price maker and not a price taker. China's rise in world trade has translated into a reduction of 2.261% in Mexico's export prices from 2001 to 2004.⁴⁷

⁴⁶ Kim, 2005, 3-4.

⁴⁷ Kim, 2005, 12. The overall effect in terms of trade was a deterioration of 0.95%.

Comparative advantage

The main comparative advantage of Mexico is its geographic location as the neighbor of the US but, as has been mentioned, it is also a major challenge. Geographic location next to the US gives Mexico advantages in the establishment of industries where transportation costs are high and proximity to the market is a must.

In terms of factor endowments, Mexico has abundant labor and energy. So, in addition to geographic location, there is a great deal of complementarity between the Mexican and US economies: Mexico has a young workforce that is eager and willing to take up jobs in the US. Migration from the South to the North continues unabated even with stricter regulations in force after the 9/11 terrorist attacks in the US. It is estimated that there are more than 11 million Mexicans living in the US,⁴⁸ more than 40,000 annual attempted crossings,⁴⁹ and that 373 Mexicans died in 2003 while attempting to cross the border.⁵⁰ Economic push and pull forces override attempts to stop illegal immigration.

Mexico possesses significant energy reserves while the US has capital and technology, and is not self-sufficient in energy. In this instance, politics have trumped economics and the Mexican energy sector remains out of bounds to foreign investment in a large number of areas.⁵¹

A comparative advantage that has eroded in recent years but could still be obtained is that of political stability:⁵² while many Latin American countries experienced a great deal of political instability during the second half of the 20th century, especially regarding civil-military relations, Mexico was politically stable under the Institutional Revolutionary Party (PRI), which controlled the executive from 1929 to 2000, and Congress from 1929 to 1997.⁵³ 1994 saw the start of the Zapatista rebellion in Chiapas, the assassination of the PRI's presidential candidate (Luis Donaldo Colosio) and of another leading PRI politician (José Francisco Ruiz Massieu). The Zedillo presidency (1994-2000) had an intermittent confrontation with his predecessor, Carlos Salinas, but in 2000 the opposition managed to win the presidency and open the door for the peaceful transfer of political authority between parties. As will be discussed below, this ushered in an era of greater political pluralism but also increased the difficulty of arriving at decisions. Should Mexico be able to have a political system allowing for adequate

⁴⁸ US Department of Labor Current Population Survey, available at: Current Population Survey, available at: <http://www.bls.gov/cps/home.htm>, accessed on November 16, 2005.

⁴⁹ CONAPO, Encuesta Sobre Migración en la Frontera Norte de México, available at: http://www.conapo.gob.mx/mig_int/3.htm, accessed on November 16, 2005.

⁵⁰ Secretaría de Relaciones Exteriores, Dirección General de Protección y Asuntos Culturales. Telephone communication with SRE official, November 16, 2005.

⁵¹ Ortiz Mena L. N. 2006.

⁵² I am indebted to Luis de la Calle for this idea.

⁵³ See Cornelius, 1991, for an overview of the Mexican political system. A more recent work is Schedler, 2004.

interest representation and at the same time an acceptable measure of efficiency it could yet reap the economic benefits derived from political stability in a region where instability appears to be the norm.

Institutional Factors and Key Actors

Mexican politics are in flux. While there has been a transition from the PRI controlling all three branches of government to an executive held by the PAN and a Senate and Chamber of Deputies in which no single party has a majority, the basic rules of the political system have remained with little change. Mexican presidents were regarded as all-powerful during the PRI era, but this was so only because the president was the *de facto* head of the PRI, was able to handpick his successor, and the PRI controlled all branches of government and virtually all governorships.

In formal terms, however, the Mexican president has quite limited powers, especially when compared to the power of presidents in other presidential systems.⁵⁴ The executive and the legislature are frequently at odds with each other and it has become very difficult to govern. The current institutional setup and correlation of forces have resulted in a strong bias in favor of the *status quo*; the president has veto power but without partial or line-item veto and with no agenda-setting power, so a veto results in maintaining, and not changing, the *status quo*.⁵⁵ While a more decentralized policy-making process, evinced by increased political pluralism in Congress and a greater role for all three branches of government, it is able to represent a wider array of interests that under PRI rule, it also makes it more difficult to enact policy reforms, especially those with clear distributive implications (such as tax, energy and labor reform),⁵⁶ some of which are the underpinnings of a new impetus for trade policy.

A long-standing aim of political elites, both during the authoritarian period under the PRI and since the advent of full electoral democracy, has been the search for growth and prosperity, while maintaining as much discretion over foreign policy (including foreign economic policy) as possible. Thus, from a purely economic perspective, the rational policy could be to seek as deep as possible economic integration with the US.

From a political and economic perspective this strategy would entail risks: economically, because a downturn in the US economy would adversely -and severely- affect the Mexican economy; a more diversified trade relation would mean that an economic downturn in some countries would be compensated by prosperity in others, so the impact of adverse foreign economic developments would be mitigated in Mexico.

⁵⁴ See Lehoucq *et al.*, 2005.

