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DIRECTORATE OF
INTELLIGENCE

Intelligence Memorandum

*The Mexican Economy in 1967
and Prospects for 1968*

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CENTRAL INTELLIGENCE AGENCY
Directorate of Intelligence
February 1968

INTELLIGENCE MEMORANDUM

The Mexican Economy in 1967 and Prospects for 1968

Summary

Mexico remains one of the brighter spots in the economic scene in Latin America. Production rose by about 7 percent in 1967 and is expected to continue the rapid growth of recent years in 1968. A high rate of investment and the 1968 Summer Olympics will stimulate construction, industry, and tourism. Also, agricultural output should continue the strong growth recorded in 1967. Pressure on resources may push up prices more than in 1967, but the rise probably will be small by Latin American standards.

The spurt in imports that helped to raise Mexico's trade deficit by \$160 million in 1967 may well continue this year. Exports should recover from last year's stagnation, however, and the Olympic Games should give a good boost to tourist earnings -- which usually cover most of the trade deficit. There appears to be at least an even chance that the deficit on current account can be held at the 1967 level, which can be handled without serious difficulty. Mexico also is in a strong position to cope with an increased deficit, considering its foreign exchange reserves of \$575 million and its excellent reputation as an international borrower.

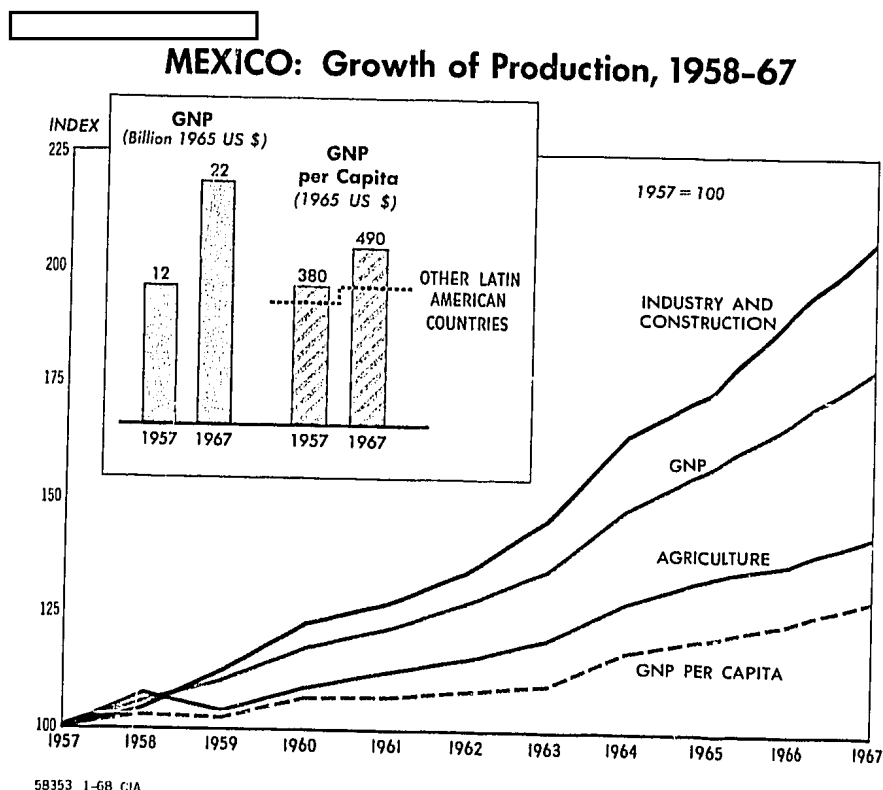
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Recent Growth

1. In 1967, Mexico carried forward one of the most encouraging records of economic growth in Latin America. As in 1966, the total output of goods and services, as measured by the gross national product (GNP), rose in volume by about 7 percent. Even with an increase in population of 3-1/2 percent -- a little above the average for Latin America -- the economy yielded a gain of almost 3-1/2 percent in per capita GNP. Industry continued to lead major economic activities in the pace of expansion. Agricultural production, which has risen for eight consecutive years, increased at an above-average rate (see the accompanying chart).



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2. Mexican economic growth generally has run well ahead of the average in other Latin American countries ever since the beginning of World War II. Moreover, while the rate in the rest of the area has slowed recently, that in Mexico has accelerated. In the last decade alone, Mexico has raised its per capita GNP from \$380 to \$490 while the population has grown by 13 million persons, to a total of 46 million. As the chart shows, Mexico has conspicuously improved its relative position in Latin America with respect to per capita GNP.

