Executive Summary
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How Reforms in Mexico Could Make the U.S. More Secure

James M. Roberts and Israel Ortega

President Felipe Calderón has made significant progress in the fight against narcotrafficking, but Mexicans are still waiting to see whether his government will successfully challenge the private- and public-sector monopolies and duopolies that dominate huge portions of Mexico's economy in energy, telecommunications, construction, food production, broadcasting, financial services, and transportation and have long been a drag on competitiveness and job creation. Notwithstanding Mexico's membership in the North American Free Trade Agreement (NAFTA), this "roping off" of large sectors of the Mexican economy to benefit politically powerful rent-seekers has the same practical effect that traditional protectionist trade barriers have.

Calderón should also lead the fight to dismantle a state-corporatist system of price supports, subsidies, and special-interest tax exemptions that gives an unfair advantage to the wealthy and well-connected while restricting competition and holding down economic growth and job creation.

Evidence of the damage to the Mexican economy from the lack of competition can be seen in the *2008 Index of Economic Freedom*, published by The Heritage Foundation and *The Wall Street Journal*. Mexico achieved only ninth place out of 29 Western Hemisphere countries, well behind Canada, the U.S., Chile, and El Salvador.

"Supply Push" and "Demand Pull." There is a clear link between Mexico's economy and America's immigration problems: Mexico's 50-year failure to realize its full economic potential has caused unemployed, unskilled Mexicans to be "pushed" toward the U.S. The artificially low cost of this illegal labor here has multiplied its value and created a strong "demand pull."

It is equally clear that illegal immigration directly affects America's economy, culture, and future as a nation. Currently, anywhere from 12 million to 20 million illegal aliens reside in the United States—enough to populate America's three largest cities: New York, Los Angeles, and Chicago. An estimated half-million more people enter illegally every year.

If Mexico made the changes required to reduce the "supply push," and if the U.S. diminished the power of the "demand magnet" by simultaneously implementing much-needed improvements in its border control and immigration laws, the result would be new, sustainable private-sector jobs. More Mexicans would want to stay home to start businesses; others would stay to work for them. Some Mexicans currently in the United States would likely return home and use their savings to start small businesses. In the U.S., prospective employers of legal laborers would be forced to pay the true cost

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of that labor, including taxes to offset the additional costs to the government that are generated by these new residents; migration pressures would be reduced; the unemployment rate would drop; and national security would be enhanced.

An emerging industrial nation, Mexico is at a point similar to that of the United States at the beginning of the 20th century, when President Theodore Roosevelt pressured Congress to enforce existing anti-trust legislation and create the Interstate Commerce Commission. By doing so, Roosevelt led the U.S. government to curb the ability of powerful banking, oil, and steel magnates to block competition. President Calderón faces a similar situation today, with entrenched economic interests and a Congress—dominated by leftist parties that favor statist policies—that obstinately defend the status quo. Can Felipe Calderón be the Teddy Roosevelt of Mexico? He has five more years to secure that place in history. If he succeeds, both Mexico and the United States will be the better for it.

What Should Be Done. Mexico should open its nationalized oil, natural gas, and electricity sectors to private investment and participation. Pemex should lease deep-water areas in the Gulf of Mexico to private oil companies to develop the fields, sell the oil, and pay royalties from profits to the Mexican government. Private electric companies in Mexico and the U.S. should be encouraged to sell power to the state-owned Federal Electricity Commission and Central Power and Light and to build and operate additional power plants in Mexico.

Mexico should break up private-sector monopolies and duopolies with more effective anti-trust legislation and should enforce its laws more aggressively to protect intellectual property rights (IPR) for both Mexicans and foreigners, increasing funding and staffing of the three relevant government agencies (the Office of the Attorney General, the Mexican Institute of Industrial Property, and the National Institute of Author Rights), and should train Mexican police and the Mexican Customs Service to spot—and prosecute—IPR violations.

Mexico should eliminate the price controls and subsidies that have tilted the competitive playing field toward monopolies and duopolies. This would encourage foreign direct investment and competition in all sectors, resulting in lower prices for Mexican consumers.

Mexico should implement a multi-year infrastructure-improvement plan with dramatically increased public and private funding (e.g., privately owned toll roads), beginning with the Mexican Congress's passage of the ambitious infrastructure program recently proposed by President Calderón.

The U.S. Department of Justice should investigate the operations of Mexican monopolies in the United States, especially in the telecommunications, transportation, and energy sectors. The department should identify those monopolies and describe any actions that the U.S. government can take to encourage them to welcome viable domestic and foreign competitors. The U.S. Department of the Treasury should commission an independent study to determine the level of remittances in all forms that are sent to Mexico by migrants in the U.S.

The Bush Administration and the Mexican government should design new co-funded programs focused on intensive infrastructural, developmental, and technical assistance in regions of Mexico that are the major sources of migration to the U.S. The Bush Administration and the Mexican government should also design new assistance programs in conjunction with leading U.S information technology and adult-education companies to improve educational opportunities in Mexico. Private U.S. companies should fund the bulk of the projects in return for access to the Mexican market.

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How Reforms in Mexico Could Make the U.S. More Secure

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Felipe Calderón, who began his single *sexenio* (six-year term) as President of Mexico in December 2006, has made significant progress in the fight against narcotrafficking, but Mexicans are still waiting to see whether his government will successfully challenge the private- and public-sector monopolies and duopolies that dominate huge portions of Mexico's economy.

These combines—in energy, telecommunications, construction, food production, broadcasting, financial services, and transportation—have long been a drag on competitiveness and job creation. Notwithstanding Mexico's membership in the North American Free Trade Agreement (NAFTA), this "roping off" of large sectors of the Mexican economy to benefit politically powerful rent-seekers has the same practical effect that traditional protectionist trade barriers have.

Calderón should also lead the fight to dismantle a state-corporatist system of price supports, subsidies, and special-interest tax exemptions that gives an unfair advantage to the wealthy and well-connected while restricting competition and holding down economic growth and job creation.

Evidence of the damage to the Mexican economy from the lack of competition can be seen in Mexico's ranking in the *2008 Index of Economic Freedom*, published by The Heritage Foundation and *The Wall Street Journal*. Mexico's economy scored 66 of a possible 100 (with zero being "least free" and 100 indicating "most free"), making it the world's 44th freest

Talking Points

- Private- and public-sector monopolies and duopolies dominate huge portions of Mexico's economy, reducing competitiveness.
- Mexico's statist-corporatist price supports, subsidies, and special-interest tax exemptions unfairly advantage wealthy and well-connected business and political elites, especially the Institutional Revolutionary Party (PRI), which strongly resists reform.
- Failures in Mexico's economic model have "pushed" millions of unemployed semi-skilled and unskilled Mexican workers toward the U.S., creating a crisis on both sides of the border and impairing U.S. national security.
- Huge remittances allow Mexican politicians to avoid confronting structural economic problems.
- President Felipe Calderón must reform the economy to create new private-sector jobs so that Mexicans will want to stay home to work and start small businesses.
- President Bush and Congress should support the Mexican government's efforts to help solve the immigration crisis, open Mexico to more U.S. exports and investment, and secure our border.

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economy out of the 157 countries ranked in the *Index*. It also ranked ninth out of 29 Western Hemisphere countries, well behind Canada, the U.S., Chile, and El Salvador.

Mexico's overall *Index* score is only marginally higher than the regional average in the Americas. In addition, although Mexico's overall score has improved slightly in the year since Calderón took office, it has not changed much in recent years, and this lack of change is due, at least in part, to the absence of any meaningful reform process.[1]

The health of Mexico's economy has a direct impact on U.S. immigration patterns. The failure of the Mexican economy to perform at peak efficiency and to realize its full potential over the past half-century has resulted in a flood of unemployed semi-skilled and unskilled Mexican job hunters seeking employment with their alluringly successful neighbor to the north. Illegal workers from Mexico are often willing to accept lower wages than legal U.S. workers will accept. U.S. employers in various labor-intensive fields operate much more efficiently than their Mexican counterparts do, and these low-wage workers magnify that productivity. The artificially low cost of this labor (which also does not include all of the taxes necessary to offset the additional costs to the government that are generated by these new residents) has created a strong demand for illegal workers from Mexico.

To remedy this situation, the Mexican government should open its oil, natural gas, and electricity generation and distribution sectors to private investment and participation. It should also break up private-sector monopolies and duopolies with more effective anti-trust legislation. The U.S. government should offer technical assistance to help Mexico liberalize and open up its economy. The resulting flood of new private investment would create hundreds of thousands of new jobs that would encourage many would-be economic migrants to remain at home in Mexico.

"Supply Push" and "Demand Pull"

Immigration has become the most controversial, complex, and sensitive subject facing the United States today. It directly affects America's economy, culture, and future as a nation. Currently, anywhere from 12 million to 20 million illegal aliens reside in the United States—enough to populate America's three largest cities: New York, Los Angeles, and Chicago. An estimated half-million more people enter illegally every year.

