THE MAKING OF A NEW ALLIANCE:
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THE MAKING OF A NEW ALLIANCE: THE PRIVATIZATION OF THE BANKS IN MEXICO
In this paper I analyze the privatization of the Mexican banks that started in May of 1990 with the initiative of reform of articles 28 and 123 of the Constitution and that ended on June 16, 1992 in a public meeting between the government and the new bankers in which they celebrated their new alliance. If the reestablishment of a good relationship between business and government has been crucial to the success of the program of economic reform initiated by the de la Madrid government and deepened by the Salinas' administration, the reestablishment of a strong alliance with private financiers seems a key variable in making this new relation politically and economically stable. Only private-led growth can make the new economic model sustainable. Therefore, one of the major difficulties of the new economic project is the mobilization of the voluntary domestic and foreign savings needed to promote growth and to allocate them in the most efficient way.

The reestablishment of a good relationship between government and business has already been studied in some depth. Most authors have pointed out the importance of the new economic project in itself in making the rapprochement possible. The new project is very close to the economic project of big businessmen. Middle and small size businessmen are more sceptic about its virtues. While the ideological leadership of big businessmen and their control over the more important business organizations is significant, their opposition, both political and economic, diminished once big businessmen agreed on the nature of Salinas' project.

The politics that made new links with private financiers possible, and gave substance to the nature of this alliance, however, is relatively unexplored. This is not surprising due to the recent conclusion of the process of privatization. Although an analysis of contemporary issues runs the risk of not assessing properly the weight of recent events, I believe that as the process of privatization is completed one can attempt to make an initial analysis without excessive cost in terms of precision.

The bankers' alliance was effective in the 1960's in promoting stable growth, although it later showed its shortcomings. It is again becoming the basis of the new economic project. This alliance, according to Sylvia Maxfield, involves private financiers, big commercial houses and major industrialists, public officials, and members of the international financial community. The close relationship between private financiers and public officials in charge of Mexico's finances "shaped state economic policy creating institutions in a way that helped give the
bankers a strong voice in policy making". In spite of the power of the Cardenista alliance, which influenced policy makers in the Echeverría and López Portillo administrations, the bankers' alliance has dominated Mexican economic policy. The process of privatization is useful for assessing the current state of this alliance.

The importance of the banker's alliance, I shall argue, comes less from the personal links between members of the alliance and even the institutions in charge of economic policy making, than from the needs of the current economic program. This program was decided by the government as the only option due to the concentration of wealth in Mexico, the internationalization of financial circuits, and Mexico's vicinity with the United States.

Under these circumstances, the traditional liquidity of Mexican deposits, and the lack of currency control deposits have increased the structural power of property holders, namely its capacity to decide where and when to invest. It has increased, in particular, the power of private financiers. For the construction of a stable mechanism through which to channel international and domestic savings (concentrated in a small segment of the population), a good relationship with private financiers is fundamental.

It was the structural power of Mexican private financiers that forced de la Madrid to devise ways of creating a new alliance with them. This alliance, based more on the need to induce private investment than on the personal relationship with some specific bankers, was therefore not entirely with the same people as before. It was led by those that after the turbulent 1980's, had more resources to buy the banks in an open bid.

The rules of the game have changed as well: the new bankers have more liberty to allocate resources, but are more restricted in the discretionary use of the deposits in favour of their own investments. The bankers, moreover, face a political elite, that although sympathetic to their interests, is more coherent and thus more difficult to divide and manipulate.

Although the new alliance originated in the government's need to recapture the confidence of Mexican businessmen, it has been strengthened after repeated interactions where both sides have learnt to trust the other. This incites future cooperation.

The structural power of the financial sector is important for understanding the government's need to construct a new bankers' alliance, but it is not enough to appreciate the specific role this alliance plays in Mexico. To understand this role, and the nature of the new alliance one has to analyze the way this relationship has been reconstructed, with whom and under what rules.

I shall argue that in the process of privatization the government showed its relative autonomy from the former bankers who had been pivotal in the alliance before the nationalization. This alliance was certainly very close and important, as is the new one. But the Mexican State has shown, as it did when it nationalized
the banks in September 1982, that it is not at the mercy of specific private financiers. The banks were not sold back to their previous owners, but to the highest bidder.