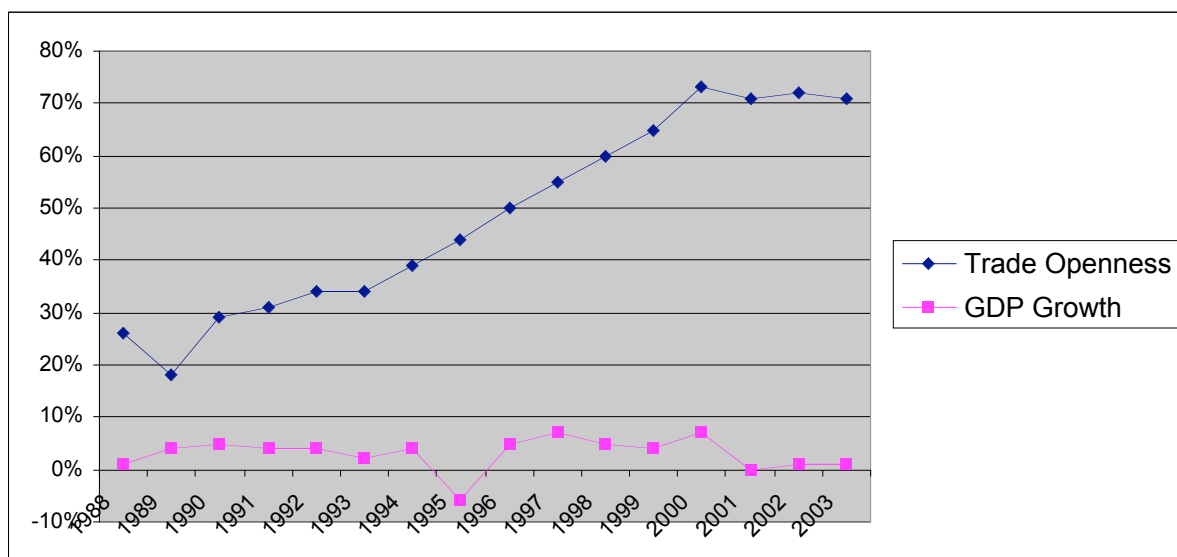
⁵⁵ Lehoucq *et al.*, 2005, 30, 32.

⁵⁶ Lehoucq *et al.*, 2005, 54-55.

From a political perspective, there is always a fear -explicit or implicit- that an overriding dependence on the US would mean that Mexico would be vulnerable and open to US political pressures. This has been a concern not only of the Left, but also the Right. For instance, during NAFTA negotiations a leading politician from the right-of-center National Action Party (PAN) was squarely against NAFTA negotiations on the ground of its possible effect on Mexico's sovereignty.⁵⁷

A more recent discussion has involved the relation between trade and growth. While Mexico has subscribed a record number of FTAs and its trade has taken off dramatically, GDP growth has been mediocre at best.

Figure 10
Mexico: Trade Openness and GDP Growth



Source: World Bank, 2005.

Some politicians, such as President Fox, believe that free trade should be part and parcel of Mexico's foreign economic policy and does not attribute the challenges faced by the Mexican economy to the active engagement with the world economy.⁵⁸

Other politicians, such as the Left's (PRD) Andrés Manuel López Obrador, a leading presidential candidate for the 2006 election, believe that the country needs to focus more on the domestic market and to have a more active

⁵⁷ See Conchello, 1992.

⁵⁸ See "Llama Fox a lograr un acuerdo comercial continental en América Latina" available at: <http://www.presidencia.gob.mx/actividades/?contenido=21727&pagina=2>, accessed on November 8, 2005.

industrial policy coupled with protection of sensitive sectors such as maize and beans, including renegotiating NAFTA.⁵⁹

As will be shown below, the major Mexican business organizations are calling for a halt to further trade liberalization, either reciprocal or unilateral, and are not requesting improved market access; their chief concern is Mexico's lagging competitiveness which is allegedly due to the lack of reforms in a number of areas such as labor laws, fiscal policy and energy costs. Multinational companies are likewise concerned about lagging competitiveness, but have not been opposed to further liberalization, especially unilateral tariff reductions.

Notwithstanding the different positions on trade policy shown by political leaders and business groups, the overriding fact remains that divided government and the weak constitutional powers of the president will make it difficult to enact significant policy change in whichever direction is deemed desirable. Some of the main challenges facing trade policy are noted below.

Intra-Executive Relations

The Ministry of the Economy, known as the Ministry of Trade and Industrial Development until 2000, has been in charge of negotiating preferential agreements since the early 1990s. NAFTA was negotiated by the NAFTA Negotiation Office, which was created expressly for that purpose at that time. Once NAFTA negotiations concluded, the Office was turned into the Deputy Ministry for International Trade Negotiations (SNCI), which to this day coordinates all trade negotiations.⁶⁰

SNCI is responsible for establishing communication channels with business groups and civil society so as to hear their views regarding trade policy. Likewise, it contacts other federal ministries, as appropriate, to undertake consultations before and during negotiations.

Frictions between the Foreign Ministry and the Ministry of the Economy over the conduct of foreign economic policy have sporadically arisen. When Jorge Castañeda became Fox's Foreign Minister in 2000, he asked for the transfer of vast areas of foreign economic policymaking authority to the Foreign Ministry, but the then Minister of the Economy, Luis Ernesto Derbez, refused to facilitate the process.⁶¹ When Derbez became Foreign Minister in January 2003 he applied the maxim of "where you stand is where you sit," and also asked for a transfer of foreign economic policy authority to the Foreign Ministry. A draft proposal was prepared, but never submitted to the legislature.

