

Making Markets and Competition Work: Key Initiatives

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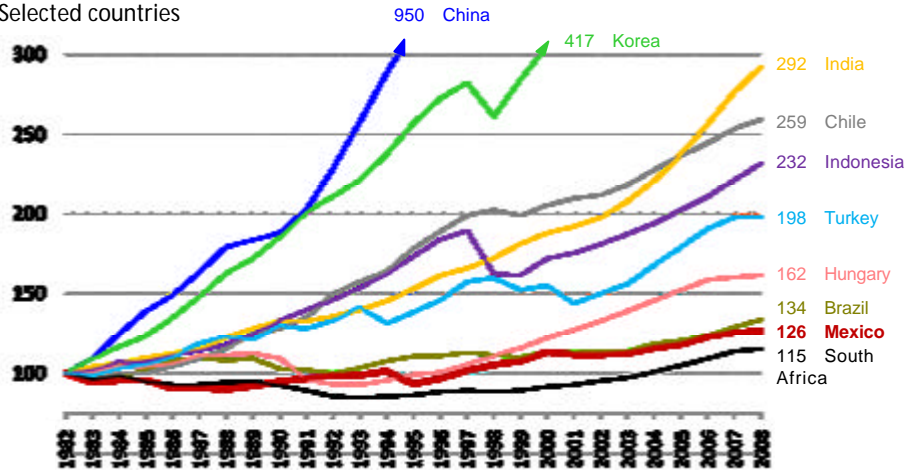
Main messages

- 1 The economic crisis has exposed Mexico's structural problems that have led to low growth low growth.
- 2 A fundamental tool for solving this problem is an economic policy geared towards competition and market efficiency.
- 3 There are significant political obstacles for a policy of this kind, but substantial progress can be made through "surgical" reforms to the legal framework.

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The crisis has shown a structural problem of low growth...

GDP per capita (Constant prices)
Index 1982 = 100
Selected countries



Notes: Estimated values for 2007 and 2008.
Source: International Monetary Fund (IMF), *World Economic Outlook Database*, April 2009

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... associated with low levels of competitiveness ...

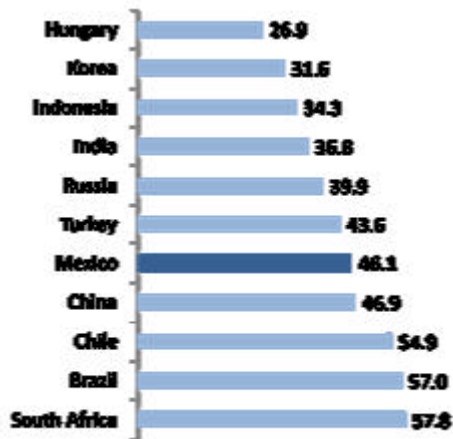
| Institution | Publication | Mexico's ranking | Trend |
|-------------|--|------------------|-------|
| <i>WEF</i> | <i>Global Competitiveness Report 2008-2009</i> | 60 of 134 | ↓ 8 |
| <i>IMD</i> | <i>World Competitiveness Yearbook 2009</i> | 46 of 57 | ↑ 4 |
| <i>WB</i> | <i>Doing Business 2009</i> | 56 of 181 | ↓ 8 |
| <i>IMCO</i> | <i>Situación de la competitividad en México 2006</i> | 33 of 45 | ↓ 3 |

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... and high income concentration

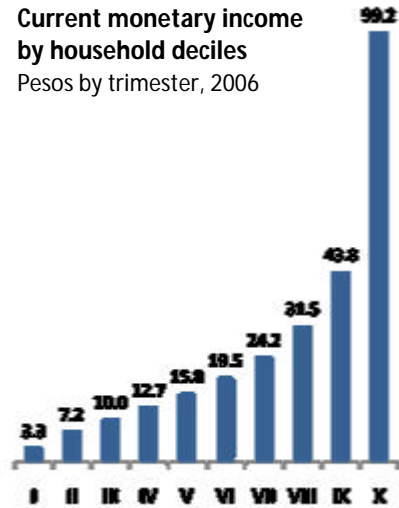
Gini Index

Selected countries, 2006



Current monetary income by household deciles

Pesos by trimester, 2006



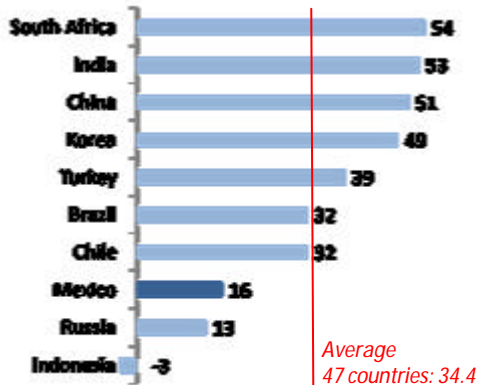
Sources: World Bank, *World Development Indicators 2007*
INEGI, *National Survey of Households' Income/Spending 2006*

