The Impact of the Mexican Crisis of 94-95 on the *Maquiladora* Industry

Paul Cooney, Queens College

(Draft: not for quotation)

I. Introduction

Despite all the warning signs, the world of finance was caught off guard with the collapse of the Mexican peso in December 1994. The ensuing devaluation was followed by the largest bail out by the IMF until then, and by early 1995 Mexico was in its most serious depression since the 1930s. Through 1995 Mexico endured significant negative rates of growth, and waves of bankruptcies. In addition, the population experienced a decline of real wages by more than 40% during 1995 alone. This led to a significant increase in poverty: reaching 50% or more of the population, and one fifth was enduring extreme poverty. In addition to the impact on the working class and peasants of Mexico, local manufacturing was severely affected, as evidenced by the increase of bankruptcies in the manufacturing sector. In stark contrast to the **-6.9%** growth rate for the overall Mexican economy, the *maquiladora* industry expanded by **30%** in 1995. In fact it grew from 2200 plants with 550,000 workers at the end of 1994, to over 3000 plants employing over 800,000 workers in 1996. This paper will begin by examining the impact of the peso crisis and the subsequent depression in Mexico, and then go on to analyze how the *maquiladora* industry was able to flourish while much of domestic manufacturing in Mexico was in crisis.

II. Peso Crisis of 94 and Depression of 95

Several different factors could be pointed to as causes of the peso crisis, but in general it is the result of an extended period of overspeculation, involving both domestic and foreign investors. Through 1994 there were several indicators suggesting a peso crash was imminent. Most significant was the decline of foreign exchange reserves, dropping from $26 billion early in 1994, down to a dangerously low $2 billion just before the US bailout. Secondly, almost 80% of the $85 billion invested in Mexico between 1991 and mid-1994, was in the form of portfolio investment, leaving only 20% in the form of direct investment. Thirdly, was the very clear and evident shift away from the government bonds denominated in pesos (*cetes*) to those denominated in dollars (*tesobonos*) over many months. The decline in in reserves and shifting from *cetes* to *tesobonos* is graphed in Figure 1 below.

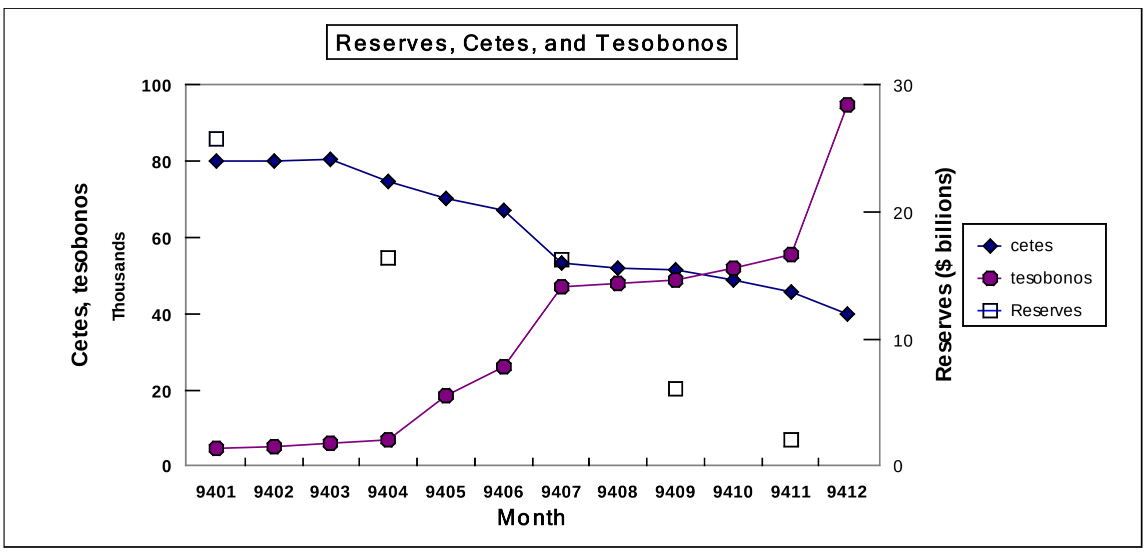

Figure 1. Reserves, *Cetes* and *Tesobonos* in 1994.