⁵⁹ López Obrador, 2004, chapters 2, 4 and 5.

⁶⁰ For an overview of the bureaucratic process of trade negotiations in Mexico, see Schiavon and Ortiz Mena L. N., 2001.

⁶¹ It would also require legislative approval.

In any case, the accommodation is at times a tense one. While in previous WTO Ministerials it had been the Trade Minister who represented Mexico, at the Fifth WTO Ministerial which Mexico hosted in Cancun in September 2003, it was the Foreign Minister who hosted the meeting, while the Minister of the Economy merely headed the Mexican delegation.

Conflicting signals regarding Mexican trade policy have been the result of this tug of war. As mentioned, in November 2003, shortly after the conclusion of the Cancun Ministerial, the Minister of the Economy declared that there would be a moratorium on the negotiation of more trade agreements. Five months later, in April 2004, the Foreign Minister formally submitted a request for Mexico to become an Associate Member of MERCOSUR, which requires the negotiation of free trade agreements with all MERCOSUR countries.⁶²

Preferences over the nature of economic links with China have also differed. While the Foreign Ministry has been an avid supporter of closer trade and investment links with China, the Ministry of the Economy has followed a defensive strategy focused more on combating alleged unfair trade practices by China and the imposition of AD duties than on searching for ways to improve market access for Mexican exports and attract Chinese investment.

During the Fourth Summit of the Americas held in Mar del Plata, Argentina, in November 2005, President Fox was an outspoken advocate of relaunching the FTAA process, and was seconded by Foreign Minister Derbez.⁶³ This is clearly not in line with an alleged moratorium on FTAs, and represents an about-face regarding the situation that prevailed in the late 1980s and early 1990s, when the Foreign Ministry was seen as a bastion of economic nationalism and a potential stumbling bloc for NAFTA negotiations, while the then Ministry of Trade and Industrial Development was regarded as being at the forefront in the push for trade liberalization.⁶⁴ COCEX, an inter-ministerial coordination mechanism for trade policy formulation that is supposed to avoid situations such as those that have erupted between the Foreign and Economics Ministries, has not been up to the task.⁶⁵

Dissension pervades not only inter-ministerial relations but also the Ministry of the Economy itself. While it is natural to have different and at times opposing views within a given ministry, there are usually decision-making procedures that tend to facilitate the formulation of a coherent set of policies. During NAFTA negotiations this was enabled by a very hierarchical and centralized decision-making procedure in the NAFTA Negotiation Office,⁶⁶

⁶² By that time, FTA negotiations with Uruguay were concluded, and the agreement entered into force in July of that same year.

⁶³ "México: preocupa poco avance en declaración de Mar del Plata," available at: <http://ar.news.yahoo.com/051026/4/Inco.html> Accessed on November 9, 2005.

⁶⁴ See Schiavon and Ortiz Mena L. N. 2001.

⁶⁵ COCEX members are Banco de México, the Federal Competition Commission and the following ministries: Foreign Affairs, Economy, Finance, Social Development, Agriculture, Environment and Health.

⁶⁶ See Cameron and Tomlin, 2000.

but decisions at the Ministry of the Economy have been fragmented, with the Minister favoring a moratorium on the negotiation of free trade agreements, and the Deputy Minister for Industry and Trade pursuing unilateral trade liberalization under the aegis of the PROSEC programs.

One may ask whether there is a contradiction between a moratorium on FTA negotiations and unilateral liberalization. Strictly speaking there is none, for precisely unilateral liberalization does not require engaging in international trade negotiations. However, the spirit of the moratorium is that the government would cease further trade liberalization to concentrate on making the most out of the agreements that are already in place. If liberalization was to proceed apace, the logical approach would be to seek reciprocity through negotiations.⁶⁷

Executive-Legislative Relations

The challenge of securing a modicum of coordination within and between ministries is compounded by the increasing activism of the legislature in the formulation of trade policy. The Senate has the exclusive faculty to accept or reject international treaties and agreements, and all of Mexico's FTAs have been submitted to the Senate for approval. However, the lower house has significant faculties on budgetary and fiscal issues and can affect trade policy through fiscal policy, with tariffs being a central part thereof.⁶⁸

While extensive consultations with the Senate took place during NAFTA negotiations, there was no formal obligation of the Trade Ministry to do so and was only done as a matter of political experience. However, on September 2, 2004 a new Law on International Economic Agreements entered into force, providing for ample consultations prior to, during, and after negotiations.⁶⁹

The law was promoted as a show of force by legislators, who believed that the legislature had been sidelined in previous trade negotiations. While greater transparency and accountability of the actions taken by the Executive in the conduct of foreign economic policy is welcome, the new law could hamstring the Executive and severely hinder the effective conduct of trade policy.

For instance, Article 3:I mandates that for an agreement to be approved it must contribute to improve the quality of life of Mexicans. Many economists are agnostic as to the effect of liberalization on economic growth and job creation, and agree merely on the fact that liberalization would tend to

⁶⁷ The sub-section on government business relations addresses some reasons for the FTA moratorium and the unilateral liberalization.

⁶⁸ In addition, it can affect trade policy through the use of internal taxes, such as when in 2004 it granted favorable fiscal treatment to the soft drinks industry when it used locally produced sugar, as opposed to imported high fructose corn syrup, in its production processes.

