> **"Weak economic performance . . . and the great rise in violence and insecurity associated with the war on drugs have contributed to public doubts about democracy."**

Drug Violence Isn't Mexico's Only Problem

FRANCISCO GONZÁLEZ

In 2010, as Mexico celebrated the bicentennial of the start of its war of independence against Spain and the centennial of its pioneering social revolution, the nation found itself in the midst of another general and bloody conflict, the "war on drugs" that President Felipe Calderón declared shortly after he took office in December 2006. Indeed, commentary about Mexico has come to be so dominated by this "war" that the country's broader political and economic challenges have receded to the background.

If one steps back to assess these structural challenges facing Mexico, the picture that emerges is fraught with hazards. The risks stem on one hand from dysfunctional democratic institutions, and on the other from low economic and employment growth.

It goes without saying that the institutional and economic problems, however important for Mexico's medium- to long-term well-being, are subsidiary right now to the climate of violence and insecurity intensified by the war on drugs. It is important to note that drug-related violence as well as common crime increased significantly in the wake of the country's 1994–95 financial and economic collapse, and that such crime and violence became a top concern for the citizenry as well as the government during the administrations of Presidents Ernesto Zedillo (1994–2000) and Vicente Fox (2000–2006).

Still, if the evolution of annual murder rates per 100,000 inhabitants is taken as a proxy (the rate rose from approximately 6 to 7 in the 1990s to 10 to 12 recently), the explosion of violence and insecurity belongs to Calderón's presidency. At this point, the president will stay the course; he will step down next year hoping that a restoration of some measure of security on the ground will soften the verdict of history. That verdict, however, could be harsh on him and his circle of collaborators for having fanned the flames of barbarism that overtook Mexico in the second half of the 2000s.

The top priority for whoever wins the presidency in 2012 will be to reduce the insecurity and violence intensified by the war on drugs. This may require secret negotiations—about which the public at large and foreign governments will know nothing, because any Mexican government, left, center, or right, will advocate continuing an uncompromising war on drug traffickers while trying to draw red lines agreed on by the combatants.

Only after, and if, the violence is tamped down will a future government generate the leadership and legitimacy necessary even to raise the likelihood of accomplishing the political and economic reforms that the country needs. Until then, Mexicans will yearn for the social peace, political stability, and solid economic performance that they now recall with a sense of morbid nostalgia. Better a respected, effective authoritarian regime than a dysfunctional democracy, some Mexicans are thinking to themselves.

For the longer term, the political dangers facing the country arise from perverse institutional incentives that have generated short-term horizons and pronounced self-serving behavior among the nation's principal leaders and their followers. The economic danger results from the country's specialization as a manufacturing assembler and re-exporter, in which capacity Mexico adds little local content value to the goods that it

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supplies to the US market. Opportunities for finding new sources of growth abound, but they have remained underexploited in the current climate of political and economic uncertainty, and particularly amid the generalized domestic and foreign perception that the risk of random physical harm in Mexico is high and growing.

Nonetheless, if Mexico between now and 2030 successfully meets the structural challenges that it faces, it could take its place among the leading emerging-market countries in the world.

LEARNING DEMOCRACY

Democracy is a relatively new game that Mexicans are still learning to play. The fight for effective political rights—in a nutshell, the fight for free and fair elections—in Mexico took the form of a long-term, highly institutionalized transition to democracy, based on successive electoral reforms enacted between 1977 and 1996.

From 1929 the country was ruled by an authoritarian regime under a hegemonic party that since 1947 has been called the Institutional Revolutionary Party (PRI). When alternation of power finally occurred in 2000, with Fox of the conservative National Action Party (PAN) winning the presidency peacefully and through the ballot box, the country achieved a remarkable feat.

It is not far-fetched to say that the average Mexican citizen lives in fear of both criminals and public authorities.

However, the 2006 presidential election aroused considerable controversy. That year Calderón, the PAN candidate, defeated Andrés Manuel López Obrador of the left-wing Party of the Democratic Revolution (PRD) by less than a quarter of a million votes—out of more than 41 million votes cast. Following the election protests erupted, lasting several months, which ultimately resulted in a credibility deficit for the Federal Election Institute (IFE), one of Mexico's two most important electoral institutions. (The other electoral pillar is the judiciary's Federal Electoral Tribunal.)

