

Pedro Aspe, *Economic Transformation the Mexican Way*, Cambridge, Mass., MIT Press, 1993

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This book comprises the Lionel Robbins lectures delivered at LSE in 1992. Since Pedro Aspe was at that time some two-thirds of the way through his term as Mexico's Finance Minister, it provides an account of what he thought he was doing and what he was hoping to achieve, without the benefit of hindsight.

The book is agreeably straightforward and surprisingly comprehensive. It could have done with more careful editing, but this is a fault more easily forgiven when the author is a Finance Minister than when he is an academic. The introductory chapter deals with macro policy, with much emphasis on the *Pacto*. This is followed by chapters on financial and fiscal reforms, the debt problem and liberalization of external trade and

payments, privatization, and future prospects for the Mexican economy. The book will surely provide the definitive inside account of the Salinas reforms.

Given the author's position, one can hardly review the book he has authored without also reviewing the program of which he was a principal architect. With the benefit of two years more hindsight than Aspe had, it seems that there are three major grounds for concern about the strategy that he describes and defends. The first is that it led to a new overvaluation of the peso. The second is that the *Pacto* may have outlived its usefulness. The third is that the evidence so far does not seem to support his hope that Mexico will become an economically more just society. I will discuss these in turn.

In his concluding chapter, Aspe makes great play with the supposed contrast between the old and new "mechanism of transmission". In pre-reform days, a current account deficit

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resulted from a public sector deficit that was induced by the attempt to keep up employment despite poor investment opportunities for the private sector and could be financed only by sovereign borrowing: it was therefore proper to treat it as a warning signal. Post-reform, a current account deficit reflects a wealth of private investment opportunities that attract foreign investment and the repatriation of flight capital, so that a bigger current account deficit is good news. This contrast is illustrated with a four-quadrant diagram and backed up with some econometric equations whose parameter values change in critical ways at two points in the 1980s.

Should one have been as reassured by this as he evidently was that the real appreciation of the peso and the associated current account deficit were no cause for concern? The contention would have been more convincing to someone who did not recall that Nigel Lawson had espoused a similar doctrine about the inappropriateness of worrying about the British payment deficit in 1988, just as Nigel Lawson may have seemed more persuasive to those who did not recall General Pinochet's economic team making the same case in 1981. In the previous two cases, the fact that a current account deficit was associated with a fiscal surplus did not suffice to prevent ultimate tears. We now know that Aspe's successor also found the argument unpersuasive, and decided shortly after he took office to devalue in order to restore competitiveness and thus rekindle growth. Given

the large financial loss of the Mexican authorities to those who speculated against the peso as well as the slow growth of the Mexican economy during Aspe's last two years, one has to wish that he had allowed the top of the band to crawl much faster when the peso was spontaneously strong and more scope for subsequent depreciation could have been developed without the market noticing.

However, the trade unions might have noticed, and refused to renew the *Pacto*. But would this have been such a disaster? Aspe makes a convincing case for having accompanied inflation stabilization with the *Pacto* rather than having relied on deflation alone to reduce inflation. But the general view in the profession, even of those of us sympathetic to incomes policies, is that these are a short-term expedient rather than a desirable trait of steady state. It seems paradoxical that an administration that put so much effort into liberalizing the economy should have kept the fetters so tightly clamped on the labor market. Was this a necessary part of Mexico's strategy of maintaining employment at the expense of real wages (a strategy that it seems to have pursued even more aggressively than the United States)? Or might an end to the *Pacto* have increased labor market flexibility and permitted a more competitive real exchange rate without any significant cost in terms of slower progress in reducing inflation?

The final worry about the Salinas strategy is that it does not seem to be achieving the dividends that

Aspe obviously hoped for in terms of greater social fairness. We read in the newspapers about Chiapas and the mushrooming of Mexican billionaires. Real appreciation seems to have occurred without real wages getting back within striking distance of where they were before the debt crisis. Much of this is a mystery. There are many reasons articulated by Aspe for expecting elements of the strategy that he pursued, such as privatizing loss-making public enterprises whose products are mainly consumed by the affluent (like airlines), increasing the proportion of public expenditure devoted to social programs, and opening the economy, to lead to a less concentrated income distribution, yet there is no evidence that this is happening.

Mexico undertook a truly impressive set of reforms during the six years that Aspe served as Finance Minister. With the exception of exchange-rate policy and the failure to phase out the *Pacto*, I find it difficult to fault what the Salinas government did. Certainly there is no reason for believing that matters could be improved by reverting to populism and protection. Yet the fact is that that set of reforms (dare I speak of the "Washington consensus"?) did not usher in a promise land of rapid growth and growing equality. The next order of business is not to reject what has been accomplished, but to decide what is missing.