⁶⁹ Ley Sobre la Aprobación de Tratados en Materia Económica, available at: [http://www.ordenjuridico.gob.mx/Federal/PL/CU/Leyes/02092004\(2\).pdf](http://www.ordenjuridico.gob.mx/Federal/PL/CU/Leyes/02092004(2).pdf)

generate incentives for a more efficient use of factors of production and foster an increase in productivity. Likewise, many agreements have short-term costs and long-term benefits. How then can it be clearly stated that an agreement will improve the quality of life?

Article 8 awards the Senate the faculty to initiate hearings with the presence of negotiators. Again, this sounds reasonable but the faculty could be abused so as to request the frequent presence of negotiators and make it impossible for them to stick to a negotiation calendar and adequately program meetings with their counterparts.

Under Article 9:III, at the conclusion of negotiations the Executive must provide a list of all the concessions granted by Mexico. While the language is reminiscent of "GATT speak" it also has a mercantilist slant: concessions may be seen as a cost for Mexico, when in many instances it may be that concessions could be what most benefits the Mexican economy, for example if they provide for greater competition in areas where there are oligopolistic practices.

Finally, Article 12 provides for consultations with local governments and legislatures. Although consultations are non-binding, this nevertheless means that trade policy could easily be "captured" by extremely localistic interests and make it very difficult to move from the *status quo*.

In short, the new law, if used prudently, could generate greater credibility and legitimacy for trade policy, but it could also translate into mutual "hostage taking", whereby a group of legislators make it nigh impossible for the Executive to conduct trade policy, and when the party in charge of the Executive loses power it may then apply the same treatment to the former opposition.

Regarding the preferences shown by political parties over trade policy, it is safe to say that, despite grandstanding and protestations to the contrary, all parties have awarded ample support to the FTAs that Mexico has subscribed,⁷⁰ although dissension is greater in the Chamber of Deputies.

The latest agreement to be approved by the Senate was the Japan-Mexico Agreement for the Strengthening of the Economic Partnership. Out of the 128 potential votes, 80 were in favor of the agreement. There were no negative votes or abstentions, and the favorable votes included Senators from the PAN, PRI, PRD and PVEM.⁷¹

In contrast, the Law on International Economic Agreements, which required approval by both chambers, generated a great deal of dissension. It was approved by unanimity by the Senate on December 13, 2002, but it took a

⁷⁰ E-mail communication with Eduardo Ramos, Chief of Staff to the Deputy Minister for International Trade Negotiations, August 19, 2005. Senate votes are not easily accessible and are not available on the Internet.

⁷¹ PVEM is the Green Ecological Party of Mexico. The remaining 48 votes were not cast because the Senators were absent. See Senado de la República, 2004. I am grateful to Diego Díaz, a Research Assistant at CIDE, who managed to track down Senate votes on the issue.

further sixteen months to receive a vote in the Chamber of Deputies. The result was almost strictly along party lines, with the PRI, PRD, PVEM, PT⁷² and Convergencia providing 270 votes in favor and the PAN 129 votes against. There were four abstentions (1 from the PRI and 3 from the PAN).⁷³ The remainder of the 500 potential votes were not cast because of absenteeism. Given that at the time of the vote the PAN controlled the presidency and was responsible for the conduct of foreign economic policy, it is not surprising that there was great opposition to curtail the ability of the Executive in the area of foreign economic agreements.

The Chamber of Deputies has also been active in areas that affect trade policy, such as fiscal policy. In 2002, it introduced a tax on imported high fructose corn syrup, to favor the use of locally produced sugar in the soft drinks industry. This was done because the US had ostensibly not complied with NAFTA commitments on access to sugar exports from Mexico. The Executive had tried to find an outlet for domestically produced sugar by imposing AD duties to imports of high fructose corn syrup (HFCS) from the US in 1998. A NAFTA Chapter 19 panel heard the matter and in August 2001 determined that AD duties should be removed; the Mexican government complied.

Some members of the Chamber of Deputies then decided to take matters into their own hands and were able to pass legislation in January 2002 whereby a 20% tax would be levied on soft drinks made with HFCS. This in turn generated a NAFTA Chapter 11 dispute and another one at the WTO. Mexico lost the WTO dispute, but members of the Chamber of Deputies have dragged their heels and want not only to maintain the tax on soft drinks made with imported HFCS, but to award preferential treatment to soft drinks made with Mexican sugar or Mexican HFCS. In November 2005 the Senate refused to follow suit, but the issue remains contentious and unresolved.⁷⁴

If we focus on actual behavior as opposed to grandstanding, it seems safe to say that the Senate has been generally in favor of FTAs, but at the same time it wants greater oversight faculties over foreign economic policy. The lower house is divided over the role the Senate should play in trade policy (as demonstrated by the divided vote on the Law on Foreign Economic Agreements), but is quite active regarding the protection of local economic interests even if it means disregarding Mexico's international commitments.

⁷² Partido del Trabajo.

⁷³ CIDE Division of Political Studies database on legislative votes in Mexico (under construction). I am grateful to Dr. Benito Nacif for granting me access to the database and to Diego Díaz for providing the information.