Selling back to previous owners has been a relatively common practice. In particular when the property sold was expropriated relatively recently. In this case it is perceived as the reestablishment of property rights.

The Mexican government did not accept the notion that property rights had been violated with the nationalization of the banks. The government decided that the cost of the expropriation in terms of the confidence lost by businessmen had already been paid and that confidence had returned with the new economic project, which included selling the banks.

The government decided it was better to maximize income and ensure that those willing to pay more controlled the banks rather than giving the banks back to their original owners. It seems that the compensation that the bankers received after being expropriated was considered to be sufficient and legitimate, at least in the Mexican press during the privatization process. The success of privatization also shows that the new bankers believe that new expropriation is not likely, despite the maintenance of the institutional framework that made nationalization possible.

Most States, as Peter Evans has argued in a criticism of the rent seeking literature, are not like the predatory State he exemplifies with Zaire. State action is not generally explained by a corrupt alliance between government and business. In his words, many third world states have developed some kind of “embedded autonomy”, where the state has some autonomy, but is not insulated from society, so it can quickly and effectively respond “to a changing economic reality”.

The Mexican government has so far shown a significant degree of autonomy to sell at a high price. It is yet to be seen how developed is its embedded autonomy, that is its capacity to regulate the private banks correctly in a way that promotes economic development in a process that involves close and frequent contact with private financiers.

Privatization makes evident the existence of a state project embodied in a more or less coherent elite that has (partially) internalized the definition of public interest assumed by this project. The “motivational logic”, following Evans, that gives cohesion to this elite and that enables it to avoid the rent seeking temptation comes from its ideological belief in the need for devising a more rational and limited State. This elite knows that if it achieves this it will open up more personal opportunities.

As Evans argues, government elites develop links with society, in particular with businessmen that are crucial for implementing their interpretation of economic development. It is true that links can be ineffective and corrupted, but many States are not controlled by the holders of capital. There exists a complex
relationship whereby both parts have their own resources of power that can be used to collaborate or not with the other part. It is usually in the long-term interest of both sides to collaborate. Sub-optimal solutions in which there is no cooperation, however, are common. In this work a story of some collaboration without collusion between government and private financiers is described. It is, however, only the first part of a longer story still to be developed.

In the first section of this work I summarize the history of the banker’s alliance. In the next part I analyze the process of privatization. In the third, I discuss the composition of the new bankers. In the last section I analyze an explanation for the stability of the new alliance. In the conclusion I discuss the more important implications of the new alliance.

**THE BANKERS’ ALLIANCE IN RETROSPECT**

During the so-called Mexican miracle of the 1960’s, the Mexican economy grew by an average 6.6% per year, with an average annual inflation rate of 4.13%16. One of the factors underlying this stable picture was the close relationship between government and business, and in particular, the close links between the Treasury and the Bank of Mexico (the central bank) and the private financiers.7

In Mexico, holders of capital have traditionally invested heavily in financial services. Even before the creation of modern banks, merchants devoted a lot of energy to financial activities. Before the 1982 bank nationalization the private bankers were the most powerful and sophisticated group of businessmen.

Bankers served as the most important link between government and business. In the words of Camp, they “took on a role separate from their typical function as dispensers of scarce capital. They operated in Mexico as sophisticated influence peddlers, brokers between politicians and the private sector.”18

The links between government officials, primarily those in the Treasury and the Bank of Mexico, and the more powerful Mexican bankers, and the consensus among the political elite on the need to ensure macroeconomic stability, reinforced a macroeconomic policy pattern that sought a moderate public deficit financed through the domestic and international financial markets which was a substitute for a tax reform. This strategy enabled the government to maintain price stability, which coupled with a fixed exchange rate *vis à vis* the dollar, free currency movements and interest rates slightly higher in dollar terms than in the United States, led to high growth in domestic savings.

The domestic financial sector could then serve as the major source of resources for a booming private investment which sustained stable economic growth. In this virtuous scenario, if the government could count on the confidence of the private sector, investment would follow. This, coupled with a propitious inter-
national environment and the early success of a strategy of development based on import substitution, allowed the economy to grow at a high and steady pace.