As the Milken Institute's Joel Kurtzman has reported, former President Vicente Fox hoped to see 6 million jobs created during the six years of his presidency (2000–2006). Of course, neither presidents nor governments can create good sustainable jobs; only the private sector can do that. The role of government is to set policies conducive to that job creation. In any case, Fox "fell far short" of his goal:

> Between 2000 and 2006…Mexico created only 1.4 million jobs. Though accurate figures are difficult to arrive at, the [U.S. Government] Accountability Office estimates that during each year of Mr. Fox's presidency between 400,000 and 700,000 illegal immigrants arrived in the United States from Mexico. The number of illegal immigrants from Mexico was roughly equal to the number of jobs Mr. Fox did not create.[2]

If the Mexican government were to make the many changes needed to reduce the "supply push," and if the U.S. were simultaneously to make necessary changes in its immigration laws to weaken the "demand pull," there would be several positive developments. In Mexico, the result would be the creation of new, sustainable private-sector jobs. More Mexicans would want to stay home to start businesses, and others would stay to work for them. Some Mexican migrants currently working in the United States would very likely return home, using their savings to start small businesses.

1. Kim R. Holmes, Edwin J. Feulner, and Mary Anastasia O'Grady, *2008 Index of Economic Freedom* (Washington, D.C.: The Heritage Foundation and Dow Jones & Company, Inc., 2008), pp. 275–276, at *http://www.heritage.org/index/countries.cfm*.
2. Joel Kurtzman, "Mexico's Job-Creation Problem," *The Wall Street Journal*, August 3, 2007, p. A9, at *http://www.milkeninstitute.org/publications/publications.taf?function=detail&ID=38801010&cat=Arts*.

On the U.S. side of the border, prospective employers of legal immigrants would be forced to pay the full, true cost of that labor, including taxes to offset the additional costs to the government that are generated by these new residents, thereby weakening the demand magnet. The result would be a lessening of migration pressures at the U.S.–Mexico border, a reduction in the U.S. unemployment rate, and improved U.S. national security.

Creating an Opportunity Society in Mexico

Under Vicente Fox, who governed Mexico and headed the center-right National Action Party (PAN) from 2000 to 2006, a divided Mexican Congress adopted some needed reforms after 71 straight years during which the center-left Institutional Revolutionary Party (PRI) had reigned supreme by controlling both the presidency and the Congress. The PRI, backed and financed *inter alia* by the Pemex and electricity workers unions, enjoyed such total control that pundits jokingly described Mexico as "the Soviet Union of the Western Hemisphere."[3]

In December 2006, Fox's fellow PAN-ista, Felipe Calderón, succeeded him as president after barely defeating Andres Manual Lopez Obrador of the leftist Revolutionary Democracy Party (PRD). Lopez Obrador is from the same mold as Venezuelan dictator-president Hugo Chavez, and his election would have been a major blow to economic reform in Mexico as well as to the national security of the United States. Calderón, a lawyer who also earned a master's degree in public administration from Harvard University's Kennedy School of Government, had been President Fox's energy minister.[4]

Mexico has benefited from its more than 10 years of membership in the North American Free Trade Agreement (NAFTA) with Canada and the United States. In fact, to some degree, Calderón can thank the thousands of new middle-class Mexican voters that NAFTA has created for giving him his razor-close margin of victory.[5] They did not fall for the false promises of the populist left.

Nevertheless, the Mexican government has failed to implement fully the many reforms that were envisaged when Mexico joined NAFTA—reforms that would have created more opportunities for employment and prosperity in Mexico.

For example, of the 178 countries covered in the World Bank's *Doing Business 2008* report, Mexico ranks 134th with regard to employment: Hiring employees is problematic, there are rigid restrictions on shift scheduling, and firing anyone is extremely difficult.[6] Another economic performance indicator is Mexico's ranking in the *Index of Economic Freedom*, published by The Heritage Foundation and *The Wall Street Journal*. Although NAFTA membership has helped Mexico to improve its overall ranking from 85th of 160 countries in 1998,[7] when it had just entered NAFTA, to 44th of 157 countries in 2008, it still places only ninth out of 29 Western Hemisphere countries, well behind Canada, the U.S., Chile, and El Salvador.[8]

According to the United Nations Development Program's *Human Development Index*, Mexico ranked 53rd of 177 countries in 2006, which is relatively low for an emerging-market country and indicates a substantial poverty problem.[9] Similarly, Mexico's "Gini coefficient," a measurement of

3. Author's recollection from service at the U.S. Embassy in Mexico City, 1982–1984.
4. Government of Mexico, "President of the United States of Mexico," September 18, 2007, at *http://www.presidencia.gob.mx/en/felipecalderon/* (February 14, 2008).
5. Alejandro Moreno, "The 2006 Mexican Presidential Election: The Economy, Oil Revenues, and Ideology," *PS: Political Science and Politics*, January 2007, at *http://www.apsanet.org/imgtest/PSJan07Moreno.pdf* (May 8, 2008).
6. World Bank Group, "Mexico," in *Doing Business 2008*, at *http://www.doingbusiness.org/ExploreEconomies/?economyid=127* (February 12, 2008).
7. Bryan T. Johnson, Kim R. Holmes, and Melanie Kirkpatrick, *1998 Index of Economic Freedom* (Washington, D.C.: The Heritage Foundation and Dow Jones & Company, Inc. 1998), pp. 363–364.
8. Holmes, Feulner, and O'Grady, *2008 Index of Economic Freedom*, pp. 275–276.
9. United Nations Development Program, *2006 Human Development Index*, 2007, at *http://hdr.undp.org/hdr2006/statistics/* (December 10, 2007).

income inequality, has not improved much over the past 10 years.[10]

According to Inter-American Development Bank (IADB) statistics, Mexico's economy is heavily dependent not only on its commercial relations with the U.S., but also on the more than $24 billion in remittances that Mexican migrant workers in the U.S. send home each year.[11] These remittances equal about "one third of the total wage earnings in the formal sector of the Mexican economy and 10 percent of Mexico's exports."[12] Many observers believe the actual measure of annual remittances would be even larger if it measured the flows through other channels, like the unknown quantity of cash that migrants bring with them when they make visits back home, as well as money sent via the Internet and cash smuggled in by criminals. These channels are not reflected accurately in the official statistics.[13]

In addition, recent reports indicate that the level of remittances may be falling, reflecting the economic uncertainty in the U.S.[14] If so, this will put more pressure on the Calderón government to act quickly to reform the economy.

Tempted to Take the Easy Way Out

Historically, Mexican leaders have taken the easy way out—encouraging out-migration and receiving large inflows of hard-currency remittances in return—rather than confronting their economy's structural problems. In so doing, they took a page from the late Marshall Tito of Yugoslavia, who did the same thing when confronted with the failure of the Communist economic system in the 1970s. Tito simply exported his surplus workers to Western Europe.[15]

While this artful dodging by the politicians has benefited the elites who control the monopolies, state-owned firms, and powerful unions that represent their workers, it has not responded to the needs and aspirations of the average Mexican citizen. Mexicans might be able to get higher-paying jobs in the U.S. as illegal aliens, but they must live in constant fear of deportation. Many of these illegal workers are young single men, the demographic most likely to commit crimes and abuse drugs and alcohol.[16]

The failure of the Mexican government to address these problems has been widely noted. According to the U.S. Department of State, for example:

> Mexico has become less competitive relative to other emerging economies, particularly China but also India and countries in Eastern Europe, as it has failed to address serious crime and safety issues or pass much needed fiscal, labor and energy sector reforms. Recent reports from AT Kearney, Transparency International, the World Economic Forum and the Organization for Economic Cooperation and Development

10. World Bank, *World Development Indicators Online*, 2007, at *http://go.worldbank.org/B53SONGPA0* (November 2007; subscription required). The Gini coefficient measures income inequality on a scale from zero to one, with one being perfect inequality and zero being perfect equality. See Francisco H. G. Ferreira, "The Role of Conditional Cash Transfers in the Process of Equitable Economic Development," at *http://siteresources.worldbank.org/SAFETYNETSANDTRANSFERS/Resources/281945-1131468287118/1876750-1140119752568/Ferreira_En.pdf*.
11. Press release, "Migrant Workers Worldwide Sent Home More Than US$300 Billion in 2006, New Study Finds," Inter-American Development Bank, October 17, 2007, at *http://www.iadb.org/news/articledetail.cfm?Language=En&artid=4077&artType=PR* (November 26, 2007).
12. Steve H. Hanke, "Mexico's Yugoslav Model," *Latin Business Chronicle*, June 26, 2006, at *http://www.cato.org/pub_display.php?pub_id=6483* (February 12, 2008).
13. "International Forum on Remittances 2007," International Fund for Agricultural Development, at *http://www.ifad.org/events/remittances/index.htm* (November 26, 2007).
14. Manuel Roig-Franzia, "Mexicans Get Less Aid from Migrants," *The Washington Post*, April 18, 2008, at *http://www.washingtonpost.com/wp-dyn/content/article/2008/04/17/AR2008041703786.html* (April 24, 2008).
15. Hanke, "Mexico's Yugoslav Model."
16. Heather MacDonald, "The Illegal-Alien Crime Wave," Manhattan Institute *City Journal*, Winter 2004, at *http://www.city-journal.org/html/14_1_the_illegal_alien.html* (April 25, 2008).