⁷⁴ The HFCS, sugar, and NAFTA saga is extremely complex. See Hufbauer and Schott, 2005, 310-327. See also "El Senado rechaza extender la exención del impuesto de 20% a los refrescos fabricados con fructosa", available at <http://www.sentidocomun.com.mx/articulo.phtml?id=9338&text1=Arca> Accessed on November 12, 2005.

Government-Business Relations

The main business organization dealing with trade policy is COECE, the Foreign Trade Business Organizations Coordinating Council. It is an umbrella organization that, upon its establishment at the outset of NAFTA negotiations, encompassed all the major business organizations with an interest in foreign trade. It survives to this day and plays a key role prior to, during and after all of Mexico's trade negotiations.⁷⁵

COECE carries out consultations with its members and with the Ministry of the Economy on an "as a needed" basis. It organizes itself according to the demands of each negotiation. For instance, during NAFTA negotiations it was organized in 19 groups that paralleled the areas into which the negotiations were divided. Some of its members also commissioned studies to help them -and negotiators- establish a negotiating position. After that, COECE members accompanied negotiators to all meetings and were available *in situ* for consultations during the negotiation process. There was an additional round-up meeting after each negotiating session, and it followed through the agreement until the drafting of implementing legislation by the US Congress.

While COECE is representative in that it encompassed all major business organizations with an interest in trade, it has tended to overrepresent large firms and underrepresent SMEs. This was so because large firms have the resources to undertake sophisticated studies to detail the situation of their sector and make negotiation proposals in such terms as may be used by negotiators. In addition, they have the funds to pay for their COECE representatives to travel to all negotiating venues. Lastly, several large firms have representatives in several constituent units of COECE.

In contrast, many SMEs did not have the resources to pay for pre-negotiation studies nor to fund the travel of representatives to foreign venues. The problem with the representativeness of SMEs, however, runs deeper than their say in the trade policymaking process; business chambers in Mexico are usually organized by industrial sector and not size, so SMEs tend to get short shrift in the economic policymaking process in general.⁷⁶

A frequent complaint of business groups since the late 1990s has been the lack of progress in implementing "second generation" structural reforms, chief among them fiscal reform, labor reform and energy reform. The lack of progress in these areas is evinced in the drop that Mexico has experienced in several "competitiveness" indicators, and in fact led to the creation in 2003 of the IMCO (the Mexican Institute of Competitiveness), which was charged with developing objective and sound competitiveness indicators, ranking

⁷⁵ See Alba and Vega, 2002; and Zabludovsky, 2005.

⁷⁶ Alba and Vega, 2002; and Ortiz Mena L. N., 2004a. Alba and Vega point out that CANACINTRA and ANIT represented SMEs but both organizations complained that SME interests had not been taken into account during negotiations.

Mexico according to those indications, explaining the reasons behind Mexico's lagging competitiveness, and proposing remedies.⁷⁷

In 2005, it issued a report on Mexico's Competitiveness. IMCO's competitiveness indicator is comprised of 150 variables that cover ten broad areas: a functioning legal system, sustainable management of the environment, a well educated and healthy society, stable macroeconomy, stable and functional political system, efficient factor markets (capital, labor, and energy), adequate transportation and financial services, efficient government, benign international relations, and economic sectors with potential for further development. It compared Mexico with other 44 countries with which it competes in the world political economy.

The result of the study shows that Mexico ranks 31 among the 45 countries in the study, a result of lagging performance in each one of the ten main elements of competitiveness; in none of them is Mexico even in the top half of the draw. In some elements, such as efficient factor markets, Mexico ranks 42nd. Business groups have been increasingly vociferous regarding, for instance, the high costs of energy, which hinders any attempt at being competitive.

The creation of IMCO and its 2005 report are the capping stone of business complaints over Mexico's lagging competitiveness in the face of the government's insistence in further opening up the economy. The drop in Mexico's competitiveness is in fact the main reason given by business groups in their request, which became increasingly vociferous in 2003, to place a moratorium on further trade liberalization. The logic was that if, and when, Mexico increased its competitiveness as a result of domestic economic reforms, further liberalization could be countenanced.

Some business groups that had basically accepted the fact that the government would keep on pushing for more FTAs have become more outspoken in their opposition, and on the terms in which liberalization is carried out. This has happened within COECE itself,⁷⁸ and independently through the leadership of the Mexican Foreign Trade Council (COMCE).

For instance, the long-winded Mexico-Japan trade negotiations were supposed to have ended by the time President Fox visited Japan in October 2003,⁷⁹ and in fact the signing of the agreement by Fox and Japanese Prime Minister Koizumi had been planned. Some business groups representing export agriculture with interests in penetrating the Japanese market remained dissatisfied with the quotas for pork and melons that had been agreed upon by negotiators, and exerted direct pressure on the Minister of the Economy so as

⁷⁷ <http://imco.solutrends.com/opencms/opencms/en/>

⁷⁸ Interview with Luis Martínez Argüello, Director of COECE, Mexico City, November 8, 2005. Mr. Argüello related the anecdote regarding Mexico-Japan negotiations explained in the following paragraph.