In order to back up first world investments and also given the importance of Mexico as a shining example of the success of neoliberal policies, when the peso crisis of 1994 hit, special efforts had to be made to prevent the Mexican economy from going into freefall. This justified the precedence of the $50 billion bailout which included the IMF's loan of $17.8 billion, more than twice the total it lent *all* countries in 1994. It also justified the notable decision by Clinton to make use of an obscure

Treasury entity called the Exchange Stabilization Fund (ESF). Of course this huge loan will have to be paid for by Mexicans though continued government cutbacks, increased taxes, and further reductions in wages. This is all in order to maintain a healthy investment environment as Mexico heads toward the 21st century after enduring its worse depression ever.

Although mainstream economists are allergic to the concept, there is no denying that Mexico experienced a depression in 1995, as evidenced by the decline of GDP of 6.9%. This is even more pronounced for GDP per capita which declined by 8.6% (see Figure 2 below). From the outbreak of the peso crisis in early December 1994 till Februrary 1995 the value of the Mexican currency had declined by more than 50% and inflation had increased from 7% in 1994 to 52% in 1995. The economic crisis brought about the collapse of Mexico's internal market, forcing consumption to decline substantially. There was also a severe lack of credit as domestic banks struggled with non-

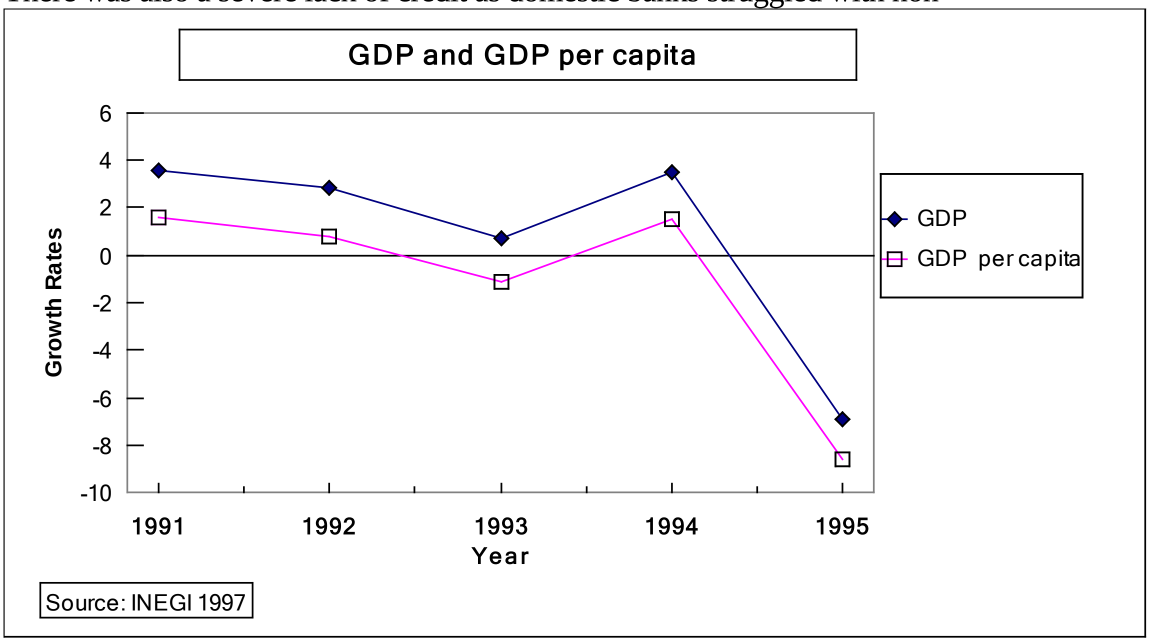

Figure 2. GDP and GDP per capita.

performing loans and needed to build up reserves after their near exhaustion in 1994. This implied a virtual disappearance of credit for small and medium businesses. Although it had begun in 1993, this further strengthened the *barzonista* movement which was an alliance of debtors, many of whom were farmers, demanding renegotiation of their debts.

