6

Mexico: The Laissez Faire Paragon Gone Wrong

Introduction to country analysis

The following chapters (Chapters 6, 7 and 8) explore how three different middle-income emerging economies, Mexico, Brazil and South Korea, headed towards financial crises in the 1990s. These economies are chosen as the best representatives of different economic policy designs devised to deal with the problem of the absorption of foreign inflow surges following Palma’s ‘three route approach’.

Economic and financial developments in Mexico, Brazil and South Korea

The most significant economic trends characterising the period from the late 1980s to 2000 can be summarised by decreasing interest rates in the financial centres of the world (Figures 6.1.a and 6.1.b are indicative of the US real interest rate, US dollar LIBOR and ‘immediate’ interest rate developments), recovering rates of profitability in emerging markets, and a decreasing share of labour in GDP pushed by a spirit of markets’ liberalisation. The economic trends most frequently observed in developing countries in particular in the same period were: the opening up to trade, the liberalisation of their financial sectors and the privatisation of state-owned enterprises.

In the 1990s growth rates in the advanced economies were fairly stagnant, real interest rates in the financial centres of the world were very low and asset prices were rising rapidly. These factors have historically comprised systematic determinants of capital flow surges (Calvo, Leiderman and Reinhart, 1996). Harcourt similarly suggests that recently the system has been made conducive to financial crises – especially
Figure 6.1a  US dollar LIBOR interest rate (six-month)
Source: WB, World Development Indicators.

Figure 6.1b  Immediate interest rates, USA
Source: OECD Statistics.