⁷⁹ Negotiations formally started only in February 2002, but Mexico and Japan had been talking about a trade deal as early as the mid 1990s.

to actually prevent signing the agreement in Japan. It took almost an additional year to finally sign the agreement.⁸⁰

Some COECE members have recently become more outspoken on their trade policy views, albeit this is usually done privately in meetings with Mexican trade negotiators rather than through the use of the press and contacting legislators. During a meeting between COECE and staff of the Deputy Ministry for International Trade Negotiations on Korea-Mexico FTA negotiations,⁸¹ several COECE members stated that they were dead-set against a Korea-Mexico FTA, saying that they did not understand President Fox's decision to go ahead with negotiations since no business group had called for improved access to the Korean market.

In addition, one member representing the chemical industry said that they were also against the unilateral liberalization carried out under PROSEC. He argued that, although PROSEC is supposed to help increase the competitiveness of firms based in Mexico by reducing the costs of their imported inputs, in reality the unilateral liberalization is carried out on behalf of multinationals from countries like Korea, who want to use the inputs provided by their affiliates, and has nothing to do with the lack of availability of Mexican products at competitive prices. Thus, unilateral liberalization was displacing Mexican producers not because they were not competitive but because it allowed international production links to take place according to guidelines set out by multinationals who want to benefit their affiliates.

While COECE has not called for a moratorium on FTAs (after all, it is merely a coordination office of existing business groups and is called upon when negotiations are to take place), COMCE has taken a strong stand against further liberalization. COMCE was established in 1999 to promote foreign trade, foreign investment and technology transfer. Thus, while COECE was supposed to assist the government and represent business groups during trade negotiations, COMCE was interested in promoting trade. However, COMCE has gradually veered into pressing the government on trade policy and in fact it reports being a link with the government during trade negotiations as one of its mandates.⁸²

The increased activism of COMCE regarding trade negotiations created a tiff with COECE leadership in 2005; COECE formally remains the official channel through which business groups are supposed to press for their demands with the government regarding trade negotiations, but COMCE has not abated its activism regarding trade negotiations.

⁸⁰ The agreement was signed in September 2004 during a visit to Mexico by Prime Minister Junichiro Koizumi.

⁸¹ COECE-SNCI meeting on Korea-Mexico negotiations, FTAA and the WTO Hong Kong Ministerial. Ministry of the Economy, November 8, 2005.

⁸² http://www.comce.org.mx/index.php?opc=mv_opc1&secc=5 http://www.comce.org.mx/index.php?opc=mv_opc1&secc=5, accessed on November 5, 2005.

Despite the supposed moratorium on FTAs established in late 2003, in November 2005 the leader of COMCE still saw fit to again call for a moratorium on FTAs. The argument is that the existing agreements should be exploited, for they are underused, before embarking on additional ones. Regarding ongoing negotiations with Korea, COMCE's position is that an FTA is unadvisable and a sectoral approach should be followed. It is also contacting legislators to vent its opinion.⁸³

Finally, an issue that COMCE has also spearheaded is that of competitiveness. The President of COMCE is also the President of IMCO, whose report is mentioned above. Other IMCO board members include part of the Mexican business elite, representing large industrial groups from Monterrey (Cydsa, Imsa and Alfa) Mexico City (DESC, Posadas) and a multinational (Kimberly-Clark). It is worth noting that most of them participated actively in favor of NAFTA negotiations, so their reluctance to engage in further liberalization is especially telling.

The efficient and largely collaborative stance on trade negotiations that developed as a result of COECE-Ministry of the Economy interaction thus seems to be in peril, and it is likely that more channels of communication will be used by business leaders to get their views across, and that the legislature will play a larger role in channeling business concerns to the executive.

Civil Society and Trade Policy

If business-government links on trade policy were fairly stable and functional from the early 1990s up until recently, this clearly has not been the case regarding civil society-government links. As part of the consultation process undertaken during NAFTA negotiations, an Advisory Council on the Free Trade Agreement was created.⁸⁴ The idea was to have the Council represent "civil society", and its members included four representatives from each of the following sectors: academia, agriculture, labor and business. The Council met approximately on a monthly basis during NAFTA negotiations, at which time the Trade Minister would update its members on the status of negotiations; some of them would also be *in situ* during trade negotiations, to advise negotiators on as needed basis, in a similar manner to COECE.

⁸³ "Plantean suspender apertura comercial", *El Universal*, November 7, 2005, available at: http://www2.eluniversal.com.mx/pls/impreso/noticia.html?id_nota=48251&tabla=FINANZAS_h, accessed on November 8, 2005.

⁸⁴ The Advisory Council (Consejo Asesor para el Tratado de Libre Comercio) was first convened in September 1990 expressly for NAFTA negotiations, although it was until December 1993 that it was formally established through a governmental decree published in the Daily Register, and it was then supposed to represent civil society in all trade negotiations. See "Acuerdo por el que se crea el Consejo Asesor para las Negociaciones Comerciales Internacionales," *Diario Oficial de la Federación*, December 13, 1993.

The Council was definitely not representative of civil society -if ever such a body could be conceived independent of a legislature-.⁸⁵ The representatives of the labor sector were affiliated with the PRI (CTM, CROC, CROM) or at least not in strong opposition to the government (such as the head of the Workers' Council);⁸⁶ rural interests were represented by the PRI-affiliated CNPR, and by CNA and CNG, which encompass prosperous rural landowners; business interests were heard through CCE, COECE, CMHN, COMCE, CONCAMIN, CANACINTRA, ABM, DESC and Grupo San Luis.⁸⁷ Academia was represented by the deans of UNAM, IPN, COLMEX, ITESM, COLEF and ITAM.⁸⁸ Although the academic representatives did herald from the most important public and private universities, they took a basically passive stance toward negotiations.