As 1994 brought NAFTA and increased vulnerability to foreign, predominantly US imports, many Mexican farmers, small- and medium-sized businesses were pushed to the edge of bankruptcy. This became exacerbated with the depression of 1995, worsening their already precarious situation. For example, Pedro Salcedo, the president of the National Association of the Transformation Industries (ANIT), representing medium and small manufacturers, stated towards the end of 1996, that between 300,000 and 400,000 such manufacturers could collapse in the short run. As of mid-1997, actual bankruptcies recorded since NAFTA has been in place are estimated at 28,000. The current number is assumedly higher, though probably not reaching the worst case scenario described by Salcedo.

The official unemployment rate reached a peak of 7.6% in August of 1995 after being 3.2% in December of 1994 and hovering around 6% through much of the depression. Although the official rate more than doubled in just the first six months of 1995, it is still rather biased and not a very reliable measure. It does not reflect the extent of underemployment at all and significantly underestimates the number of people looking for work. In fact, it is estimated that up to two thirds of all Mexicans are either under-employed or unemployed. That is, of the 36 million people in the economically active population, only 9.37 million have permanent, full-time jobs. The significant contraction of formal employment through 1995, lead to a shift toward informal employment. In such instances, workers have neither health benefits, pensions, minimum wages or other protections. As Mexican workers either lose their jobs or are forced to take lower paying jobs or pay cuts, there is the expected increase of poverty. In fact, the estimates of the percentage of Mexicans living in poverty range from between 50 and 75% for 1995. A 1996 report by the UNDP claimed that “out of Mexico’s 91 million inhabitants, 37.2 million (40.8%) were living in extreme poverty or indigence.”

As a result of the austerity brought about by monetarist policies, Mexico experienced a decline of real wages of 50% through the 1980s as can be seen in Figure 3. The late eighties and early 1990s provided a brief respite, though this is only reflected in

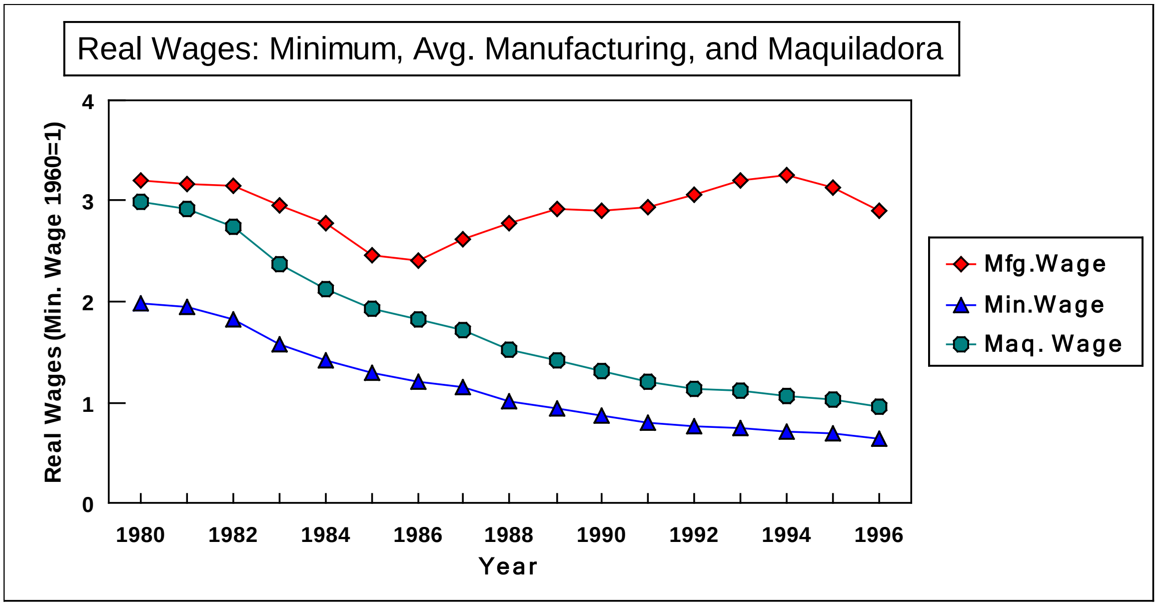

Figure 3. Real Wages: Minimum, Average Manufacturing and *Maquiladora*[1]

the upward shift of real wages in manufacturing. However, during the depression of 1995 Mexico lost a total of 1.85 million jobs and as a result of the peso devaluation, real wages further declined by over 40%. Even as ‘recovery’ was being heralded by Zedillo and Ortiz, real hourly wages in 1996 were still 27% lower than in 1994 and 37% below 1980 levels.