3. Rapid expansion has been promoted by a high rate of capital formation. Investment is equivalent to about 19 percent of GNP, compared with an average of 17 percent in Latin America as a whole, and about 90 percent of this investment is financed with domestic resources. Mexico's emphasis on industrialization (especially through import substitution) has greatly stimulated manufacturing. Output in manufacturing industries now accounts for almost 27 percent of GNP, whereas agriculture accounts for only 16 percent. However, various agricultural products -- cotton, coffee, sugar, fresh vegetables and fruits, shrimp, corn, and wheat -- are the leading earners of foreign exchange.

Outlook for 1968

4. In 1968, Mexico is expected to continue the rapid growth that has characterized the economy in recent years. A high rate of government-induced construction activity plus the stimulation provided by the 1968 Summer Olympics are leading growth factors, but agricultural output should show a further strong advance. The presence of investment and rising consumer income on resources may bring a larger increase in prices than in 1967, when the wholesale price index moved up by about 4 percent. The increase should be small by Latin American standards, however, because of cautious fiscal policies of the Mexican government, effective Central Bank restraints on credit expansion, and the likelihood of plentiful food supplies.

5. Prospects are less certain in 1968 for narrowing the perennial trade gap, which in 1967 widened beyond the \$400-million level that can

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readily be covered by tourist receipts. The demand for imports probably will again be strong in 1968. Exports are expected to rise moderately after stagnating in 1967 (see the table). Also, the Olympic Games should bring a substantial rise in Mexico's receipts from tourism, which are the largest in Latin America. The deficit on current account nevertheless may equal or exceed the \$565-million level incurred in 1967.

6. Mexico probably would have considerable room for maneuver in covering such a deficit. Reserves of gold and foreign exchange amounted to about \$575 million at the end of September 1967, and 13 years of exchange stability have given the country an excellent reputation in international credit markets. In part because of government incentives to develop industry on the Mexican-US border, inflows of direct foreign investment also should continue to be strong.

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External Debt

7. Mexico's policy of industrialization has generated heavy demands for imported capital goods and industrial raw materials and has led to heavy borrowing abroad. The medium-term and long-term external debt probably exceeded \$2 billion at the end of 1967. Interest and amortization payments on this debt approximated \$450 million in 1967, or about 28 percent of the value of exports and net earnings from tourism. Debt servicing obligations of this magnitude are manageable. But, as Mexican authorities are aware, a sustained rise in Mexico's deficit on current account at the rate recorded in 1967 could threaten the peso.

Stability of the Peso

8. Since the last devaluation of the peso, in April 1954, the Central Bank rate has been steady at 12.5 pesos to the US dollar. The peso is a hard and freely convertible currency. After the devaluation of the British pound, the Mexican Finance Secretary stated that Mexico would continue to sell gold freely.

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9. The government now is under growing pressure to accelerate outlays on basic development projects, which have been curtailed for the past three years. Pressures to benefit rural areas are particularly strong. Although average income per rural inhabitant has grown at about the same rate as per capita incomes in urban areas, most of the gains have been made by farmers producing cotton, wheat, and a few other crops on large-scale, mechanized farms. As a consequence, poverty in rural areas still is widespread and severe.

10. The government also must complete facilities for the 1968 Summer Olympics, repair extensive damage caused by hurricanes in late 1967, and continue with construction of a subway for Mexico City. Higher interest rates may dampen private investment, but this squeeze probably would only partly offset the rise in public investment. Increased demand by investors for imported capital goods and industrial raw materials thus may well raise balance-of-payments difficulties in 1968. To cope with this, the government would have to implement an administratively difficult cutback in public investment, levy additional taxes, or further restrict credit to the private sector, thereby weakening an already depressed private housing market. The Diaz Ordaz administration nevertheless can be expected to react quickly and effectively, continuing the prudent financial policies that it has pursued during its first three years in office.

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Table

Mexico: Balance of Payments
1965-67

	Million US \$		
	1965	1966	1967 (Estimated)
Imports	1,560	1,605	1,765
Exports	1,114	1,192	1,190
Trade surplus (+) or deficit (-)	-446	-413	-575
Net receipts from tourism <u>a/</u>	368	385	400
Net receipts from other services, production of gold and silver, and transfer payments	-319	-324	-390
Current account surplus (+) or deficit (-)	-397	-352	-565
Net receipts of long-term capital	163	355	575
Net receipts of short-term capital <u>b/</u>	176	-2	
Payments surplus (+) or deficit (-)	-58	+1	+10
Corresponding increase (-) or decrease (+) in holding of foreign assets	+58	-1	-10

a. Including border trade.

b. Including net errors and omissions.

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