While the Council met on a monthly basis during NAFTA negotiations, it met only 28 times from 1994 to 2000, and it did not meet at all during the Fox Presidency (2000-2006). While the dynamic of trade negotiations ebbs and flows, and it is natural that Council meeting should do likewise, the absence of meetings during the whole of the Fox administration signals that the former composition and *modus operandi* of the Council was not appropriate for the new political and economic circumstances, but a way to channel civil society voices in the trade policymaking process has not yet been offered. In 2001, the Ministry of the Economy prepared a draft to widen the membership of the Council and provide new rules of operation, but the matter was put on hold.⁸⁹

The most critical groups of NAFTA and trade liberalization remained outside the Council, with the Mexican Trade Action Network (RMALC) being the most visible one.⁹⁰ The Network represents the views of a vast and diverse array of interests, from environmentalists to feminists, to some SMEs. It has not been effective in influencing trade policy.⁹¹ While the government figures out a way to channel civil society views into the trade policymaking process, it is likely that RMALC activism rather than dialogue will continue, although it

⁸⁵ The membership that is mentioned is that prevailing at the end of the Zedillo administration. Its composition during NAFTA negotiations was similar, albeit not identical. For the NAFTA era composition, see Zabludovsky, 2005.

⁸⁶ For a discussion of these business organizations and state-labor relations in Mexico, see Middlebrook, 1995.

⁸⁷ CCE, CMHN and COMCE represent the interests of large and powerful Mexican business groups; ABM is the National Bankers Association; CONCAMIN and CANACINTRA have more varied membership than the other more elite organizations but not the same amount of political influence and access. DESC and Grupo San Luis are two large Mexican industrial conglomerates that prospered greatly during the closed economy era; San Luis produces auto parts in Mexico, the US and Brazil, while DESC was linked to the petrochemical industry and has recently fallen on hard times.

⁸⁸ UNAM is the most important public university in Mexico, IPN is the major public polytechnic, COLMEX and COLEF are two smaller but highly regarded public institutions of higher learning, while ITESM and ITAM are two of the leading private universities.

⁸⁹ Secretaría de Economía, 2001.

⁹⁰ www.rmalc.org.mx

⁹¹ Ortiz Mena L. N., 2004a.

may have a greater impact if it starts to channel its disquiet through the legislature.

Should the legislature truly reflect public opinion, however, RMALC will find that its views are not in line with those of general public opinion. In 2004 CIDE, the Mexican Council on Foreign Relations, and the Chicago Council on Foreign Relations presented the results of their public opinion survey on Mexico and international affairs.⁹²

While Mexicans do have qualms about globalization (only 34% believe it is mostly good for Mexico), the WTO (only 48% are willing to comply with WTO decisions that go against Mexico), and rich countries (66% disagree that rich countries play fair in trade negotiations), they are not in favor of greater protectionism: the second most important foreign policy objective is promoting the sale of Mexican products abroad, 64% of Mexicans favor NAFTA, 70% favor the Chile-Mexico FTA and 62% favor an FTAA.

Mexican views on FDI are more divided, with 54% favoring it and 42% opposing it. Only a plurality favors FDI in telecommunications and in media companies, and a majority (68%) opposite it in oil production and distribution, in electricity and gas (60%), and even in local currency government bonds (57%).

Mexican political and economic elites were also covered in the survey, and while they have a similar position to the general population they are much more favorable to foreign investment, including the energy sector (76% favors foreign investment in oil production and distribution, and 85% favors it in electricity and gas).⁹³

Finding a way to channel diverse opinions on trade policy and investment and then to construct a trade strategy that has broad support will be a tall order for whoever is in charge of the executive in Mexico from 2006 to 2012. In the concluding section, some of the main challenges facing Mexican trade policy are highlighted.

⁹² The findings were issued in two reports (a Mexico report and a comparative Mexico-US report). They are available in English and Spanish at: <http://mexicoyel mundo.cide.edu/index.htm> They are cited here as Minushkin *et al.* 2004a (the Mexico report) and Minushkin *et al.* 2004b (the Mexico-US report). The figures presented in the following paragraphs were obtained from both reports.

⁹³ The elite survey is not representative, and is based on Mexican Council on Foreign Relations membership.

Conclusions

What challenges lay ahead in light of Mexico's revealed preferences and strategies, and given the domestic sources of such preferences and strategies? Let us start with the first issue to then concentrate on the role of structural determinants and actors.

Mexico has an open economy, both in terms applied tariffs (especially when trade-weighted tariffs are concerned) and with outcome measures of trade openness, such as the share of trade to GDP, which has reached approximately 70% in recent years.

That is not to say that it is fully open —no large economy ever is—. It is an avid user of AD duties, and despite stating otherwise in NAFTA negotiations, it seems highly unlikely that it will be willing to discard the use of that trade policy instrument for the foreseeable future.

Its favored liberalization strategy since the 1990 has been the negotiation of FTAs. It is now in a privileged position due to its excellent access to the world's major developed country markets: the US, Europe and Japan. Its regional trade strategy, however, has not resulted in a reduction of its trade dependence with the US. Trade shares with the US remain virtually unaltered since 1993, despite Mexico's having FTAs with other 42 countries. Its trade share with Europe actually decreased during such time, and the only increases worth mentioning are with some countries with which it has no FTAs: Brazil and especially China.

