2. ECONOMIC ENVIRONMENT

With the objective of reducing the inflation rate, the Mexican authorities implemented a stabilization program, called the Economic Solidarity Pact, which features traditional austerity measures, entailing tight fiscal and monetary policies and unorthodox measures, such as price, wage and exchange rate controls. This program has been the cornerstone of Mexico's economic policy over the past three years and has resulted in a drastic reduction of the inflation rate, from an annual rate of 159% in 1987 to 52% in 1988 and 19.7% in 1989. An 18% inflation rate is expected in 1990. Along with the objective of consolidating the progress made in price stabilization, Mexico's macroeconomic policy in 1990 aims to reaffirm gradual and sustained economic recuperation, basically by establishing the necessary conditions to encourage national and foreign investment. In 1991, the Mexican authorities expect to reach an inflation rate equivalent to international levels and to relax price controls.

Mexico's gross domestic product (GDP), after increasing 3.7% and 2.7% during 1984 and 1985 respectively, diminished by 3.5% in 1986. In 1987, it increased a moderate 1.5% and an additional 1.1% in 1988. Domestic economic activity recovered for the third consecutive year in 1989 with a growth rate of 2.9% to reach $200 billion (1). With an 84.5 million population, per capita GDP is estimated at Cdn$2,550. During the 1990-1994 period GDP is expected to maintain an average annual growth rate of 2%-3%. In disagregated terms, this represents an annual growth rate of 5.3% in the manufacturing sector, 2.3% in the services sector and only 0.6% in the agricultural sector. After several years of stagnation, public investment will grow 5% and private investment will also rise 5%.

In an effort to revitalize and open the Mexican economy, the Mexican Government undertook a series of structural changes, including the accession to the General Agreement on Tariffs and Trade (GATT) on August 24, 1986 leading to an extensive trade liberalization process: import permits were eliminated on all but 325 of the total 11,950 tariff items based on the recently adopted Harmonized System. Official import prices are no longer applicable, nor the 5% export development tax, and import duties were lowered from a maximum of 100% in 1982 to 20% in January 1988. The automotive and computer industries are also being opened up, through the elimination of prior import permits, to allow free entry of products in these industries.

According to official data from the Mexican Secretariat of Commerce and Industrial Development (SECOFI), Mexico's trade balance in 1989 dropped to a $644.8 million deficit, down from a surplus of $1.75 billion in 1988 and $8.4 billion in 1987. Total exports increased 10.7% in 1989, from $20.6 billion in 1988 to $22.8 billion. Imports increased 23.9% from $18.9 billion to $23.4 billion, having already increased 48% from $12.2 billion in 1988. During 1989, imports of consumer products grew 82%, while those of intermediate goods increased by 17% and capital goods by 18%.

Total Mexican imports from Canada increased 24% in 1989 and amounted to Cdn$603 million, while total Mexican exports to Canada were valued at Cdn$1,698 million. Mexico and Canada have traditionally been strong trading partners. According to Mexican figures, in 1989, 1.9% of Mexico's imports came from Canada, while 1.2% of its

1. Note: All values in this report, unless otherwise stated (Mexican pesos, Mex$, Canadian dollars, Cdn$, etc) are quoted in United States dollar equivalents.