> (OECD) have detailed the perceived decline in Mexico's attractiveness as an investment destination.[17]

Taking on the Drug Kingpins. Although President Calderón pledged during the 2006 presidential campaign to continue the modest economic liberalization efforts begun by Fox, he has spent more of his political capital on another worthy goal—fighting the dangerous and *über*-wealthy organized crime networks that traffic and ship illegal drugs through Mexico to the USA. This illicit activity is one of the main contributors to the pervasive atmosphere of corruption that has long plagued Mexico.

Calderón's efforts have had some success: The cartels are running scared and trying to shake Calderón's confidence with a series of brutal assassinations of Mexican law enforcement officers and military officials (and, in some cases, their families) who are involved in the fight against the narcoterrorists. But Calderón has not backed down. As *Time* magazine reported recently:

> "When you see the killings, the cartels are trying to make a statement to the authorities not to interfere with their enterprises. And they are also trying to send a message to the public saying they are in control," said a U.S. anti-drug official…. "It's a P.R. campaign. But it's not going to work. Because, quite frankly, this country has a new sheriff."[18]

Presidents Bush and Calderón recently announced a joint U.S.–Mexico program, the Mérida Initiative, to support the Mexican government in its war against drugs by providing U.S. technical assistance, training, high-tech surveillance equipment, and anti–money laundering financial intelligence software. Funding of $550 million for the second tranche of the three-year project was included in the Bush Administration's FY 2009 budget request to Congress.[19] When added to the first appropriation for the Mérida Initiative that was requested in the FY 2008 War Supplemental, the total funding to date is $950 million for Mexico and $150 million for Central American countries to fight against drug-related gang violence.

A More Insidious Threat: Economic Stagnation. Mexicans are still waiting to see whether the Calderón government will bring the same degree of commitment and resolve it has demonstrated in the drug war to the many systemic and structural problems that historically have prevented the Mexican economy from performing anywhere near its full potential. At growth of just 3 percent, Mexico's roughly $900 billion economy lags behind both Brazil (4.5 percent) and the overheated, poorly managed Argentine economy (a sizzling 8.5 percent).[20]

Calderón is acutely aware of the huge growth opportunities that Mexico is missing domestically, as well as Mexico's increasing vulnerability to competition from Asia, and has proposed an ambitious package of reforms to the Mexican Congress.[21] Calderón's reputation as a pragmatist may help him strike a political deal with the lawmakers.[22] The PRI's nearly 80-year hold on political power in the Congress through deeply entrenched, well-connected economic monopolies, however, is proving difficult for Calderón to unravel.

In a hopeful sign, Calderón recently announced the creation of a $25 billion fund to build highways,

17. U.S. Department of State, Bureau of Economic, Energy and Business Affairs, "2006 Investment Climate Statement—Mexico," at *http://www.state.gov/e/eeb/ifd/2006/62015.htm* (February 12, 2008).
18. Ioan Grillo, "Mexico's Narco-Insurgency," *Time*, January 25, 2008, at *http://www.time.com/time/world/article/0,8599,1707070,00.html* (February 12, 2008).
19. Ray Walser and James M. Roberts, "The U.S. and Mexico: Taking the 'Mérida Initiative' Against Narco-Terror," Heritage Foundation *WebMemo* No. 1705, November 16, 2007, at *http://www.heritage.org/Research/Crime/wm1705.cfm*.
20. U.S. Central Intelligence Agency, *The 2008 World Factbook*, at *https://www.cia.gov/library/publications/the-world-factbook/index.html* (April 25, 2008).
21. Andrew Dean, Deputy Director, Economics Department, Organisation for Economic Co-operation and Development, "The Macroeconomic Challenges for Mexico," OECD Forum on the Mexican Economy, February 7, 2007, p. 3, at *http://www.oecd.org/dataoecd/8/46/38255270.pdf* (February 20, 2008).
22. "Calderón Reshuffles Mexican Cabinet," *Latin American Weekly Report,* January 17, 2008.

bridges, and other infrastructure. As the *Los Angeles Times* reported, Calderón wants to avoid dependence "on the external motor of the U.S. economy" to keep Mexico growing. He also warned that Mexico must make "difficult decisions" to reverse the decline in Pemex's production and to raise funds from a source other than the government budget to "pay for exploration in the deeper waters of the Gulf of Mexico." The money, Calderón said, could come only from two sources: reducing government spending for public services or looking to the examples of China, Norway, and Brazil, where the state-owned oil companies benefit from private investment.[23]

President Calderón faces an uphill fight to win reforms from the divided Mexican Congress to permit greater private investment in the energy sector. The opposition, including entrenched special interests in the PRI and anti-globalization activists in the PRD, will try to "forestall reaching the two-thirds majority needed to change Mexico's constitution and allow for participation of private companies in oil exploration and production."[24]

A Choke-Hold on the Mexican Economy

Numerous private- and public-sector monopolies—in energy, telecommunications, construction, food production, broadcasting, financial services, and transportation—have long been a drag on competitiveness and job creation in Mexico. The oil firm (Pemex) and electric power company (Federal Electricity Commission) are both state-owned monopolies, and neither one has been disciplined by competition. Massive privately owned firms have functioned like monopolies and duopolies in telecommunications (Telmex); television networks (Televisa); cement (Cemex); bread and tortilla manufacturing (Bimbo and Maseca, respectively); and banking (Banamex/Citigroup and Bancomer/Banco de Bilbao). They enjoy monopoly rents by using their significant influence with the Mexican government to stifle competition.

As a result, Mexican consumers pay higher prices for a lower quality of service and reduced availability of goods. In addition, Mexico's state-corporatist system of price supports, subsidies, and special-interest tax exemptions gives an unfair advantage to other wealthy and well-connected businessmen while restricting competition and obstructing economic growth.[25] Of course, the most critical result for Mexico's workers is a severe shortage of jobs.

Mexico's largest unions have had a stranglehold on the Mexican labor sector since the 1930s. Granted immense leverage in workplaces, as well as tremendous resources and political power, they enjoy "closed shop" hiring and firing prerogatives, leadership elections by acclamation, and mandatory dues without transparency.

"Although union membership is gradually declining," reports the Economist Intelligence Unit, "the percentage of unionized workers remains above 30 percent," mostly "at industrial plants employing 20 or more workers. Independent unions are rare in Mexico."[26] The majority of workers belong to one of only nine national labor unions, which "enjoy strong political ties and are often organized to rally in support of a politician's campaign. Likewise, a politician who confronts unions can expect to face union-led street protests."[27]

The economic stagnation that has resulted in part from the structural distortions to the economy caused by the rigid labor market has forced 40 percent of Mexico's workers into the informal sector.

The immense political power of the National Educational Workers' Union (a teachers' union with about 650,000 members and the largest labor union in Latin America), or the oil workers' union (the richest in Latin America), or the social security

23. Héctor Tobar, "Mexican President Foresees Friendlier U.S.," *Los Angeles Times*, February 7, 2008, p. 3, at *http://www.latimes.com/news/nationworld/world/la-fg-calderon7feb07,0,3213962.story* (May 7, 2008).
24. Charles Newberry, Michael O'Boyle, and Daniel Horch, "LatamWatch: Mexico Readies More Econ Reforms: Mon Pol on Hold," *MarketNews International,* January 14, 2008.
25. Holmes, Feulner, and O'Grady, *2008 Index of Economic Freedom*, pp. 275–276.
26. Economist Intelligence Unit, "Mexico Risk: Risk Overview," *Country Briefing*, November 15, 2007.
27. *Ibid.*

employees' union (which has thwarted any attempt at pension or health reform for years) remains largely unchecked. Even a weak attempt at reforming the labor market by "the Fox administration—which avoided sensitive measures, such as linking wage rises to productivity increases—was rejected" due to "the lobbying power of the influential public-sector unions."[28] This locked-down situation leaves legions of informal and part-time workers out in the cold.

The remittances that Mexican workers in the U.S. send home to their families are spent mostly on goods and services. If a portion of this money could be drawn into investments to start small and medium-sized businesses in Mexico, and if those investments could be made in the context of a reformed domestic economic environment, the resulting economic stimulation and job growth would reduce out-migration pressures significantly. This could be achieved if Mexico's federal and state governments adopted pro-growth economic policies centering on job creation, robust free-market competition, monopoly-breaking privatization of public-sector enterprises, and anti-corruption measures.

