Opening up the barriers to trade

International trade and access to markets *3.2.1.3*

Mexico as a rising member of the MINT group of Emerging Economies

Mexico's economy
Mexico has the second largest economy in Latin America (after Brazil – a BRIC country) and the 15th largest in the world. Its 122 million people provides an internal market twice the size of the UKs with rapidly-rising purchasing power. Its annual GDP per capita is about $10 000, putting it in the same league as Turkey and Brazil, though still far less than the US ($55 000) and Switzerland ($58 000).

Foreign Direct Investment in not a new phenomenon into Mexico. In the 1930's American automobile firms were establishing vehicle plants inside the border of its southern neighbour, and by the 1960s European (VW) and Japanese (Nissan) car manufacturers were building cars in the country. Since then, VW, Toyota, Nissan, Ford, General Motors and Fiat Chrysler have all established plants or increased production in Mexico. Located on the bridge between North and South America, Mexico has been ideally situated to develop and export-led economy producing vehicles for consumers either side of it.

Two key trade developments took place in 1994: one was the start of the NAFTA trade structure (North America Free Trade Agreement) between Canada, the USA and Mexico offering free trade in goods and the dismantling of trade barriers and tariffs (taxes on imports). This gave US manufacturers a huge incentive to establish plants in Mexico to take advantage of cheaper labour costs and lower taxes, and import products into the US and Canadian markets cheaper than they might be produced there.

The second trading bloc Mexico joined in 1994 was the OECD (Organisation for Economic Co-operation and Development) – a community of 34 countries that was first established in 1961 and seeks to foster an improved trading network between member countries. All members have a democratic system of government and pursue a market economy, sharing advice, strategies and policies in order to improve the economic and social well-being of their citizens. The OECD provides a meeting-place where most of the world's richest nations (they account for 70% of the world's trading market) can come together to discuss solutions to common problems. The benefits to new entrants, such as Mexico, is that OECD countries are seen as safer destinations for FDI, government loans and having a 'quality seal' as a country with which to do international business. Mexico's membership of the OECD in 1994 (the first of any Latin American country) not only made the country more likely to receive inward-investment, but was recognition of its potential future contribution to the global trading network.

In recent decades, alongside automobiles, the electronics industry has grown hugely. Mexico now hosts the 6th largest electronics industry after China, US, Japan, S. Korea & Taiwan. It is the second largest exporter of electronics to the USA, producing TVs, monitors, computers, mobile phones, circuit boards and electronic appliances. Electronics represent 30% of the country's exports by value.

Linked to the growth in electronics has been the expansion of the aircraft and railway manufacturing sector. Mexico is now developing an aerospace industry with assembly of helicopters and regional jet engine fuselages for global companies such as Bell, Cessna & Bombardier. The latter is a Canadian firm making trains & aircraft which located in Mexico after the NAFTA commencement, & now employs 4000 highly skilled people in two main facilities.

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Not only is Mexico favourably placed between the northern and southern hemispheres of the Americas, but also between the eastern and western trading hemispheres of Europe and Asia respectively. Mexico is increasingly attracting firms that previously would have (or did) locate in China, making such basic household items as plastic brooms and brushes. As China's economy matures, the cost-advantage of the country is gradually becoming less attractive. China's labour costs used to be one third those of Mexico, but not any more – with rising wage demands and a strengthening currency. Now China's production costs are similar to Mexico's, and the reduced cost of transport, and proximity to the US such that its factories can readily answer a new production order, means Mexico's proximity and responsiveness is particularly attractive to businesses that operate a 'just-in-time' stock system. As a result, more and more US out-sourcers to China are choosing to relocate to Mexico. Production costs are slightly higher, but delivery timings and speed of response to orders gives firms located there an advantage.

Mexico's other key advantage is largely demographic: a young and rapidly expanding population with many of parenting-age. This demographic-dividend means that not only is Mexico an export-orientated economy, it is seeing an expanding and increasingly affluent internal-, or domestic-market it can sell to. Increasingly, Mexican factories are producing for the Mexican middle-class.