The movement of real wages has very different meanings for Mexican workers compared to US multinationals operating *maquiladora* plants. The latter clearly benefitted from the devaluation’s impact on real wages in Mexico, which declined to the point where they were 1/12th US wages on average. For example, in the fall of 1996, the minimum wage in the US was $4.75 while the minimum wage in Mexico was 41 cents an hour. Therefore, most multinational firms operating in Mexico have lower costs and are more competitive after the peso crisis than before.

III. *Maquiladora* Expansion

The extent of growth of *maquiladoras* in recent years can be observed in Figure 4 below, which is a graph of the number of plants and employment over time. One can see how the number of plants had a growth spurt in the early 1970s, but really took off around 1985. Their is then a significant increase in the slope of both curves around 1994 once NAFTA was in place. The increase in employment in the *maquiladoras* has been such that the percentage of manufacturing that *maquiladoras* represent within Mexico reached 27% in 1996. This is arguably a result of the impact that the crisis of 1995 has had on many of the domestic manufacturers, not only the growth of the *maquiladora* industry.

1 The real wages for the *maquiladora* industry is a rough approximation to 1½ times the minimum wage. (see EPI, 1997).

In order to contrast the growth of the *maquiladora* industry with the negative growth experienced by the Mexican economy, Figure 5 plots the GDP for Mexico with the *maquiladora* production for the years 1991-1995 together. Against the backdrop of the depression of 1995-96, the outstanding growth of the *maquiladora* industry seems

remarkable. How can we explain why the Mexican economy faired so poorly while the transnational corporations (TNCs) operating *maquiladora* plants in Mexico have done so