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Even before the crisis, there was tenuous support of the market economy in Mexico

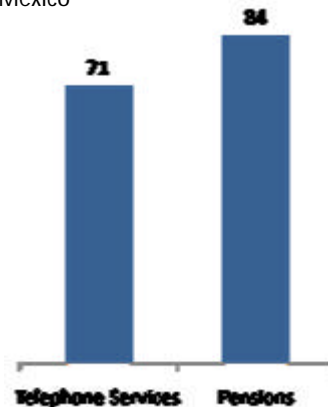
"Most people are better off in a free market economy"

Net % of positive answers*, 2007
Selected countries



"Should be mostly in state hands"

% positive answers, 2008
Mexico



*% of positive answers - % of negative answers
Sources: Pew Research Center, *Global opinion trends 2002-2007*, July 2007
Corporación Latinobarómetro, *Informe 2008*, November 2008

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National and international institutions agree that competition is a key factor to address low competitiveness and growth in Mexico ...



"[La] falta de competencia, particularmente en la provisión de insumos básicos para la producción ... propicia el deficiente desempeño del resto de los factores. Es urgente eliminar las barreras existentes para la entrada a los mercados."



"Para estimular la productividad de las empresas y mejorar su competitividad se requiere más competencia en los mercados."



"Mexico's competition environment, regulatory framework and investment climate are major priority areas to increase Mexico's competitiveness."



"Mexico needs stronger competition and better regulation to boost productivity and growth."



"Strengthening competition (...) should also have high priority, and –as international experience has shown- may also facilitate reform in other areas as well as helping equity."

"Mexico's goods markets suffer from inadequate (foreign and domestic) competition conditions, with overregulated and rather closed key economic sectors. Only by addressing these challenges can Mexico begin to fully leverage its important competitive advantages."

Sources: Banxico, Presentation by Dr. Guillermo Ortiz before the British Chamber of Commerce, December, 2007
IMCO, *Punto de inflexión: Situación de la competitividad de México 2006*
Banco Mundial, *México 2006-2012: creating the foundations for equitable growth* junio, 2007
OCDE, *Economic survey of Mexico*, 2007.
FMI, *México: Staff report for the 2007 Article IV consultation*
WEF, *The Global Competitiveness Report 2007-2008*.

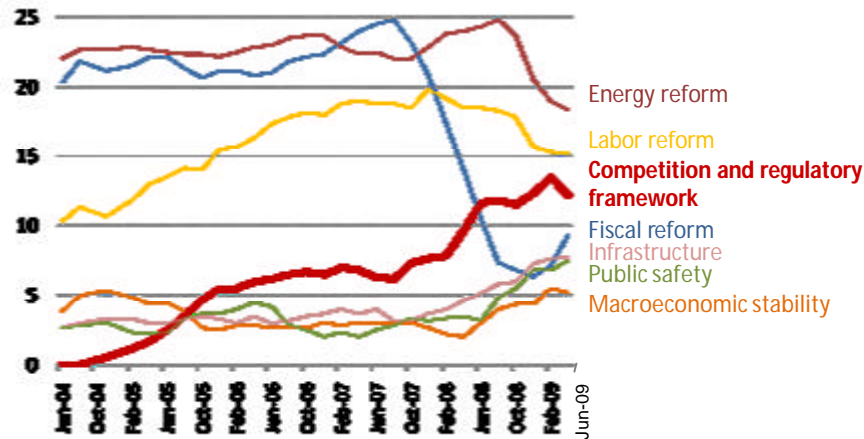
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... an opinion which is increasingly shared by private sector economists

Main policies to encourage higher investment in Mexico

Survey of specialists in private sector economics

% of answers, moving average (6 periods)



Source: Banco de México, Survey on the expectations by specialists in private sector economics 2003 - 2009

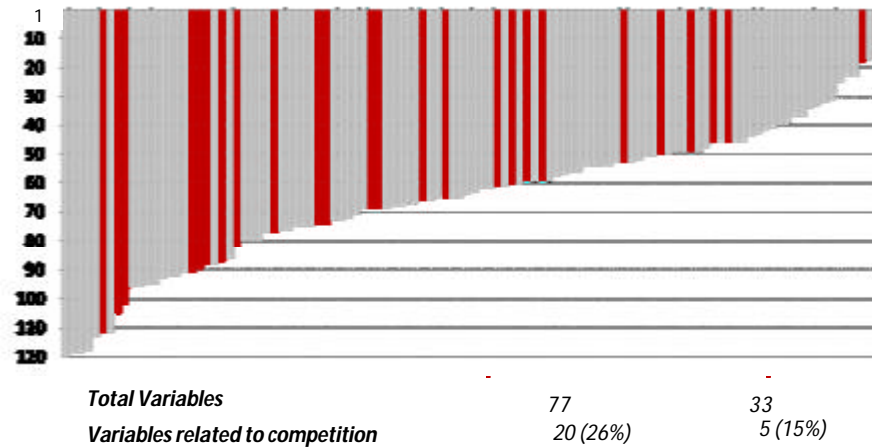
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Lack of competition slows down competitiveness in Mexico...