Case Studies in the Need for Reform

Mexico showcases numerous examples of the negative economic effects of monopolies and duopolies. It is virtually impossible for a company to break into certain markets—beer, cement, textiles, or bread among them. According to the Economist Intelligence Unit:

> [The Mexican government owns] oil and other hydrocarbons; basic petrochemicals; electricity; radioactive materials; and nuclear energy. Other state-run sectors include the following: airports, seaports and heliports; postal service; telegraph; radiotelegraphy; minting and issuing of paper money; and certain mining areas. The government also manages Mexico's development and trade banks, including the North American Development Bank, created alongside the North American Free-Trade Agreement (NAFTA) to provide financing to environmental-infrastructure projects along the U.S.–Mexico border.[29]

The Mexican Congress awarded no-cost broadcasting frequency spectrum to just two politically well-connected companies: Televisa and its only rival, TV Azteca.[30] The airline industry was opened up, but only slightly. The two major national air carriers, Mexicana and Aéromexico, were privatized in the 1980s but reacquired by the Mexican government in the 1990s after they experienced financial difficulties.[31] Within the past few years, they have been sold again to private interests,[32] but they continue to operate as a duopoly and exert their market power to block the entry of any significant competition.[33]

Further evidence of the need for extensive reform is provided by three major industries—oil, telecommunications, and electricity—that are sorely in need of competition.

28. *Ibid.*

29. Economist Intelligence Unit, "Mexico," *Country Commerce Report*, August 2007, at *http://www.eiu.com/report_dl.asp?issue_id=1202513305&mode=pdf* (May 7, 2008; login required).

30. Luis Clemens, "Televisa, Azteca Duopoly Tested: Mexican Supreme Court Ruling Reverses Sweetheart Law," Multichannel News, July 16, 2007, at *http://www.multichannel.com/article/CA6460188.html* (February 20, 2008).

31. Organisation for Economic Co-operation and Development, OECD Global Forum on Competition, "Contribution from Mexico: Merger Enforcement in Mexico (Session V)," CCNM/GF/COMP/WD(2001)18, October 9, 2001, p. 6, at *http://www.oecd.org/dataoecd/40/63/2491654.pdf* (April 29, 2008).

32. Dialog NewsEdge, "Mexico Travel: Banamex Investor Group Wins Bidding War for Aeromexico," October 19, 2007, p. 8, at *http://www.eiu.com/index.asp?layout=iwArticleVW3&article_id=472686232&refm=&country_id=1520000152&industry_id=320000032&channel_id=&category_id=&page_title=Latest+analysis&rf=0* (April 29, 2008; login required).

33. Organisation for Economic Co-operation and Development, OECD Global Forum on Competition, "Merger Enforcement in Mexico."

Pemex: Mexico's Tarnished Crown Jewel. In analyzing where reforms are needed most, a natural starting point is Mexico's oil sector, which accounts for a substantial portion—9 percent in 2006—of the country's gross domestic product. State-owned Petroleos Mexicanos (Pemex) has a monopoly on all upstream and downstream exploitation of Mexico's rich oil and natural gas resources, although the Mexican constitution specifically reserves only "ownership of…petroleum and other hydrocarbons" for the state.[34] According to several business scholars, it does not mandate the state monopoly of oil production and retail.[35]

The oil and gas sector has been extremely sensitive politically at least since the 1930s and the *sexenio* of the revered Lazaro Cárdenas. Control of the oil industry strikes at the very heart of the average Mexican's sense of sovereignty, national self-image, and independence from the U.S. (which invaded Mexico several times in the 19th and early 20th centuries).

In 1938, President Cárdenas created Pemex by nationalizing the holdings of U.S. and Anglo–Dutch companies that had largely developed Mexico's oil industry.[36] In his seminal book on the world petroleum industry, *The Prize*, Daniel Yergin writes that "petroleum nationalization [was the] great symbolic and passionate act of resistance to foreign control, which would become central to the spirit of nationalism that tied [Mexico] together."[37]

Rather than working for the Mexican people, however, Pemex seems to exist primarily to generate revenue for the government treasury and for its own union. With almost 140,000 workers, Pemex is wildly overmanned. Its pre-tax earnings in 2007 were around $50 billion, but it invested only $13 billion in development of new oil fields. As a result, oil production is already falling and will continue to decline rapidly unless new deep-water discoveries of proven oil reserves are made in the Gulf of Mexico or Mexico's Pacific waters.[38] Pemex replaces only a fifth of the reserves it depletes, and Mexico already imports 30 percent of the petroleum and 23 percent of the natural gas that it consumes.[39] According to *BusinessWeek*:

> Mexico's largest potential reserves are believed to be located in the deep waters of the Gulf of Mexico, as much as 10,000 feet below the surface. Pemex does not have the technology or the expertise to go after that deepwater oil. Over the past five years, it has drilled six test wells in waters about 3,000 feet deep, finding some gas, but it needs the help of international oil companies, such as Brazil's Petrobras (PBR) or Norway's StatoilHydro (STO), to mount a concerted deepwater campaign.[40]

Although the Pemex monopoly ensured national sovereignty, it came at a high price, feeding an unfortunate pattern of widespread and heavy-handed government involvement in the economy, as well as generating substantial graft and corruption. Former Federal Reserve Chairman Alan Greenspan characterizes Cárdenas's behavior as defiantly anti-American and observes that "[h]is action had dire long-term consequences for Mexico."[41]

34. U.S. Department of State, Bureau of Economic, Energy and Business Affairs, "2006 Investment Country Climate Statement—Mexico"; International Monetary Fund, *Mexico: 2007 Article IV Consultation—Staff Report; Staff Supplement; and Public Information Notice on the Executive Board Discussion for Mexico*, Country Report No. 07/379, December 2007, at *http://www.internationalmonetaryfund.org/external/pubs/ft/scr/2007/cr07379.pdf* (April 24, 2008).

35. "Tax Reform: Mexico Marks the Path," *Latin Business Chronicle*, October 22, 2007, at *http://www.latinbusinesschronicle.com/app/article.aspx?id=1687* (February 12, 2008).

36. RedScholar (Scholar's Network), "Historia de la decisión de expropiar las compañías petroleras extranjeras en México [History of the Decision to Nationalize Foreign Oil Companies in Mexico]," Instituto Latinoamericano de la Comunicación Educativa, at *http://redescolar.ilce.edu.mx/redescolar/act_permanentes/historia/html/expropiacion/oposicion.htm* (May 8, 2008).

37. Daniel Yergin, *The Prize: The Epic Quest for Oil, Money and Power* (New York: Free Press, 1991), p. 244.

38. "Monopoly Money," *The Economist*, November 18, 2006.

39. *Ibid.*

40. Geri Smith, "Mexico's Oil Dilemma," *BusinessWeek*, April 28, 2008, at *http://www.businessweek.com/bwdaily/dnflash/content/apr2008/db20080427_752673.htm?chan=top+news_top+news+index_businessweek+exclusives* (April 29, 2008).

The Mexican Congress has taken some timid steps to increase private investment in the energy sector, but not nearly enough market incentives have been put into place to spur necessary competition in such a vital sector of the economy.[42] This has led to a Pemex that is "inefficient, undercapitalized and utilized as a golden goose by the government," whose "existence exacerbates corruption."[43] In the 2000 election, according to some observers, Pemex funds wound up in the coffers of many PRI candidates.[44] By 2000, the PRI had exercised a political monopoly in Mexico for 70 straight years, since the time of President Cárdenas. The PRI power base rested (and continues to rest) heavily on Pemex and the Pemex workers' union. An almost identical and equally negative phenomenon can be observed today in the Venezuela of Hugo Chavez.