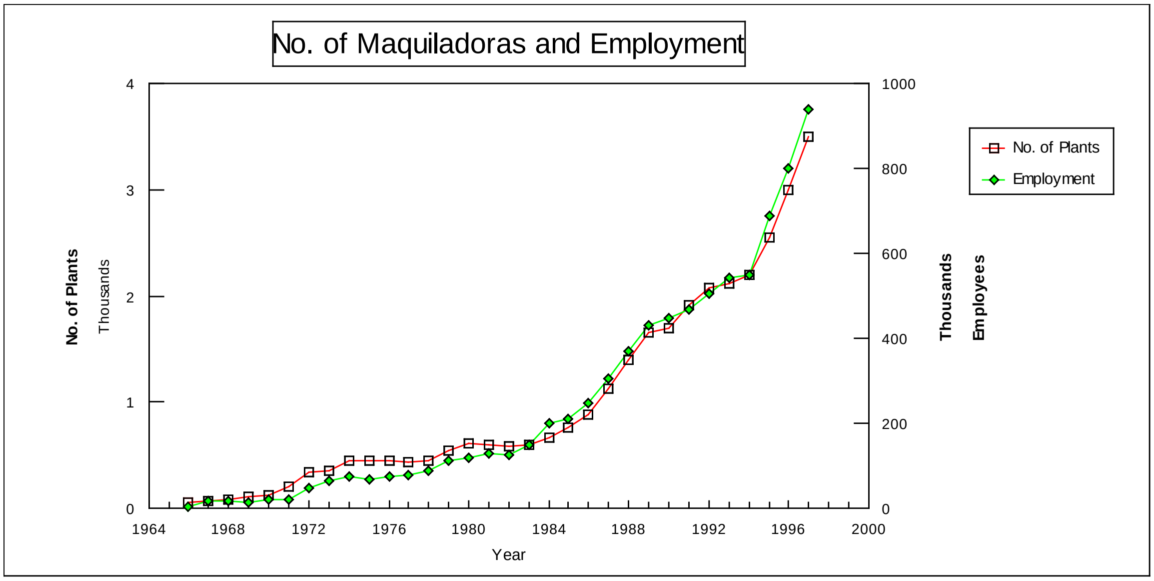

Figure 4. *Maquiladora* Plants and Employment

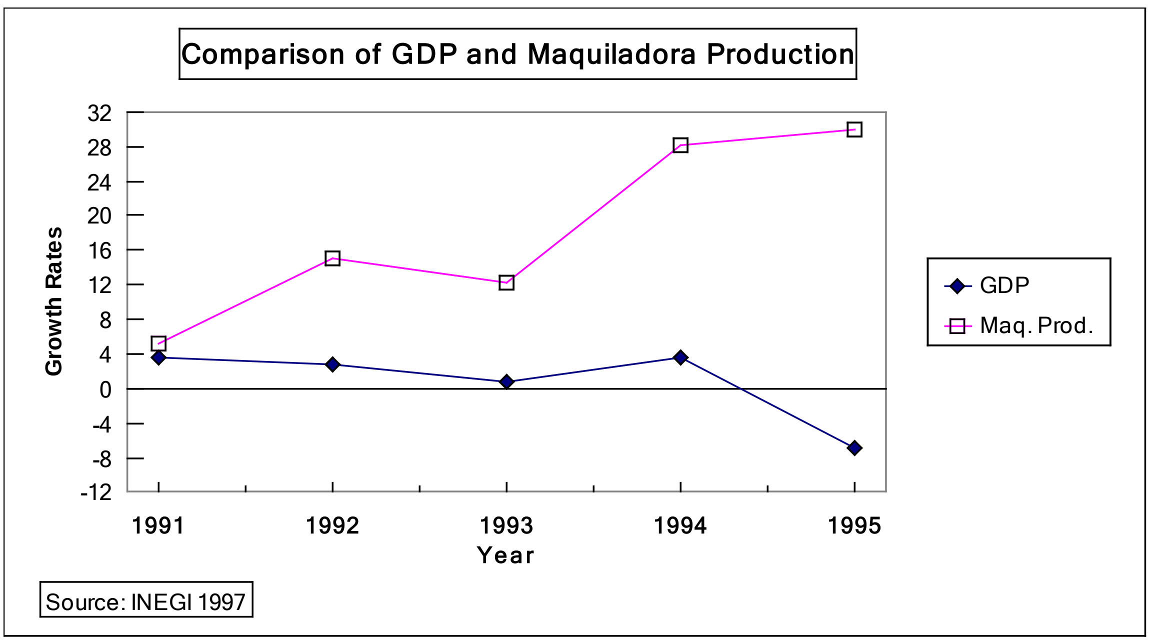

Figure 5. Growth Rates of Mexican GDP vs *Maquiladora* Production

well? A comparison between the conditions in the Mexican manufacturing sector with those of the *maquiladora* sector is a logical first step. Although they share a number of features and conditions - both operating in the national territory of Mexico and subject to many of the same laws - there are several crucial differences that need to be explored, particularly as we contrast the two sets of production conditions.

IV. Comparison of *Maquiladoras* with other Mexican Producers

First, the legal status of *maquiladoras* established in 1965 by the Border Industrialization Program is very significant, as well as any subsequent changes that have come about because of NAFTA. The remaining factors can be placed in three broad groups: (1) market conditions, (2) plant conditions, and (3) state-related and institutional aspects. The principal factors related to market conditions are the different markets for selling goods, and the labor market. Factors that correspond to the second category of plant conditions include the length of the working day, productivity, intensity of labor, and labor organization. Lastly, are the factors that reflect the TNCs' relationships with the Mexican and US governments and other institutions such as the IMF. These include taxes, subsidies, repatriation of profits and royalties, enforcement or non-enforcement of labor and environmental laws.

After the *bracero* program came to an end in 1964, a new program for employing cheap Mexican labor by US firms began in 1965, known as the Border Industrialization Program (BIP). This entailed foreign-owned assembly plants, known as *maquiladoras*, setting up shop in the border region. They would import parts and semi-finished products from the US and after assembly, export the finished goods back to the US, with import duties only on the value added of the work done by the Mexican workers. This was accomplished through the new US tariff items 806.30 and 807.00. In the case of Mexico, they did not apply tariffs on the imports with the provision that the finished products would all be re-exported and thus would not compete with domestic industry.