After the 1968 Tlatelolco student massacre, the Echeverría administration perceived a need to modify the government's economic strategy. The new model was successful in solving the political conflict behind the 1968 student movement, but created a profound crisis within the Mexican private sector. A serious conflict with a significant group of businessmen and an expansionary and incoherent economic policy led to the devaluation of the peso, the symbol of the so-called "Mexican miracle" of the 1960's, and to economic crisis.

The López Portillo administration was well aware of the need to recuperate business confidence. His inaugural speech and his initially more sober style was aimed at regaining their confidence. He thought that if businessmen could be seduced, the old style of development, with some minor adjustments, could be revived. With the help of the massive oil resources and an increasing foreign debt, the government was able to satisfy everybody.

López Portillo, however, ended the last year of his administration with an even more acute crisis than the one he had inherited from Echeverría. López Portillo response was to impose an exchange control and to expropriate the private banks.

For the private sector, nationalization was a clear infringement of the bankers' alliance and the failure of the old basis of negotiation with the government. This infringement was particularly menacing for businessmen, since bankers were perceived as the most influential in policy making, and the ones that most often benefitted from government policies, second only to the politicians.

The de la Madrid government decided not to give the banks back. His relationship with the Mexican political class that had apparently enthusiastically supported the decision of López Portillo to nationalize the banks was more important than the bankers' alliance. It was, after all, a precondition for the success of the alliance with financiers, as it provided the Mexican political system with control over the more important organizations of workers, peasants and other popular sectors.

Yet, de la Madrid's government needed businessmen's support to stabilize the economy and to recover growth and therefore made an effort to construct a new alliance with private financiers. All non-banking stock was sold back to the private sector in a process where former owners had preference. Compensation was quick and higher than book value.

As a result of the nationalization of the banks that made private financiers move their resources from the banks to other financial institutions, a series of legal changes such as restricting the roles of banks in negotiating Treasury Bonds (CETES) and other government paper stock, brokerage houses grew in a spectacular way. While in 1980 the commercial banks captured 95.5% of deposits in the formal financial system, in 1990 they only captured 62 per cent.
Although in the late 1980's it was thought that the former bankers were being compensated for the expropriation of the banks with the boom of the stock market and the growth of brokerage firms, De la Madrid's policies did not reestablish the former alliance, as I will describe in more detail in the next section. Measures taken to promote the growth of the financial sector were motivated primarily from the need to have a strong financial sector necessary for new growth and for achieving the confidence of savers. These measures did not primarily benefit the former bankers. This was particularly clear when the Salinas government decided to sell the banks back to the private sector.

**THE MAKING OF A NEW ALLIANCE**

Why did the government decide to sell the banks? Private financiers were already playing an important role in brokerage houses and the nationalized banks gave the government control over a segment of the market. It was also a source of employment for high level civil servants.

The government, moreover, was not a bad banker. The government rationalized the structure of the banking system through a number of mergers. Of 62 credit institutions, including 35 multiple banks, the government ended up with just 18.

The banks had been performing more or less correctly. Profits had gone up by more than 195% in real terms from 1982 to 1989, from 0.45% of total assets in 1982 to 1.33 in 1989, and so had productivity per worker, and other key indicators.\(^\text{27}\)

Although during most of de la Madrid administration they had been losing ground *vis à vis* other financial institutions, the legal changes announced at the end of the De la Madrid administration and the beginning of Salinas' had given the banks more freedom, which had already been reflected in an increase in their activity.

As seen by the increase of profits after their sales, however, which are described below, the national banks were relatively inefficient. Corruption, moreover, was starting to appear and some banks had problems with poorly allocated credits. After privatization, the new owners discovered that credits due were higher than expected.\(^\text{28}\)

In any case, privatization was not justified by the government in terms of the inefficiency of national banks, as it was in other privatizations. It was argued that the privatization would allow the State to devote attention to those issues that only the State can solve. Income from privatization (and the saving implied by not investing more in banking as would be needed in the light of the modernization of the economy) would allow the government to increase well targeted social spending.
Privatization was used as a way of convincing businessmen that the State reform conducted by the Salinas administration was willing to change the structure of the Mexican economy. This included reverting nationalization, which in September of 1982 was elevated by some sectors of the government as one of the myths of the Mexican revolution. It was also important to assure Mexican savers that their resources would be correctly managed.