Not only is Mexico's trade concentrated in terms of partners, but also by composition (on the import and export side) and the number of firms accounting for most of Mexico's exports. One could argue whether this multidimensional concentration is a bad thing; after all, if that is what markets determine, perhaps that may be for the best, and at any rate it is always an uphill battle when states try to go against markets. Nonetheless, there are negative economic and political consequences that derive from this situation.

On the economic side, as it has been argued, such a high degree of reliance of the US economy means that a downturn in the US economy severely affects the Mexican economy, given that it is so open: trade concentration with the US has been the norm for more than a century, but it is only since the mid 1990s that exports really took off. Concentration may be nothing new, but the degree of reliance on the US economy is at present exceedingly high.

The concentration of imports and exports in a limited number of sectors also means that Mexico is very sensitive to competition in those sectors; since China exports goods in many of the sectors which constitute Mexico's main exports, its competition with China is head-on, and unless Mexico can find

new sectors and market niches, it risks losing ground in third markets.⁹⁴ Even competitors that are not as formidable as China are eating away at Mexico's preferential market access, since both the US and the EU have subscribed preferential trade agreements with other countries since NAFTA and the Mexico-EU Association Agreement entered into force.

On the political side, such concentration means that only a handful of firms and sectors seem to have benefited from liberalization, rendering political support for an open trade policy difficult to garner. Since SMEs have not fared very well under liberalization, and they are some of the primary employers of the Mexican economy, trade-related employment is not as high as could be, and the benefits are not shared equally. While large and erstwhile competitive Mexican firms have called for a moratorium on further FTAs, there could be growing pressures not only for a moratorium but for an actual rollback of liberalization.

For instance, groups that have ventured the possibility of renegotiating NAFTA to allegedly protect Mexican agriculture could end up eating away at the credibility regarding the durability of Mexico's trade policy reforms, and credibility is one of the main gains behind Mexico's FTAs. Given a political environment in which policymaking is increasingly difficult, the benefits of Mexico's trade and investment links with other regions could be hampered.

This brings us to the issue of the forces and actors shaping Mexico's trade policy. Given the government's promise to halt further FTA negotiations in late 2003, while pushing for unilateral liberalization from 2002 up until the present, and in fact continuing with FTA negotiations with Korea, the best one can say is that either Mexico's trade strategy at present is contradictory, or that it really has no strategy and the government has responded to pressures from different political interests by engaging in contradictory actions.

The lack of a clear strategy is reflected not only in the actions carried out by the Ministry of the Economy, but in the frictions between the Foreign Ministry and the Ministry of the Economy on such key issue as how to deal with the Chinese challenge.

The legislative is becoming increasingly active in trade policy, albeit it is not doing so in a constructive manner. The 2004 Law on Foreign Economic Agreements was above all a show of force, and since there is no re-election congress members have short time horizons, making it difficult for them to have the long-term outlook which is required if Mexico is to have a coherent trade strategy.

Business leaders, even those who in the past have been in favor of free trade, are starting to ask for a slowing down of the liberalization process. While it may be a way to protect what shares of the market they still have left, it can also be seen as a genuine call for economic reforms to help Mexico

⁹⁴ Kim, 2005.

regain competitiveness. The IMCO report is an outstanding document in terms of both breadth and depth, showing what must be done in order to make Mexico more competitive. Should some of those measures suggested in the report be implemented, there would be fewer reasons to search for a halt to liberalization, which is merely a respite to the challenges posed by Mexico's competitors. In addition, increasing Mexico's competitiveness in areas such as financial and energy costs would allow many SMES that have not fully participated in international trade to benefit from the windows of opportunity that still exist as a result of Mexico's network of trade agreements.

The preferences of leading Mexican business groups are thus clear: at a minimum they want to halt further liberalization, whether unilateral or negotiated, and are not concerned about improved market access; should the *status quo* in terms of pending domestic economic reforms prevail, there could be increasing calls for a roll-back of liberalization through the renegotiation of FTAs.

Multinational corporations, which account for a large share of Mexican exports, would also benefit from the implementation of domestic economic reforms. PROSEC has breathed some life back to import-intensive exports but, on the basis of the IMCO report, it will not be nearly enough to put the Mexican economy in competitive shape.

Should there be closer interaction and improved collaboration between business and the legislature, there could be a momentum toward restoring domestic economic reforms to improve Mexico's competitiveness; this would help both firms that produce for the local market as well as Mexican and foreign export-oriented firms.

If there is no progress from the legislature or even from the executive itself in areas in which reforms can be carried out without congressional approval, the status quo and an increasingly defensive stance toward integration with the world economy will tend to prevail. This means that FTA negotiations with Korea and other potential partners will be halted. WTO negotiations, on the other hand, will go on regardless of what groups in Mexico want. If the current WTO negotiations manage to succeed, Mexico will be caught ill prepared.

It is to be hoped that the situation does not reach that stage and that Mexicans are able to agree on a the basic outlines of a trade strategy that makes the most out of its comparative advantages and at the same time ensures that the benefits of liberalization are realized more fully and shared more equally.

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