At that time, there was legitimate concern on the part of the Mexican government that the products from the *maquiladoras* would be sold in Mexico rather than being exported back to the US. This would imply less hard currency being generated from exports and potentially undermining Mexican producers. Therefore, only given the provision that the finished goods would be "exported" back to the US did the Mexican government waive all duties and restrictions on imports of raw materials and parts from the US. In addition, by allowing the US firms to have 100 percent ownership, Mexico made a major exception to its own 1973 Law to Promote Mexican Investment and Regulate Foreign Investment that required all new companies to have at least 51 per cent Mexican ownership, and it was intended that foreign investors set up their factories in less industrialized areas, so as not to compete with Mexican firms.

The rules of the game have changed considerably since the 1970s. In May of 1989, prior to NAFTA, there were significant changes for foreign investment with the elimination of much of the regulations that had been in place since 1973. These were predominanatly related to ownership regulations, and restrictions on repatriation of profits and royalties. With the implementation of NAFTA and the drive to eliminate most trade and tariff restrictions, the 'special' status of *maquiladoras* is expected to be less relevant. However, the suspension of duties on imports destined to *maquiladoras* is still a relevant difference since Mexican firms must still pay the minimum 10% tariff on imports in general. In the not so distant future, the extent to which *maquiladoras* end up selling in the Mexican domestic market may come to be a concern again for Mexican manufacturers.

Market conditions

In contrasting *maquiladora* plants and other producers in Mexico, the different markets that firms are predominantly serving can explain a good deal of the differences in growth. Since Mexico was enduring a depression, the demand for domestic goods declined substantially, however, since the *maquiladora* plants are producing predominantly for the US market (roughly 92%) they were minimally impacted by the decline in demand in Mexico. One needs to distinguish between the Mexican firms that have been able to export since the peso crisis, and those firms which are strictly dependent on domestic demand. While some firms had been exporting previously, a number of Mexican firms have re-oriented their sales toward exports since the consumer demand dropped off considerably. But this is not feasible for all Mexican firms, especially small- and medium-sized firms, that rely on the domestic market. This is clearly related to the inability for many firms in less-industrialized countries to compete against the larger, more technologically advanced multinational, as well as Mexican, corporations. In order to be able to orient one's production toward exports, a firm must be able to compete internationally within their industry. For many Mexican producers, the devaluation meant an increase of costs since many depended on foreign imports as inputs. Although costs of local inputs and labor were not higher, if their technology was not sufficiently productive they often had higher costs of production, and less chance of competing internationally. Furthermore, opportunities to upgrade machinery were substantially reduced as credit became tight and expensive. The outlook was rather different if you were on the other side of the border, and suddenly labor costs in dollars were dropping significantly.

In fact, the most significant impact of the peso crisis and devaluation for the *maquiladora* industry is probably the reduction of wage costs. This comes as no surprise for Marxists, that recognize the tendency for capital to drive down wages, thus providing the conditions for accelerated accumulation and growth. Given the extent and level of poverty in Mexico, it can be argued that the price of labor-power has been depressed below the value of labor power in general. This is supported by the huge difference in wage rates between the U.S. and Mexico. After the devaluation the ratio between Mexican and US wages dropped from $1/7^{th}$ down to $1/12^{th}$ overall, and approximately $1/16^{th}$ in manufacturing. With regards to the contrast between *maquiladora* plants and domestic producers within Mexico, average *maquiladora* wages are 1½ the minimum wage in Mexico.[2] However, this is still about half of the country's manufacturing average wage. This is partially explained by the greater government support in keeping wages down for the *maquiladora* industry. This will be further examined in the section considering the role of state institutions below.

Plant conditions

When considering the incentives for the *maquiladora* plants to expand one needs to compare the conditions in Mexico with those in the US, often at existing plants. Advantages are seen as not only much lower wages, but also the length of the working day, overtime, levels of intensity, productivity, and workshop control are taken into account. Where in the past, concerns of lower productivity proved to be a disincentive, this has become less and less the case. According to Shaiken, several of the *maquiladora* plants producing automobiles or engines, have attained levels of productivity comparable to the US plants producing the same items.[3] This is further supported by research by PeZa, where he refers to several *maquiladora* managers of TNCs claiming higher levels of productivity than their US counterparts.[4] This supports the notion that over the years the northern border region has come to have a more sophisticated labor force than many other less industrialized regions in the world. It can be argued that the skill level of *maquiladora* workers has been increasing despite claims to the contrary by management to treat most of the jobs as unskilled. This is often due to the pressure for higher wages that comes with employment requiring a higher skill level in general.