WEF Global Competitiveness Index Variables

Ranked from the worst to the best position of Mexico

Variables related to competition



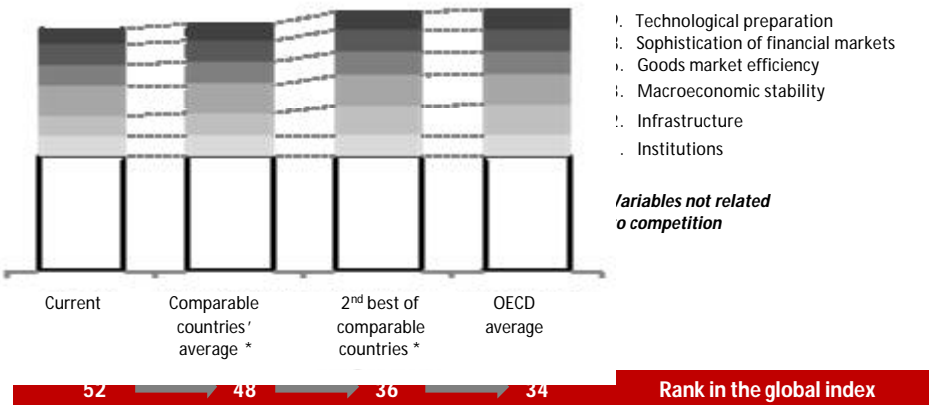
Source: World Economic Forum (WEF), The Global Competitiveness Report 2007-2008; CFC analysis

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... and therefore an effort focused on strengthening competition variables can substantially improve Mexico's ranking in the index

Mexico's score in the WEF Global Competitiveness Index

Rank in the global index for competition variables under different scenarios



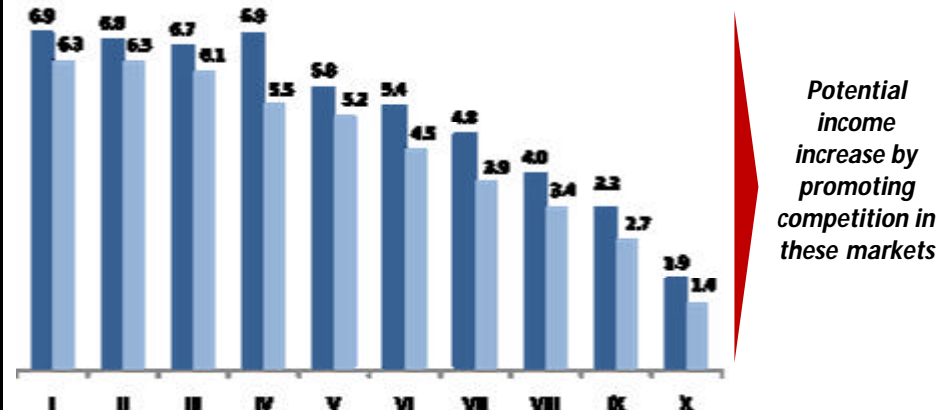
* Brazil, Chile, China, Korea, Hungary, India, Indonesia, Russia, South Africa, Turkey.
Source: CFC analysis based on WEF, *The Global Competitiveness Report 2007-2008*

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Lack of competition also worsens income inequality