"Pemex resembles a poorly run government ministry," according to *The Economist*. "Its past three chief executives have all been accused of corruption," and the company "must comply with onerous procurement rules meant to prevent graft, which in practice are merely a drag on getting things done" (and clearly have not achieved their objective of eliminating corruption within Pemex).[45] According to Joel Kurtzman, Pemex is also "the world's most heavily indebted oil company," "one of the [world's] least efficient producers," and "so bogged down by bureaucracy, conflicting interests, political meddling and sweetheart union deals, that it has failed to find any new oil reserves in years."[46]

Professor Rafael Pampillón of the Instituto de Empresa graduate business school in Spain has noted that:

> [A]ll the gas stations [in Mexico] are PEMEX. It is a good idea to provide PEMEX with higher tax revenues but it is much more important to improve competitiveness in the [energy] sector by permitting the arrival of companies from other countries—and even by privatizing PEMEX, although the current practice [of state control of PEMEX] is deeply rooted in Mexican tradition.[47]

Pampillón argues that more competition in the Mexican energy sector would benefit the entire country.[48]

The PRI members of the Mexican Congress are fiercely resisting even the minor Pemex reforms that President Calderón is proposing. The reason, as noted by *The Wall Street Journal*'s Mary Anastasia O'Grady:

> [T]he guardians of the status quo—politicians, suppliers and labor—would suffer if competition hit the market. Private Mexican contractors who "supply" Pemex are [accustomed]…to business transactions tied to political connections. If there were multiple buyers in competition with one another, those political profit margins would evaporate.[49]

That benefit will be realized if President Calderón overcomes PRI resistance and speeds up efforts at reform of Mexico's energy sector to help it catch up with the majority of other producer countries. Although some "important changes have been introduced to attract private investment in natural gas transportation and distribution":

41. Alan Greenspan, *The Age of Turbulence* (New York: Penguin Press, 2007), p. 336.
42. Sandra Dibble, "Fox Predicts Mexico's Successes Could Eliminate Illegal Crossings," Copley News Service, June 10, 2006.
43. Allan Wall, "Whither PEMEX?" *Human Events*, May 19, 2004, at *http://www.humanevents.com/article.php?id=3942* (November 26, 2007).
44. *Ibid.*
45. "Running Just to Stand Still," *The Economist*, December 19, 2007, at *http://www.economist.com/world/la/PrinterFriendly.cfm?story_id=10328190* (February 12, 2008).
46. Kurtzman, "Mexico's Job-Creation Problem."
47. "Tax Reform: Mexico Marks the Path."
48. *Ibid.*
49. Mary Anastasia O'Grady, "Playing Monopoly in Mexico," *The Wall Street Journal*, April 7, 2008, p. A12, at *http://online.wsj.com/article/SB120753042640093867.html* (April 30, 2008).

> [The most important] issue in the immediate term will be the evolution of competition in the market. Hence, one of the first issues to be tackled to enhance the role of market forces in the sector is Pemex' discretionary discounts on domestic gas and access to transport services made possible by its monopoly in domestic production and its overwhelming dominance in [pipeline] transport.[50]

Telmex: Toothless Regulation That Fleeces Mexican and U.S. Consumers. The telecommunications sector presents what is probably the best case study of the distorting impact of monopolies on the Mexican economy, in this case the *de facto* monopoly controlled by Grupo Carso, the privately held firm owned by Mexican billionaire Carlos Slim and his family. Through his ownership of the former state-owned monopoly Teléfonos de México (Telmex), which had been Mexico's "Ma Bell," Slim owns more than 90 percent of Mexico's fixed telephone landlines,[51] and "[h]is America Movil's Telcel unit has 77 percent of wireless subscribers in the country."[52]

Compare that to the United States, where four well-regulated national cell phone carriers compete ferociously and drive down prices paid by consumers. Telmex and Telcel dominate the telecom industry and wield "significant influence over key regulatory and government decision makers."[53] Telmex has often been accused of finding innovative ways to block the entry of competitors. As Mary Anastasia O'Grady has noted in *The Wall Street Journal*, "Mr. Slim's company has been masterful in protecting its turf. One example is its success in using endless litigation to fend off regulatory orders that it provide interconnections to other carriers at fair rates, as required by law."[54]

"Mexico lacks a competition culture," according to the Paris-based Organisation for Economic Co-operation and Development (OECD).[55] "The Federal Competition Commission is fairly toothless," says *The Economist*, "though a new law is supposed to give it more bite. Some analysts are hoping that technological innovation will undermine Telmex's monopoly. But it is seeking to expand into new businesses, such as cable television."[56]

In 1999, the U.S. Federal Communications Commission accused Telmex (and then-partner Sprint) of "anticompetitive practices in the long-distance market" by overcharging Mexicans in the U.S. when they called home to Mexico. "U.S. consumers have to pay much more than they should to reach friends and relatives in Mexico," said then-FCC Chairman William E. Kennard. "The carriers have not moved quickly enough to bring these rates down and ensure meaningful competition."[57] The U.S. government complained about the Telmex

50. Juan Rosellon, Centro de Investigaçion y Docencia Economica, Mexico City, Mexico, and Jonathan Halpern, Latin America and the Caribbean Region, Finance Private Sector and Infrastructure Sector Unit, World Bank, "Regulatory Reform in Mexico's Natural Gas Industry—Liberalization in the Context of a Dominant Upstream Incumbent," World Bank, Policy Research *Working Paper* No. WPS2537, January 31, 2001.

51. U.S. Department of State, Bureau of Economic, Energy and Business Affairs, "2007 Investment Climate Statement—Mexico," at *http://www.state.gov/e/eeb/ifd/2007/80727.htm* (February 12, 2008).

52. Adriana Arai, "Mexico to Begin Antitrust Probe of Slim's Companies," Bloomberg.com, October 29, 2007, at *http://www.bloomberg.com/apps/news?pid=20601086&sid=arnLKCV8kY8U&refer=news* (May 7, 2008).

53. U.S. Department of Commerce, "Doing Business in Mexico: A Country Commercial Guide for U.S. Companies," September 12, 2006, at *http://www.buyusa.gov/pittsburgh/mexicocommercial.pdf* (April 24, 2008).

54. Mary Anastasia O'Grady, "A Telecom Monopoly Cripples Mexico," *The Wall Street Journal*, February 10, 2006, at *http://online.wsj.com/article/SB113954042025370380.html?mod=opinion_main_featured_stories_hs* (May 10, 2008). See also Geri Smith, "Is the Game Over for Mexico's Monopolies?" *BusinessWeek*, October 6, 2006, at *http://www.businessweek.com/globalbiz/content/oct2006/gb20061006_567056.htm* (May 7, 2008).

55. OECD Global Forum on Competition, "Challenges/Obstacles Faced by Competition Authorities in Achieving Greater Economic Development Through the Promotion of Competition," January 22, 2004, at *http://www.oecd.org/dataoecd/23/11/25500492.pdf*.

56. "Monopoly Money," *The Economist*, November 18, 2006.

practices to the World Trade Organization, which ruled against Telmex in 2002.[58]

Critics complain that Slim's competitors have been "victimized" by his cynical "manipulation of Mexico's weak regulatory agencies and arcane laws," especially his notorious abuse of the *amparo*, or injunction, which allows any citizen who feels that a government decision violates his constitutional rights to ask a judge to delay its implementation—often for years.

> Since 1998, Slim has made use of more than 60 amparos to thwart decisions by Mexico's antitrust agency, the Comisión Federal de Competencia, ordering Telmex to reduce its interconnection rates—the fees rivals must pay to use Telmex trunk lines. "Telmex's very aggressive use of the amparo has ended any hope of an open telecommunications market in Mexico," says Karina Duyich, [former head of] AT&T Mexico's legal department.[59]

Carlos Slim: Mexico's Fattest Cat. Perhaps the wealthiest person on the planet,[60] Mexican telecommunications mogul Carlos Slim has been chastised for his lack of charity. Slim, whose father immigrated to Mexico from Lebanon, controls companies that account for one-third of the investment value of the $400 billion Mexican Bolsa (stock exchange).[61]

Slim, 68, amassed his nearly $60 billion fortune[62] in a nation where per capita income is less than $6,800 a year and half the population lives in poverty. His wealth amounts to 6.3 percent of Mexico's annual economic output: If Bill Gates owned a similar chunk of the U.S., he would be worth $784 billion. According to one account:

> [I]t takes about nine of the captains of industry and finance of the 19th century and early 20th centuries—Rockefeller, Cornelius Vanderbilt, John J. Astor, Andrew Carnegie, Alexander Stewart, Frederick Weyerhaeuser, Jay Gould and Marshall Field—to replicate the footprint that Mr. Slim has left on Mexico.[63]

As another observer has written, that's "enough to give any populist heartburn."[64]

The cash from Telmex has financed relentless diversification. Slim's America Movil is the largest mobile-phone operator in Latin America. His family also holds a string of industrial and retailing businesses, including the Mexican operations of Sears. He is the biggest tenant in the country's shopping centers. His latest venture is Ideal, an infrastructure company working mainly in the oil industry. He is also the second-largest shareholder in Televisa, Mexico's television giant.[65] In addition to landlines and cellular, Telmex also enjoys an important share of the broadband Internet market and is trying to become a dominant force in Mexico's pay-TV market.[66] Telmex also has huge business holdings in the U.S. as well as in other South American countries.[67]