The nine councilors who head the IFE are supposed to be apolitical, but their appointment is in fact a very political process. Members of the Chamber of Deputies, the lower house of the Mexican Congress, "scrutinize" prospective councilors and vote for them, which means that the IFE's composition reflects the balance of power among parties in that chamber. (The PRI and the PAN are the largest parties, followed by the PRD, and then by three or four very small parties whose votes are up for grabs.) As a result, doubts and distrust persist among the Mexican public regarding the freedom and fairness of elections. A public opinion survey conducted by the newspaper *Reforma* at the end of 2010 indicated that only about 44 percent trust the IFE and its management of elections.

This is not to say that no important steps were taken to improve elections after the turmoil of 2006. The social and political conflict ensuing from that year's election forced the PRI and the PAN—though, significantly, not the PRD—to agree in November 2007 on an electoral reform package, which was supported and signed by Calderón. The reforms changed the IFE's leadership; strengthened the institute's capacity for monitoring parties, the media, and political advertising during electoral campaigns; and also shortened the duration of campaigns. As a result, the contestation and outcomes of midterm legislative elections in 2009 and a multi-gubernatorial election in 2010 were broadly accepted.

The significance of the PRD's nonparticipation in the electoral reform negotiations of 2007 has to do with the left's accusations of foul play in presidential elections on two occasions—1988 as well as 2006. The left and its supporters believe that, unless its candidate wins in a landslide, powerful interests referred to as *los poderes fácticos* (de facto powers, including big business and its foreign partners, the mass media, the Catholic Church, and, ominously, organized criminal groups) will likely conspire with their political allies in both the PRI and the PAN to prevent a transfer of power to a popularly elected left-wing government.

LEFT OUT

In reality, the left in Mexico has traditionally been fractious and unstable, and López Obrador's combative and uncompromising stance has contributed to infighting on the left and to weakening electoral performance for the PRD since 2006. These developments have reduced the left's chances of winning a presidential election in 2012.

Still, a basic question remains for the consolidation of democracy in Mexico—namely, whether the country can alternate power not only on the right but also to the left. Can the left gain power without producing social and political turmoil that in turn creates authoritarian regression or a prolonged period of political instability?

Some insight into this question might be gained by examining what has happened elsewhere in Latin America when the left has gained power. Latin America's alternations of power to the left, according to conventional wisdom established by scholars, analysts, and the media, have in recent years belonged to two broad types. Chile, Brazil, and Uruguay are cited as countries where pragmatic left-wing leaders have pursued moderate policies once in power, thereby reassuring traditional economic elites and their foreign partners and strengthening democracy.

Venezuela, Ecuador, and Bolivia, on the other hand, are mentioned as countries where the left gained power in discredited democratic systems that had been captured by domestic elites and their foreign partners. In those situations, uncompromising radical leaders implemented populist policies and rewrote the rules of the constitutional game, leading to polarization and frequently to violent confrontation between the government's supporters and the opposition. This made democracy potentially less stable.

Mexico seems unlikely to fit into either type. By 2012, after 12 years of conservative rule under the PAN, a return of the PRI is likelier (given strong electoral victories in 2009 and 2010) than a victory by the PRD. Still, the PAN and the PRD fielded alliances during 2010 local and state elections that yielded significant gains for their partnerships at the level of governor (Oaxaca, Puebla, Sinaloa) and state legislatures and municipal governments (aside from Oaxaca and Puebla and other traditional PRI strongholds such as Hidalgo and Durango).

Although this sort of marriage of ideological opposites proved effective at slowing the PRI's electoral momentum, past experience from Nayarit, Chiapas, and Yucatán suggests that electoral triumphs based on such a strategy cannot be translated into a coherent coalition government. In all of these cases, one of the partners left the coalition or was relegated to a subordinate position once in power, leading to critics' characterization of PAN-PRD coalitions as unnatural or unviable.

The leaders of both the PAN and the PRD have said repeatedly that they would not contemplate running a common candidate in 2012. But if the governorship victories in 2010 tempt them into such a bargain, and if the strategy were to triumph—an unlikely but not impossible outcome—it is not difficult to see how a president supported by a coalition of ideological opposites could end up as a lame duck.

That is, if either of the main coalition partners withdrew its support for the government (which would not be unlikely, given that the prospective partners maintain widely diverging positions on social, economic, and cultural policies), severe weakness at the helm might ensue, or potentially even an interrupted presidency.

MEET THE OLD BOSS?