Consumer welfare loss from competition problems in 7 markets*

% of total household expenditures by decile

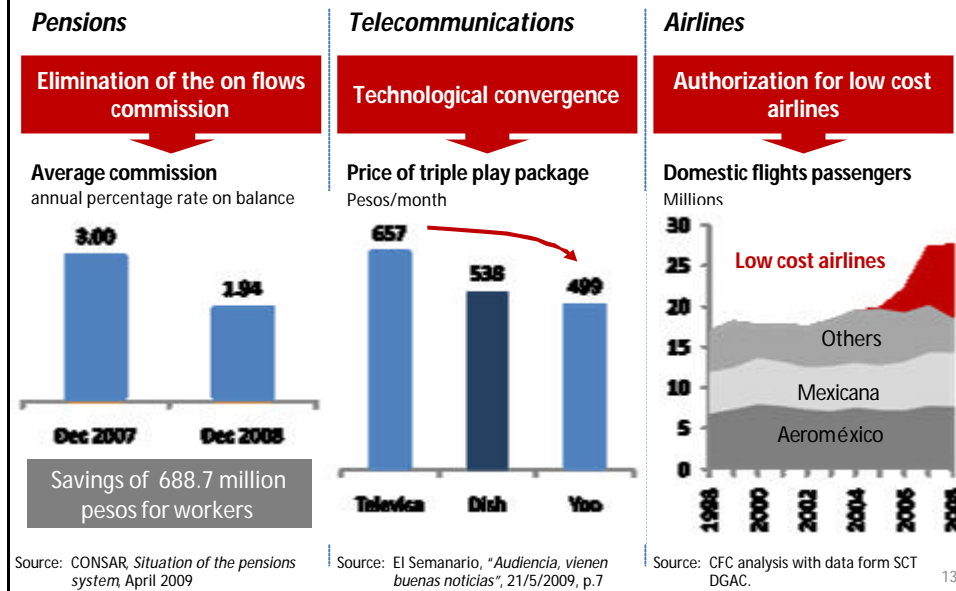


* Corn tortilla; soft drinks, water and juice; beer; medicines; milk; processed meat; chicken and eggs.

Source: Analysis made by Professor Carlos M. Urzúa (2008). "Evaluación de los efectos distributivos y espaciales de las empresas con poder de mercado en México", ITESM, CCM e INEGI, *Encuesta Nacional de Ingresos y Gastos de los Hogares 2006*.

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The results of CFC recommendations show the potential of a procompetitive policy



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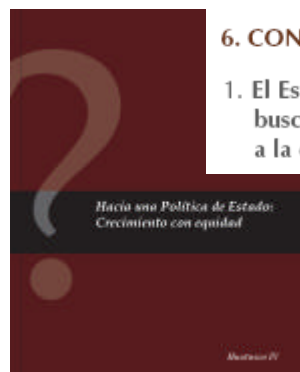
An economic policy oriented towards competition and market efficiency faces resistance from the beneficiaries of the *status quo*

| | First generation reforms | Second generation reforms |
|----------------------------|--|--|
| Strategy for reform | <ul style="list-style-type: none"> • Macroeconomic adjustment • Reduction in size of government • End protectionism and statism | <ul style="list-style-type: none"> • Institutionalization • Strengthening of competitiveness • Education reform, health reform, etc. |
| Main actors | <ul style="list-style-type: none"> • President and cabinet • Central bank • Private sector and investors | <ul style="list-style-type: none"> • President and cabinet • Congress • Bureaucracy • Judicial Branch • Unions • ... |
| Political impact | <ul style="list-style-type: none"> • "Temporary corrections" • Atomization effects | <ul style="list-style-type: none"> • Permanent elimination of privileges for specific groups |

Source: Naím, Moisés, "Latin America: The second stages of reform", *Journal of Democracy* 5, no. 4, 1994

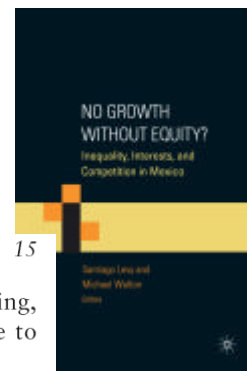
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This trend is emerging as a main factor in the case of Mexico



6. CONCLUSIONES

1. El Estado mexicano ha sido capturado por grupos de poder y buscadores de rentas y ha perdido su capacidad para conducir a la economía por una senda de crecimiento con equidad.



EQUITY, COMPETITION, AND GROWTH IN MEXICO: AN OVERVIEW 15

We argue that Mexico is characterized by a self-sustaining, rent-sharing equilibrium, and that this is the main obstacle to faster growth and reduced inequality.

Source: Grupo Huatusco, *Hacia una Política de Estado: Crecimiento con equidad*, 2005

Levy, Santiago y Michael Walton (eds.), *No Growth without Equity*, Palgrave Macmillan/The World Bank, 2009.

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In order to recover the state’s ability to ensure competition, there is a need for “surgical” legal reforms

| | Current status | Best international practices |
|---------------------------|--|---|
| Maximum fines | <i>1.5 million minimum wages (~82.2 millions of pesos)</i> | 10% of annual sales of the company <ul style="list-style-type: none"> ✓ EU (global sales) ✓ South Africa ✓ India ✓ Brazil: <u>30% of sales</u> |
| Criminal sanctions | <i>Not applicable</i> | <ul style="list-style-type: none"> • United Kingdom: prison terms, up to 5 years • USA: up to 10 years • Australia: up to 10 years • Brazil: 2 to 5 years |