57. Stephen Labaton, "Int'l Business: F.C.C. Says Sprint and Telmex Overcharged on Some Rates," *The New York Times*, November 25, 1998, at *http://query.nytimes.com/gst/fullpage.html?res=9D01E0D61639F936A15752C1A96E958260* (April 29, 2008).
58. U.N. Conference on Trade and Development, "Ways in Which Possible International Agreements on Competition Might Apply to Developing Countries," May 7, 2007, pp. 13–14, at *http://www.unctad.org/en/docs/c2clp46rev3_en.pdf* (May 7, 2008).
59. "Slim City," *Institutional Investor*, June 1, 2003.
60. Helen Coster, "Carlos Slim Helu Now World's Second Richest Man," *Forbes*, April 11, 2007, at *http://www.forbes.com/business/2007/04/11/billionaires-helu-telecom-biz-cz_hc_0411helu.html* (December 9, 2007).
61. Stephanie N. Mehta, "Carlos Slim, the Richest Man in the World," *Fortune*, August 20, 2007, at *http://money.cnn.com/2007/08/03/news/international/carlosslim.fortune/index.htm* (February 12, 2008).
62. Christine Seib, "Gates Loses Richest Ranking to Mexican Tycoon," *The Times*, July 4, 2007, at *http://business.timesonline.co.uk/tol/business/industry_sectors/telecoms/article2023023.ece* (February 13, 2008).
63. Eduardo Porter, "Mexico's Plutocracy Thrives on Robber-Baron Concessions," *The New York Times*, August 27, 2007, at *http://www.nytimes.com/2007/08/27/opinion/27mon4.html* (April 24, 2008).
64. Helen Coster, "Slim's Chance," *Forbes*, March 26, 2007, at *http://members.forbes.com/forbes/2007/0326/134.html* (February 13, 2008).
65. "Monopoly Money," *The Economist,* November 18, 2006.
66. "Televisa: The Plot Thickens," *The Economist*, July 20, 1996.

Professor George W. Grayson, an expert on Mexico at the College of William and Mary, coined the term "Slimlandia" to describe how entrenched the Slim family's companies are in the daily lives of Mexicans. It is not a reverential term. Many Mexicans hoped that privatization, which began in the early 1990s, would create competition and drive prices down drastically, but that has not happened. "Slim is one of a dozen fat cats in Mexico who impede that country's growth because they run monopolies or oligopolies," says Grayson. "The Mexican economy is highly inefficient, and it is losing its competitive standing vis-à-vis other countries because of people like Slim."[68]

Telmex Privatization: A Sweetheart Deal. As a recent report by the OECD Economics Department notes, "Mexico remains one of the OECD countries with the highest charges, especially for business use. In the mobile telephone market, in particular, the dominant firm [Telmex] is using its market power to squeeze out other players."[69] Clearly, the many customers who are being held hostage to both Telmex and Telcel are not getting their money's worth for the high prices they pay. The government of then-President Carlos Salinas de Gortari did very little to reform or modernize Telmex when it was privatized in 1990 during the Mexican government's preparations for entry into NAFTA. The Salinas administration simply issued regulations that protected the Telmex long-distance service monopoly until August 1996.[70]

In participation with minority partners France Telecom and Southwestern Bell (now AT&T), Slim acquired a 51 percent voting interest in Telmex, representing over 20 percent of the equity in the company.[71] Although he denies accusations that Salinas gave him special treatment, Slim was able to buy Telmex from the government for just $1.7 billion.[72]

Rumors about the details of the Telmex purchase have swirled ever since then. Slim was a member of Salinas's inner circle and attended a legendary 1993 dinner at which Salinas purportedly asked each guest to contribute $25 million to his PRI party's war chest in return for favorable treatment during the coming wave of privatizations. "Although no evidence has emerged, many Mexicans suspect that Mr. Salinas secretly profited from the sale of Telmex."[73]

Telmex service was terrible in 1995 when Slim took over.[74] Although service improved after he "plowed more than $16 billion into the carrier to upgrade infrastructure and improve customer service,"[75] Carlos Slim continues to abuse his monopoly position, overcharging both Mexicans at home and those in the U.S. trying to call home.

Poor Telmex service is one of the leading complaints received by Profeco, Mexico's Federal Con-

67. Helen Coster, "Mexican Billionaire Expands Telecom Holdings," *Forbes*, April 3, 2006, at *http://www.forbes.com/2006/04/03/slim-telmex-verizon-cz_hc_0403autofacescan10.html* (February 13, 2008).
68. Mehta, "Carlos Slim, the Richest Man in the World."
69. Organisation for Economic Co-operation and Development, Economics Department, "Economic Survey of Mexico 2007: Improving Infrastructure in Mexico," summary of Chapter 4 in *Economic Survey of Mexico 2007*, October 4, 2007, at *http://www.oecd.org/document/8/0,3343,en_2649_34833_39415560_1_1_1_1,00.html*.
70. Kathleen A. Griffith, "Telecommunications in Mexico," Columbia University, Columbia Institute for Tele-Information *Working Paper* No. 631, 1996, at *http://www.vii.org/papers/mexi.htm* (February 19, 2008), and at *http://www.citi.columbia.edu/wkpa.htm* (April 29, 2008).
71. "An Interview with Mexico's Carlos Slim: The Richest Man You've Never Heard Of," *The Arizona Republic*, May 30, 2007, p. 1.
72. Adam Thomson, "Mexican Monopolist's Fortune Leads the World," *Financial Times*, July 7, 2007, at *http://www.ft.com/cms/s/2/a880023c-2bdf-11dc-b498-000b5df10621.html* (February 12, 2008).
73. Julia Preston, "Mexico's Telephone Revolution," *The New York Times*, November 14, 1996, at *http://query.nytimes.com/gst/fullpage.html?res=9E00E7DD1F3BF937A25752C1A960958260&sec=&spon=&pagewanted=2* (February 12, 2008).
74. Kerry A. Dolan, "Rooting for the Home Team," *Forbes*, September 11, 1995, p. 121.
75. Geri Smith and Stephanie Anderson Forest, "Slim's New World (Int'l Edition): Mexico's Richest Man Is Betting Big on U.S. Computer Retailing," *BusinessWeek,* February 21, 2000, at *http://www.businessweek.com/2000/00_08/b3669020.htm* (May 7, 2008).

sumer Protection Agency.[76] Under pressure in part from increased competition from such long-distance Internet phone service providers as Skype and Vonage, Telmex has publicized the fact that it has not raised rates for basic landline service for eight years, which has hurt profit margins but blunts political efforts to break up the company.[77] Meanwhile, Skype and Vonage have alleged that Telmex has attempted to block their service to Mexico.[78]

Teledensity (the number of landlines per capita, close to 100 percent in the U.S.) in Mexico, at 19 percent, is among the lowest in Latin America[79] because of the artificially high prices that Telmex charges and the lack of competition. This low level of interconnectedness is another major factor holding back Mexico's development.

Telmex owns and operates international businesses including fixed-line and wireless operators, television cable companies, and Internet service providers in Brazil, Argentina, Chile, Colombia, Ecuador, and Peru. These businesses account for about 30 percent of Telmex's total revenue.[80] In 1995, government regulators allowed Telmex to buy a 49 percent stake in Cablevision, the cable-television division of Mexico's media powerhouse, Televisa.[81] Telmex has been criticized by competitors and legislators for using its influence to head off stronger regulation. Analysts say the problem is Mexico's weak regulatory framework.[82]

Reforms to curtail Telmex's monopoly power during the Ernesto Zedillo and Vicente Fox administrations (1994 to 2006) yielded modest reforms at best. As recently as October 2007, an OECD report concluded that Mexico must do more to increase competition in its energy and telecommunications industries. Additionally, "OECD noted that telephone costs in Mexico are among the highest among OECD member countries in terms of purchasing power parity."[83] Clearly, Mexicans would be well served by increased consumer choice and a more robust and transparent telecommunications sector.

In October 2007, Mexico's Federal Competition Commission (CFC) began an investigation of Carlos Slim for alleged monopoly practices,[84] trying "to determine whether the two companies, owned by Slim, America Movil and Telmex have a monopoly on the Mexican market."[85]

Splitting up Telmex Would Create Jobs. Breaking Telmex's vise-like grip on Mexico's telecommunications sector would create new, sustainable, well-paying jobs for Mexicans in Mexico. A