The level of control from management's perspective is much greater than in the US plants due primarily to the lack of independent unions. This can improve the situation from the firm's perspective in several ways. The more precarious a work force and the less rights workers have, the more firms can force overtime, increase the length of the working day, increase the intensity of work, dock pay, or hire and fire at will (especially workers that start to form a union). The speedup which often takes place is a clear example of increases to absolute surplus value, resulting in a higher intensity of labor compared to the US. The union influence on the shopfloor with regards to workplace rules can limit the capacity for increased speedups among other aspects. The ability to regularly increase the intensity of labor combined with some of the most sophisticated technology available worldwide, such as the Dynapert robotics system, used in electronics assembly, allows firms to simultaneously increase both absolute and relative surplus-value. As

---

2 Ibid.

3 See Shaiken (1994).

4 PeZa, Devon. 1997. The Terror of the Machine.

a result, they can improve their profitability through the lowering of their unit costs, and thus be more competitive on the world market.

Returning to the comparison of the *maquiladora* plants with other Mexican producers, why would the TNCs be able to be more successful in preventing independent unions? In fact, since 1965 not one, (pending the outcome of the seesaw battle at the Hyundai subsidiary, Han Young in Tijuana), has been allowed to exist, even where they have won elections. The answer is partly explained by the corrupt regional arbitrartion boards and a proactive government committed to preventing any bad examples that could jeopardize the flow of foreign exchange into Mexico. Secondly, is the domination of the company unions, usually associated with the corrupt, government-controlled CTM or CROC, which do their best to prevent serious worker representation. Many workers at *maquiladora* plants can be working for months before they even know they have a union 'representing' them.

State-related and institutional aspects

As mentioned at the beginning of this section the third broad group of factors to consider in comparing *maquiladora* plants with other Mexican producers are state-related and institutional aspects. In this regard, the role played by the Mexican nation-state is the most significant. At the same time, the relationship of the Mexican government with TNCs operating *maquiladora* plants also reflects the former's relationship with the US government (and to a lesser degree Japanese and other governements that have *maquiladoras* in Mexico) as well as with international institutions such as the IMF and the WTO. As mentioned earlier, the importance of *maquiladoras* as a source of foreign exchange is critical, especially when considering the $170 billion debt that Mexico owes. At present, the foreign exchange generated by *maquiladoras* is only second to oil exports. These very real conditions help to explain why the Mexican government grants these TNCs certain privileges and impunity that it usually reserves for only certain elite Mexican firms. However, the breaking of Mexico's own laws is coming under greater scrutiny as NAFTA stays on course and the weakness of both the labor and environmental side accords is becoming more generaly recognized.

In addition to being able to take advantage of cheaper labor and weaker enforcement of labor laws, the TNCs are not held to the same environmental standards as the same type plants in the US. Besides the difference in standards, the level of enforcement in Mexico is minimal. This implies that transnational firms are able to get away with not providing basic safety equipment, such as gloves or masks, or installing ventilation systems and thereby jeopardizing workers' health and safety. Secondly, they can afford to be lax about installing required air pollution control devices, properly disposing of waste, or simply using lower cost processes which generate more hazardous waste or pollution for the surrounding environment. In the majority of cases when such issues are brought up by workers, they are often shown the door or even worse, blacklisted. The Mexican government simply turns a blind eye to the violation by these TNCs of many labor and environmental laws. For example, since NAFTA has been in effect, the North American Agreement on Labor Cooperation (NAALC) has completed only 5 reviews of complaints of labor violations, where four out of these 5 have centered upon labor rights violations in Mexico. None of the workers involved in these complaints - more than 200 in total- were reinstated or compensated for serious labor rights violations.