For many, meanwhile, the PRI's return to power would mean the return of the authoritarian system that the country experienced during the *presidencia imperial* from 1940 to the mid-1990s. Although a restoration of authoritarianism via the return of the PRI to Los Pinos (the presidential residence) is an attractive idea to many Mexicans who benefited under PRI rule, it is highly improbable. The country has enjoyed open pluralism for a decade and a half, and this genie cannot be put back in the bottle.

A more legitimate concern regarding a PRI return to the presidency would be whether the country's system of crony capitalism would be strengthened. Throughout Mexico, economic opportunity and advantage are inextricably connected to the governing party at all three levels of government. Many Mexicans have complained that this system has simply continued over recent years despite the PAN and the PRD having held power at various levels for extended periods.

Even so, a PRI return to the presidency could further strengthen the position of dominant vested interests that grew powerful through economic concessions granted to them under PRI presidents. This would be bad news for those who have over the past 10 years denounced public and private monopolies and called for their breakup, thus far unsuccessfully.

A more worrisome concern, at least in the short term, is that a PRI president would likely resemble his immediate predecessors—Zedillo of the PRI and Fox and Calderón of the PAN; that is, he would be constitutionally and politically weak. Certainly, a new PRI president would not be quasi-omnipotent like the PRI presidents of the *presidencia imperial*.

Congress is stronger now than the presidency, which has limited constitutional powers. Yet the national assembly is split among the three largest parties and a few smaller ones. This has led to a deadlocked legislative process, which in turn has stalled the enactment of structural reforms that the country badly needs.

A central fact of the Mexican political system is a prohibition against consecutive reelection to public offices across the board. This prohibition provides popular representatives with an incentive to demonstrate total loyalty to party leaders on whose whims their next jobs in public life depend, and to exhibit no loyalty or accountability to voters. Under this system, political actors' time horizons are short-term and their motivations self-serving, and they will continue to be.

Governors, under a federal system that was adapted from the US model, have become in the words of Mexico scholar George Grayson "new feudal lords." Federal rules and standards break down to different degrees in the states and municipalities, many of which are still ruled by traditional *caciques* (political bosses) and strongmen. Policies cannot simply be decreed from the center. Implementation varies hugely across the country's territory. Standard application of rules and norms is a faraway dream.

Unsurprisingly, many have concluded that Mexico's basic political institutions have put the country and its young democracy in a bind. Mexico's main organized political voices—including Calderón's government, the principal political parties, a large and growing pundit class, and civil society groups ranging from universities to foundations—have all put forward versions of the grand constitutional reform that the nation needs to undertake to improve what is widely perceived as dysfunctional democracy.

Mexico adds little local content value to the goods that it supplies to the US market.

But a grand constitutional bargain appears unlikely, given that the main parties' leaderships naturally oppose reforms that would weaken their grip on the power and privileges that they enjoy under the current system. Power in Mexico will remain divided and territorially fragmented, making it difficult for any president to do as he or she wishes. This should not surprise anyone, as exactly the same thing happens in more mature presidential democracies such as the United States.

TROUBLED VOTERS

Meanwhile, another great challenge stands in the way of democracy's becoming self-reinforcing in Mexico—construction of the rule of law. This shapes up as a medium- to long-term process that will require the youngest Mexicans to be exposed to a public culture in which rules are applied equally and fairly in open forums such as—crucially—criminal courts of justice. Improved rule of law would also force into the open the actions of public authorities so that citizens could scrutinize them and hold politicians accountable.

I spent a year carrying out research on behalf of the nonpartisan organization Freedom House for a wide-ranging report card (published in 2010) on democratic governance in Mexico. According to the evidence gathered by my colleagues and me, Mexico is, particularly in the spheres of basic civil rights and the rule of law, far from being a liberal democracy. Individual rights continue to be violated systematically at all three levels of government, but particularly at the state and municipal levels. It is not far-fetched to say that the average Mexican citizen lives in fear of both criminals and public authorities.

The past decade has proved a difficult one for Mexico's young democracy. Weak economic performance, inflated expectations about the peace and prosperity that democratic institutions would deliver, and the great rise in violence and insecurity associated with the war on drugs have contributed to public doubts about democracy. According to opinion polling by *Latinobarómetro*, a declining proportion of Mexicans over the second half of the past decade has expressed strong support for democracy. In 2009–10, Mexico's support for democracy was the lowest, alongside Guatemala's, of the 18 Latin American countries annually polled by *Latinobarómetro* (though Mexico's support in 2010 was stronger than it had been in 2009).