76. See Government of Mexico, Federal Consumer Protection Agency (Profeco), Web site, at *http://www.profeco.gob.mx/* (February 8, 2008). See also John Edwards, "Mexico: Slim's Tight Grip," *Global Technology Forum*, April 10, 2007, at *http://globaltechforum.eiu.com/index.asp?layout=rich_story&doc_id=10469&title=Mexico%3A+Slim's+tight+grip&categoryid=28&channelid=4* (May 7, 2008).
77. Reuters, "Update 2—Mexico's Telmex Freezes Rates for 8th Year," January 4, 2008, p. 1, at *http://www.reuters.com/article/technology-media-telco-SP/idUSN0962182320080109* (February 12, 2008).
78. Jonathan Clark, "Users Decry Decline in Service," *El Universal*, May 8, 2005, at *http://www2.eluniversal.com.mx/pls/impreso/noticia.html?id_nota=10420&tabla=miami* (May 7, 2008).
79. U.S. Department of State, Bureau of Western Hemisphere Affairs, "Background Note—Mexico," April 2008, at *http://www.state.gov/r/pa/ei/bgn/35749.htm* (April 24, 2008).
80. *Ibid.*, p. 2.
81. Anthony DePalma, "Telmex Gains in Attempt to Buy Cable-System Stake," *The New York Times*, June 22, 1995, at *http://query.nytimes.com/gst/fullpage.html?res=990CE3DD113CF931A15755C0A963958260&scp=1&sq=Telmex+Gains+in+Attempt+to+Buy+Cable-System+Stake&st=nyt*(April 29, 2008).
82. Elisabeth Malkin, "Reins Are Passed, Somewhat, at Mexican Empire," *The New York Times*, May 4, 2004, at *http://query.nytimes.com/gst/fullpage.html?res=9C03E7DF103DF937A35756C0A9629C8B63* (February 12, 2008).
83. Patrick Harrington and Thomas Black, "Mexico Must Boost Competition in Telecom, OECD Says," Bloomberg.com, October 4, 2007, at *http://www.bloomberg.com/apps/news?pid=20601086&sid=aL42ZcfFQd5g&refer=latin_america* (May 7, 2007).
84. Arai, "Mexico to Begin Antitrust Probe of Slim's Companies."
85. "Mexican Competition Watchdog to Start Monopoly Investigation Against Carlos Slim," *Latin America News Digest*, October 30, 2007.

recent paper by two prominent World Bank scholars, Isabel Guerrero and Luis Felipe Lopez-Calva, underscores this point:

> Many studies confirm that lack of competition is a crucial problem holding back the possibility of strong growth in Mexico. The Mexican Competitiveness Institute (IMCO) developed a model to assess the main factors behind the low and failing competitiveness [in] Mexico. Drawing on cross-country information, they estimated point elasticities for the impact of investment per worker of a ten percent [*sic*] in different dependent variables. The top four interventions which would bring about an improvement in competitiveness in Mexico are: (i) improvements in the competition environment; (ii) changes in taxes and tax regulations; (iii) improvements in administrative regulations and the investment climate; and (iv) education.[86]

An Inefficient, State-Owned Electricity Monopoly. Mexico's national sovereignty sensitivities historically have extended beyond the oil patch to embrace the entire energy sector, which Mexicans have considered strategic. During the nationalistic "import substitution" craze that swept through Latin America in the 1960s, the Mexican government chose to nationalize the country's electricity production and distribution companies, imposing limitations on private participation and foreign companies' ability to operate. They are permitted to do so only through specific service contracts with the Federal Electricity Commission (CFE) and Luz y Fuerza del Centro (LFC).

The electricity sector is federally owned, with the CFE having exclusive rights to provide electric services throughout Mexico. The CFE is one of Mexico's largest companies. According to the Economist Intelligence Unit:

> [Its monopoly status is] embedded in the Mexican constitution and is defined by its Electricity Law. CFE is vertically integrated and provides generation, transmission and distribution services for all of Mexico with the exception of electric distribution in the Mexico City metropolitan area. Luz y Fuerza del Centro (LFC), another wholly owned decentralized agency of the Mexican government, is responsible for the distribution of electricity in Mexico City and purchases some of its power from CFE.[87]

Past attempts at reform have been met with strong political and social resistance in Mexico, where electricity subsidies for residential consumers absorb substantial fiscal resources. Meanwhile, Mexico's power generation sector is failing to install sufficient additional power generation to meet future needs. Historically, political constraints have meant that any funding to increase generating ability had to come from the already overextended federal budget. Nevertheless, a recent report by the Mexican energy ministry shows that between 2009 and 2014, a substantial amount of new generating capacity will have to come from private investment in order to meet demand.[88]

A good illustration of Mexico's highly politicized energy regulatory environment occurred in 2004 when leftists in Congress, who oppose even the slightest degree of energy privatization, filed a complaint with the Auditoría Superior de la Federaçion (ASF), asking it to review the legality of those few generation permits that had been granted by the Comisión Reguladora de Energá (CRE) to private parties. The ASF found that the generation permits granted by the CRE were illegal and contrary to the constitution. The energy ministry filed a constitutional challenge before the supreme court alleging that the ASF does not have authority to decide on

86. Isabel Guerrero, World Bank; Luis Felipe López-Calva, UNDP Mexico and Stanford Center for International Development, Stanford University; and Michael Walton, Kennedy School of Government, Harvard University, "The Inequality Trap and Its Links to Low Growth in Mexico," Working Paper, November 7, 2006, p. 37, at *http://iepecdg.com/DISK%201/Arquivos/Leiturassugeridas/walton-ingles-24-11-17122006.pdf* (April 24, 2008).

87. Economist Intelligence Unit, "Mexico Risk: Infrastructure Risk," *Country Briefing*, November 15, 2007.

88. Government of Mexico, Secretary of Energy, "Prospectiva del sector eléctrico 2005–2014," 2006, at *http://www.energia.gob.mx/webSener/res/PE_y_DT/pub/Electrico_2005_2014.pdf* (February 12, 2008).

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the legality of the generation permits granted to private parties by the CRE, and the supreme court agreed to hear the case, thereby tying up the permits for lengthy periods of litigation.[89]

President Zedillo, a Yale-trained economist, proposed a complex set of reforms in 1999 that would have led to the sale of the CFE and LFC, but the Congress killed the reforms.[90] "An electricity reform package that would have strengthened the legal framework and facilitate growth in private investment was proposed by the Fox administration," according to the Economist Intelligence Unit, "but was blocked. The Calderón administration hopes to push a similar project through [in 2008]."[91]

Increasing private participation in the electricity sector would also help Mexico to do a better job of controlling air pollution, for which Mexico City is justly infamous. According to a study by the International Energy Agency, Mexico is one of the 10 worst polluters among developing countries.[92] Generally, only countries with a high degree of economic freedom and market-based democracy have the means to spend the large sums required to clean the air.

Other Obstacles to Reform

Mexico's Plutocracy. For any of its reform measures to succeed, the Mexican government must dismantle the country's corporatist system of price supports, subsidies, and special-interest tax exemptions. This system has evolved over many years in an incestuous atmosphere of collusion among senior government, labor, and business elites.

Among the primary systemic failures of Mexico's current political arrangement is the control that key economic actors in the private sector exercise over the country's legislative and executive bodies. In effect, Mexico is governed by a permanent and unelected plutocracy. The wealth of the country is concentrated in the hands of too few individuals.[93]

Failure to Protect Intellectual Property Rights. If the monopolies can be reined in, not only will domestic competitors benefit, but so will foreign competitors. There is another problem, however, that is impeding foreign investors.

In order for Mexico to attract additional foreign direct investment (most notably in telecommunications and energy), it must strengthen enforcement mechanisms to protect intellectual property rights. By placing Mexico on its Special 301 Watch List in 2007 for the third year in a row, the Office of the United States Trade Representative (USTR) rebuked the Mexican government for its weak enforcement of intellectual property rights.[94]

Inadequate Highways and Other Infrastructure Problems. As noted by the OECD, the competitiveness of Mexican firms is being hampered by the poor quality and high cost of transportation, which are also disincentives to foreign investment and to Mexico's productivity growth:

> The road network and trucking are plagued by inefficiencies and there are border issues that need to be addressed. The government is committed to further developing road infrastructure through public-private partnerships and concessions for toll roads. Clar-

89. Haynes and Boone, LLP, "Mexico's Power Generation Sector: Constitutional Challenge Against Permits Granted to Private Parties," HG.org, August 16, 2004, at *http://www.hg.org/articles/article_411.html* (February 12, 2008).
90. Elisabeth Malkin, "Mexico's Fox Proposes Opening Power Sector," *The New York Times*, August 19, 2002, at *http://query.nytimes.com/gst/fullpage.html?res=9502EFD6133DF93AA2575BC0A9649C8B63&sec* (February 12, 2008).
91. Economist Intelligence Unit, "Mexico: Energy Provision," *Country Background*, August 20, 2007.
92. Jake Schmidt, Ned Helme, and Pedro Barata, "Sector-Based Approach for 'Post-2012': Electricity Sector and Major Industries," Center for Clean Air Policy, Powerpoint lecture from IEA-ENEL Workshop: Sectoral Approaches for Greenhouse Gas Mitigation in the Power Sector, October 30, 2006, at *http://www.iea.org/Textbase/work/2006/enel/Session%204/Barata%20Session%204.pdf* (February 13, 2008).
93. Eduardo Porter, "Mexico's Plutocracy Thrives on Robber-Baron Concessions," *The New York Times*, August 27, 2007, at *http://www.nytimes.com/2007/08/27/opinion/27mon4.html* (December 9, 2007).
94. Office of the U.S. Trade Representative, *Special 301 Report*, April 30, 2007, at *http://www.ustr.gov/Document_Library/Press_Releases/2007/April/SPECIAL_301_Report.html* (December 10, 2007).