However, there is still a big wealth disparity between rich and poor. The upper 10% own 36% of the assets. Until more of the country's wealth is in a larger proportion of the population's hands, the internal market is likely to grow only slowly. One effect of this is that Mexicans tend to spend heavily on low-cost consumables. Mexicans consume more carbonated drinks per person than anywhere else in the world – particularly Coca Cola. Each person drinks an estimated 163 litres of carbonated drink per person per year (that's more than 3 litres each week), compared with 118 litres per person per year in the US. It is resulting in obesity levels topping world charts – particularly in childhood obesity.

The other key issues restricting further growth of the Mexican economy is a lack of investment in infrastructure provision – particularly electricity. The Mexican government is particularly inefficient at collecting tax revenue (the lowest collection rate of all the OECD members). This, together with unreliable electricity generation and distribution means that further growth of the Mexican economy is restricted until these issues are resolved.

The Mexican dictator, President Diaz, (d. 1915) was famous for the saying: "Poor Mexico, so far from God, so close to the United States", commenting on various border disputes his country had had with its northern neighbour during his time in power. The current (2017) President Nieto – elected in 2012- claims: "We have to be in an environment of competitiveness, of free trade, open economies, of transparency, of rules of engagement." Proximity to the USA is clearly no longer the burden it was a century before. How the US Presidency of Donald Trump, who is demanding a 35% tariff wall on all goods imported from Mexico in order to deter American firms from locating in Mexico, will pan out for the Mexican economy, is a question still waiting to be answered.

Exam style questions:

1. **What are the benefits that may accrue a national economy that enters a trade bloc or becomes a member of an international trading organisation? (4 marks)**

2. **Examine the factors that contribute to certain countries being considered 'emerging economies'. (6 marks)**

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1. **What are the benefits that may accrue a national economy that enters a trade bloc or becomes a member of an international trading organisation? (4 marks)**

This will be a point-mark response. One mark is awarded for each point of knowledge or understanding. Extra marks are allowed for the development of points.

Points that may be included:

- Opportunity to trade with fewer tariff barriers or quotas so goods from your country avoid import taxes as they enter foreign markets, creating a larger market. (EU, NAFTA etc.)
- Cheaper goods can increase the market for contributing businesses, improving their profitability and encouraging expansion/labour recruitment.
- Tariffs and trade protection may be installed around the whole bloc, protecting businesses inside from external competition (as with the EU).
- Agreed regulations, standards and trading laws for all members of the bloc/organisation so it's a 'level playing-field' for all contributors.
- FDI may be forthcoming from within the bloc/other members so the level of economic activity is higher than the investment from internal finance could sustain. Increases tax revenues.
- Possibly certain conditions/standards of political and economic measures are required for membership, so acceptance is a recognition of quality standards being achieved within a country.
- Economic peaks and troughs can be filtered by the bloc/group to provide a more even business environment with fewer shocks to the system.

2. **Examine the factors that contribute to certain countries being considered 'emerging economies'. (6 marks)**

Level 1 (1-3 marks): Basic knowledge and understanding of factors that contribute to emergence of a fast-growing economy. Limited in scope and context.

Level 2 (4-6 marks): Clear knowledge and understanding of wide range of factors that contribute to emergence of a fast-growing economy. Well applied to context.

Points may include:

- Major in-demand commodity that generates enough profit to re-invest in stimulating other aspects of the economy (Nigeria – oil)
- Well-educated population that is able meet the production needs of modern technology and hi-tech equipment (Taiwan – electronic goods)
- Low-cost location plus additional incentives for FDI to select that country, such as infrastructure, political stability and/or language (Thailand - clothing)
- Low-cost location plus proximity to affluent large market to offer fast-response to new orders (Mexico – household consumer items)
- Large internal market as well as export market potential with large total population and growing young-adult population (India – steel industry)
- Significant net export surplus that provides capital for re-investment in domestic industry and rising wages to stimulate domestic demand (China – large Sovereign Wealth Fund)

The best answers will classify key groups of factors into political, economic, demographic, social and cultural factors and identify countries where different ratios of these factors are key.