With average Mexican citizens fearful about the most basic and immediate aspects of their well-being—their physical security as well as their socioeconomic opportunity—it is unsurprising that a diffuse sense of malaise and pessimism has begun to affect public evaluations of democracy, its prospects, and even its desirability.

To be sure, weakening support for democracy is not specific to Mexico. It has been observed in other Latin American countries when social and economic conditions have worsened, particularly after harsh financial shocks and during economic crises. The majority of Mexican citizens do not highly value democracy as an end in itself, independent of its consequences. But again, this is not unique to Mexico; it is part of the fabric of democracy everywhere.

And citizens are justified in caring about the outcomes of procedures, not just their effective implementation. Although candidates across the ideological spectrum promise growth, jobs, and general prosperity, Mexico's economic growth under PAN governments starting in 2000 has been very unsatisfactory, compared with the economic performance of countries such as Brazil, Argentina, Peru, and Chile.

ASSEMBLED IN MEXICO

One cannot assign all the blame to the Fox and Calderón governments, nor to the Banco de Mexico's monetary policy, criticized as too orthodox and conservative. In fact, Mexico has experienced more than a decade of fiscal discipline and under-control inflation. This has led to lower real borrowing rates, which in turn have helped create a vast consumer credit market that has helped make Mexico a society, according to some analysts, in which the middle class is now a majority.

But it is not government or central bank policies that are the key determinants of the Mexican economy's main challenges. Instead, it is the country's integration with the economies of the United States and Canada under the North American Free Trade Agreement since 1994. This project was launched by President Carlos Salinas and consolidated under Zedillo, both of the PRI; PAN representatives in the federal and state legislatures supported the agreement and governments under PAN presidents have continued to support it. The result of the project is that about 80 percent of Mexico's external economic activity now involves the United States.

The US economy is more than 15 times larger than Mexico's, and when it registers high, sustained growth, as in the second half of the 1990s, Mexico benefits. But when the US economy undergoes crises—such as the dot-com bust and the Great Recession—Mexico suffers. In 2009, Mexico experienced by far Latin America's biggest year-on-year decline in economic activity (6.5 percent). Contractions in US economic activity are transmitted to Mexico via several channels, including manufacturing activity, tourism, oil production and exports, mining, and remittances. Some specialists estimate that for each 1 percent decrease in US GDP, Mexico's GDP drops by 3 percent.

Mexico's comparative strength—preferential access to the biggest consumer market in the world—has also become a basic structural weakness. Indeed, academics and analysts tend to prescribe offhandedly that Mexico should diversify its export markets. This is much easier said than done. Mexico's economy has become specialized as a supplier of finished manufactured goods to the United States. Many assembly plants have been relocated to Mexico, where labor is relatively cheap, and they produce goods that, to qualify for free entry into the United States, contain varying amounts of inputs from the United States, Mexico, and Canada.

In my view, these so-called rules of origin are a source of potential strength for Mexico but also a source of current weakness. The potential strength derives from the fact that finished products could qualify for free entry into the United States even if they had much higher Mexican content than they typically have. The weakness derives from the fact that most of the high–value-added manufacturing that Mexico produces, from automobiles to electronic goods to refined textiles, is made with American inputs, which are not necessarily the cheapest in world markets.

Throughout Mexico, economic opportunity and advantage are inextricably connected to the governing party.

The finished products are priced competitively in the US market thanks to relatively low Mexican wages and the products' free entry into the country. But Mexico finds it difficult to sell its goods in, say, the European Union or Japan, because the international market offers cheaper alternatives to high-cost US inputs.

An example often used to illustrate this phenomenon—known among trade economists as trade diversion—involves the price of textile inputs. To enjoy free entry into the US market, a majority of textile inputs must come from US sources, but such inputs are considerably more expensive than equivalents from, say, Bangladesh or India. If Mexico were to purchase inputs from such countries, prices for its finished textile products might be internationally competitive—but such goods could not gain access to the US market free of charge.

Mexican assemblers have thus far remained linked to their US input suppliers, and have concentrated on re-exporting high-volume goods to the United States. In spite of the fact that Mexico is among the world's leaders in free trade agreements, a vast majority of its importing and exporting is conducted with the United States and to a much lesser extent Canada. Commerce with other free trade partners has remained very modest.