ifying long term government plans would help private sector involvement.[95]

Additional detail is provided by the Economist Intelligence Unit:

> Mexico's road network stood at 355,796 km in 2005, including 122,677 km of paved roads and 14,874 km of major road systems. Poor coordination at the state and federal level has resulted in poor planning of the road network [in the 1990s] and in maintenance problems. Mexico's roads and highways are still inadequate in the more remote parts of the country…. It continues to prove difficult to attract private capital to road building, maintenance and operation; in addition, government auctions for road concessions are complicated.[96]

Subsidies. Although President Calderón is trying to reform the energy sector, these reforms are doomed to fail unless he is able first to address the excessive government subsidies for that sector. According to a 2007 study by the International Association for Energy Economics, electricity prices in Mexico are "heavily and unevenly subsidized"—the average electricity subsidy is 30 percent of non-discounted retail rates, and residential subsidies are more than 50 percent. To offset the cost of the subsidies, excessively high energy prices are charged to those businesses and consumers that do not receive subsidies, and those high rates are "hurting the competitive position of Mexican industries."[97]

These subsidies are also hurting the government's budget, frittering away resources that could be used more productively to improve infrastructure. "In 2007," reports the *Financial Times*, "the Mexican federal government…earmarked 105.6 billion pesos to subsidize power consumption, which is equal to 1.1 percent of Mexico's gross domestic product (GDP)."[98]

Mexico's Political Oligopoly. For 70 years, just one party—the PRI—had a complete lock on Mexican politics. Now three parties share the power, but no fourth party can enter the political arena or have access to the taxpayer subsidies handed out to these three (to the tune of more than half a billion dollars in 2007) without their consent.

Independent candidates are not allowed to run. The absence of consecutive re-election at any level reinforces the party machines' power: They pick candidates to run for all local and state offices who are then merely ratified by the voters at the polls. The only primaries or conventions that are held are to determine candidates at the national level.

Political Reforms Blocked. Last year, President Calderón won approval from Congress for a package of fiscal reform measures intended to increase non-oil tax revenue by 2 percent of Mexico's GDP. Its approval gives the president political momentum as he seeks the energy reform that is next on his agenda in 2008. But this victory came at a price: The president was forced "to acquiesce in an opposition-inspired constitutional amendment on electoral reform" that is "the legacy of last year's bitter presidential election, in which Mr. Calderón narrowly defeated Andrés Manuel López Obrador of the center-left Party of the Democratic Revolution (PRD)."[99]

Does Mexico Need a Teddy Roosevelt?

In the late 19th and early 20th centuries, the United States faced similar challenges. President Theodore Roosevelt pressured Congress to implement existing anti-trust legislation (e.g., the Sherman Anti-Trust Act of 1890) and to pass additional measures, such as the law that created the Interstate

95. Organisation for Economic Co-operation and Development, Economics Department, "Economic Survey of Mexico 2007: Improving Infrastructure in Mexico."
96. Economist Intelligence Unit, "Mexico Risk: Infrastructure Risk," *Country Briefing*, November 15, 2007.
97. Bruce T. Laxdal, "Structural Issues to Resolve in Mexico in Support of Electric Industry Reform," from panel on "Energy, Environment and Economics in a New Era" at 24th International Association for Energy Economics North American Conference, Washington, D.C., July 8–10, 2004, at *http://www.iaee.org/documents/washington/Structural_Issues.pdf* (April 22, 2008).
98. "1 Pct of Mexico GDP Earmarked for Power Subsidies," *The Financial Times*, December 7, 2006.
99. "Reforms at Last," *The Economist*, September 20, 2007.

Commerce Commission. By doing so, Roosevelt led the U.S. government to stand courageously against powerful banking, oil, and steel magnates of the day and enforce regulations and laws to curb the power of monopolies to choke off competition and hamper free-market operations.

Although President Roosevelt's name is most often associated with trust-busting in the U.S., his successor, William Howard Taft, broke up twice as many trusts during his tenure. Rather than encouraging unnecessary and burdensome regulations, Roosevelt and Taft used governmental powers in the manner envisioned by the Founders to create a space where competition could provide American consumers with the best goods and services at the lowest price.

The head of Mexico's Federal Competition Commission, Eduardo Perez Motta, recently announced that his agency (the equivalent of the Anti-Trust Division in the U.S. Department of Justice) will reopen an investigation of Carlos Slim's telephone companies, Telefonos de Mexico and America Movil. Slim's empire today is far greater than even John D. Rockefeller's at the time of his death in 1937.[100] If President Calderón can be Mexico's Teddy Roosevelt, perhaps Mr. Perez Motta can become Mexico's President Taft.

Calderón himself is on record as supporting the changes that he knows are needed: "As the head of Mexico's energy sector [2003–2006], he promoted the modernization of state-owned companies as president of the Board of Directors of PEMEX, the Federal Commission of Electricity (CFE) and the electricity company Luz y Fuerza del Centro (LyFC)."[101]

A Transformed Mexico Would Help Everyone

The prosperity and national security of the United States have already been enhanced by the progress made by Mexico since it joined NAFTA in 1994. For further progress, however, the barriers to entry into the marketplace of political ideas also have to come down.

What is required is a careful examination of the vast areas of Mexico's economy that are state-owned or where private monopolies and duopolies are permitted by the state to operate without competition. Attention must also be given to labor laws that hobble the indigenous workforce and force millions into the informal economy, as well as to the political straightjacket that has bound Mexico's leadership. These reforms will require a level of political will by all Mexican politicians that is strong enough to break these shackles and create an atmosphere that fosters greater economic opportunity.

This would, of course, be a daunting task at every level, perhaps even a dangerous one. But it is not impossible. The result would be a transformed Mexico—a Mexico that has never before existed, that attracts workers with its economic opportunities rather than repelling them. The pressure on the U.S. border would ease considerably and might even disappear.

With strong personal leadership that inspires the Mexican population, a coalition with the political will to persist just might be forged. President Calderón, were he to succeed, would be hailed as the Teddy Roosevelt of Mexico, and Mexico and the United States would both be the better for it.

What Needs to Be Done

The Mexican government should open its nationalized oil, natural gas, and electricity sectors to private investment and participation. Pemex, for instance, should consider leasing deep-water areas under its control in the Gulf of Mexico to private oil companies to develop the fields, sell the oil produced, and pay royalties from their profits to the Mexican government. Private electricity-generating companies in Mexico and the U.S. should be encouraged to sell power to the two state-owned companies, the Federal Electricity Commission and Central Power and Light, and to invest in building additional power-generating ability in Mexico.

The Mexican government should break up private-sector monopolies and duopolies by passage,

100. Mehta, "Carlos Slim, the Richest Man in the World."

101. Government of Mexico, "President of the United States of Mexico."

implementation, and enforcement of more effective anti-trust legislation.

The Mexican government should enforce its laws more aggressively to protect all intellectual property rights, for Mexican as well as for foreign rights holders, by increasing funding and staffing of the three relevant government agencies (the Office of the Attorney General, the Mexican Institute of Industrial Property; and the National Institute of Author Rights). The government should also increase training for Mexican police and the Mexican Customs Service to spot IPR violations and take enforcement actions.

The Mexican government should eliminate the distortionary price controls and subsidies that have tilted the competitive playing field toward monopolies and duopolies in numerous sectors of the economy, especially in telecommunications, airlines, banking, broadcasting, and food production. These changes would encourage foreign direct investment in all sectors, especially energy, banking, and telecommunications, and the lower prices from increased competition would benefit Mexican consumers.

The Mexican government should implement a substantial, multi-year infrastructure improvement program with dramatically increased public and private funding of infrastructure development projects (e.g., privately owned toll roads), beginning with passage by the Mexican Congress of the ambitious infrastructure program recently proposed by President Calderón.

The Bush Administration, through the U.S. Department of Justice, should investigate the operations of Mexican monopolies in the United States, especially in the telecommunications, transportation, and energy sectors. The Justice Department should produce a report for the President that identifies those monopolies and lays out any actions that the U.S. government can take to encourage these companies to support the creation of viable domestic and foreign competitors within their economic sectors in Mexico.

The Bush Administration, through the U.S. Department of the Treasury, should commission a study by an independent private consultant to determine the level of remittances in all forms that are sent to Mexico from migrants in the U.S.

The Bush Administration should negotiate with the government of Mexico to design new co-funded assistance programs focused on intensive infrastructural, developmental, and technical assistance in those areas within Mexico that are the major sources of immigration to the United States.

The Bush Administration should negotiate with the Mexican government to design new assistance programs in conjunction with leading U.S information technology and adult-education companies with the goal of improving educational opportunities in Mexico through greater access to technology and information resources. Private U.S. companies should provide the bulk of funding for the projects in return for access to the Mexican market, to be negotiated with the Mexican government.

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