V. Conclusions

As a result of the peso crisis of December 1994 and the subsequent devaluation, Mexico entered its worst depression ever. The impact on workers and peasants being the most severe, as real wages plunged again by over 40% in just one year and more than 50% of the population was living in poverty. And yet in the middle of this crisis, the *maquiladora* industry was booming, growing by over 30% in 1995 alone. In order to explain this seeming anomaly, a comparison of characteristics of *maquiladoras* with other Mexican firms was made.

These ranged from the legal status of *maquiladoras* as established in 1965 to changes that came about through NAFTA and other neoliberal policies such as the foreign investment deregulation of 1989. Three broad categories were also described: market conditions, plant conditions and state-realted and institutional aspects. The most significant characteristics were the different markets where goods were sold and the level of wages. With regards to the former, the importance of distinguishing Mexican firms that were export oriented producers from those relying strictly on the domestic market was evident. With regards to wages, the US and other transnational corporations saw a huge reduction in labor costs in terms of dollars. In contrast, for the small- and medium-sized producers in Mexico, lower real wages were not going to compensate for higher foreign input costs or suddenly allow them to compete globally. Lastly, the influence of the Mexican government in preventing independent unions from operating in the border region and granting the TNCs operating *maquiladora* plants additional privileges and impunity when it came to violations of labor and environmental laws. This situation combined with the technologically advanced assembly plants meant paying wages less than average manufacturing wages in Mexico (not to mention the US), having greater workplace control and not having to recognize worker's rights. All of this translates into some of the most competitive production conditions worldwide, which is how the *maquiladora* industry attained such fantastic growth as most Mexicans tried to ride out the storm of the depression of 1995.

As referred to above, the disporportionate influence of TNCs on the Mexican government, reflects the importance of foreign exchange revenue, which is needed to pay off its $170 billion debt, the second largest for a third world country. After considering the advantages and privileges of many TNCs it seems appropriate to pose the question- are these TNCs advancing Mexico's level of development? In other words, as a result of the *maquiladora* plants, is Mexico obtaining a net gain, and if so, how is it being distributed between classes? Given the appalling statisitics on the economic conditions for the majority of Mexicans, it is fitting to call into question the neoliberal policies that laid the groundwork for the peso crisis and depression of 1995-96, exacerbating the degree of inequality and poverty in Mexico.

References

CEPALC, 1996. Mexico: La Industria Maquiladora.

Economic Policy Institute et. al. 1997. "The Failed Experiment: NAFTA at Three Years".

Fatemi, K. (ed.) 1990. The Maquiladora Industry 'Economic Solution or Problem?',

Praeger Publishers, New York.

Henwood, Doug 1995. "The Contract with Mexico", Left Business Observer, No. 68.

INEGI, 1997. Estadisticas Economicas: Industria Maquiladora de Exportaci\ n, Feb. 97, Mexico.

INEGI, 1996. Estadistica de la Industria Maquiladora de Exportaci\ n 1990-1995, Mexico.

Kopinak, Kathryn 1996. Desert Capitalism 'Maquiladoras in North America's Western Industrial Corridor'. The University of Arizona Press, Tucson.

Krooth, R. 1995. Mexico, NAFTA and the Hardships of Progress, McFarland, North Carolina.

La Botz, Dan. 1992. The Mask of Democracy: Labor Suppression in Mexico Today, South End Press, Boston.

NACLA 1996. "Report on Latino Labor". New York.

NACLA 1997. "Report on Mexico". New York.

Peña, Devon G. 1997. The Terror of the Machine *Technology, Work, Gender & Ecology on the U.S.-Mexico Border.* CMAS (Center for Mexican American Studies), University of Texas at Austin.

Pradilla Cobos, Emilio. 1994. "Los Limites de la Industria Maquiladora Mexicana.", Economia: Teoria y Practica, Nro. 3, 1994.

Shaiken, H. 1994. "Advanced Manufacturing in Mexico: A New International Division of Labor?" Latin American Research Review, 29(2): 39-72.

Shaiken, H. 1990. Mexico in the Global Economy, "High Technology and Work Organization in Export Industries". Center for U.S.-Mexican Studies, Univ. of California, San Diego.

Sklair, L.. 1993. Assembling for Development "The maquila industry in Mexico and the United States". Unwin Hyman, Inc., London.