INVESTMENT POTENTIAL

A chorus of voices advances a "decline and fall" narrative regarding US political and economic performance and relative power. I am of the opinion, however, that Mexico should deepen its economic relationship with the United States, and smarten it up. This does not mean that Mexico should cultivate relations only with the United States, but neither should Mexico desperately attempt to be seen in the near term as a global player—as some Mexican political leaders, from left, right, and center alike, seem to favor.

Mexico has no reason to disperse its scarce resources trying to emulate big emerging-market countries like China and Brazil. Mexico's core interests should remain its bilateral relationships with the United States, the small nations of Central America and the Caribbean, and the two large countries of northern South America: Colombia and Venezuela. In addition, basic geopolitics and the global shift of economic activity to the Far East suggest that Mexico should ramp up its relations with China, India, Japan, and South Korea.

Nonetheless, no plan for raising Mexico's long-term growth trajectory can be successful without a sequence of events that starts with raising rates of investment. Substantially higher rates of capital formation are required if Mexico is to generate the infrastructure, knowledge, networks, and labor capacities that will in turn allow it to generate locally a higher proportion of inputs for the US market.

Unfortunately, Mexico's investment potential is limited because of entrenched weakness in fiscal capacity. The federal government gathers very low revenues in proportion to GDP—around 12 to 15 percent, in contrast to an average of 30 percent in other OECD countries—and also relies significantly on steeply declining oil rents. More than one third of the annual federal budget currently comes from the revenues of the state oil monopoly PEMEX. Given long-neglected investment in upstream activity, Mexico has experienced a sharp drop in oil production and proven reserves, threatening to transform the country, according to analysts, into a net crude oil importer before the end of the 2010s if no new sources are found.

For these reasons the country's sovereign debt was downgraded toward the end of 2009. Public investment in Mexico will continue to be modest compared with levels achieved in countries like Brazil and China over the past decade, or other high-growth East Asian countries since the 1970s; in these nations, public investment has been the backbone of rapid, sustained growth.

At the same time, Mexico's private investment is highly concentrated among the top 20 Mexican corporations. Such concentration of credit access and affordability has starved the potentially vast sector of small and medium-sized enterprises of credit. These businesses are the main generator of formal employment and of finished goods that have higher local content and higher added value. But the past two decades have been very adverse for a majority of them.

Inasmuch as competitive entry into the US market will remain a desirable objective for producers around the world, Mexico's preferential access and, crucially, its geographical proximity might make it an attractive investment location for manufacturing giants such as China. Mexico *could* benefit enormously from "near-shoring," which involves moving closer to final market destinations production that was previously offshored to, say, China or India.

The extent to which near-shoring could become a trend depends on questions such as whether Chinese wages increase or global transportation costs rise due to increasing demand for energy resources. In any case, Mexico should not only pursue a strategy of luring the production of US firms whose manufacturing is now carried out in China. It should also encourage cash-rich investors from China, India, Japan, and South Korea to form ventures aimed at adding both Asian and Mexican value to production chains that will continue to supply the US and also a growing Mexican consumer market.

THE CHALLENGES AHEAD

But before such Asian-Mexican capital ventures can be established, or grow where they already exist, Mexico's public authorities and industrial leaders have to prove that the country is a safe, cost-effective, value-adding platform for the North American economic space. Regarding these issues, investors have seemed increasingly unconvinced over the past decade.

It is understandable that so much attention has been focused over the past four years on Mexico's war on drugs and the appalling mayhem that has accompanied it. Civilized human interaction disintegrates among barbaric acts of violence and the degenerate triumphal display of such acts. Sadly, Mexicans have come to expect daily reports of such outrages in mass media that morbidly cultivate accounts of violence. But even if the state gains the ability to protect civilization against the barbarians—and that is a big *if*—Mexico is due for a hangover after its bicentennial and centennial celebrations. The hangover is likely to be head-pounding and wretched, given the magnitude of the challenges ahead.

First, Mexico's government and society must restore basic social peace in many parts of the country. Second, they must reform institutions so that political actors' time horizons are lengthened, and so politicians become more responsive to the citizenry, not just their party leaders. Third, they need to attract investment that will raise capital formation rates, allowing domestic economic actors to add more local knowledge and value to production chains.

These structural challenges—political and economic—may appear overwhelming. But I predict the 2010s will be less uncertain, less unstable, and less violent than the 1810s and the 1910s. Cold comfort? Maybe. But if events prove this prediction wrong, the future will be very cold indeed. ■