These savings are concentrated in a small number of individuals. Deposits of 18,649 people and firms with accounts of one billion pesos or more, 0.07% of total accounts, make up 53% of total deposits. Those with accounts of 250 million or more, 96,382 firms or people, represent 0.37% of total accounts and 66.10% of total deposits. According to the government, the number of shareholders after privatization amounts to nearly 130,000 people. This implies that the most important savers may own part of the banks, thus privatization allows them to directly or indirectly manage their savings.

As a sign of the confidence achieved by privatization, when it was announced, the shares of the banks listed in the stock market rose sharply. Many jumped more than 15% in the same day. Before the announcement of the privatization of the first bank its shares went up 10%.

Due to the relatively small number of potential groups that could organize such a complex buy, (44 groups actually bid for 18 banks) the absence of democratic controls over the Mexican government, the weakness of a critical press, and the close personal links between government officials in charge of the sale and many of the potential buyers, one might have feared a collusion against the public interest. Either the buyers would reach an agreement to bid at low prices, or the buyers would compensate (bribe) the sellers if they agreed to sell at low prices.

But the government, who needed the banks' money and wanted to avoid any criticism, devised a mechanism to diminish the risk of this collusion by means of a process where discretionary faculties were diminished at crucial moments. A new entity, the Comité de desincorporación bancaria, was created. Presided by the undersecretary of credit, it was formed by the General Director of the Bank of Mexico, the President of the National Bank Commission, the President of the National Stock Commission, and three civil servants of the Treasury. The Secretary of the Treasury invited two other people of prestige, whom he considered could positively contribute to the process.

This committee gave the government's side of the bankers' alliance control over most of the process, although the final decision was ratified by the Inter-secretarial Spending-Finance Commission comprised by the more important Secretaries. The President directly ratified the most difficult decisions.

The process was strictly regulated and involved two rounds. First, the Comité de desincorporación bancaria had to value the banks with the aid of an external audit and decide whether the groups wanting to buy the banks were economically
and morally solvent. Once this was done, and no former banker was apparently veteed, a second round started and a secret auction was conducted. In the second round, the government had to allocate the bank to the highest bidder except when the difference between the two highest bids was very small. This was called a technical tie. When this happened the government decided to give it to the highest bid, thus renouncing its discretionary power.

This process allowed the government to maximize revenue and minimize conflict. The first round obliged the potential buyers to partially disclose their position. Not only did the government know who the potential buyers were, but the other buyers knew how many groups were interested in buying banks. This created an incentive for bidding high in the second round.

The price paid by the bankers seem to be relatively high. There is, for example, an agreement among important losers that the winners paid too high. This was expressed by two of the more important former bankers, Manuel Espinoza Yglesias and Carlos Abedrop Dávila.\(^{35}\)

There is also the belief that the process was fair. There were no public recriminations by the losers, who have so far agreed that the process was fair. There were some difficult cases, like the case of Banco Mexicano Somex where the winner lost his deposit because he was unable to pay what he had promised, but they can be considered marginal in such a complex process. There were some accusations of partiality in the press, but they were, I think, difficult to substantiate. None could prove that the government did not sell to the highest bidders.

High prices were more evident in the smaller banks, where there were more bidders. In the two big banks prices were relatively lower. When the first bank was sold, many thought the price paid by the winning group was too high, but it ended up being one of the cheapest banks.

The government received more than was expected. According to a leading financial columnist, the government would not obtain more than 15 billion pesos for the shares of the banks.\(^{36}\) The government's objective was to obtain around 24 to 30 billion pesos.\(^{37}\) The market value of the banks was around 24 billion pesos, but the government does not own all of the shares in the banks.\(^{38}\) A maximum of 33% of the shares of most banks were sold in the De la Madrid administration,\(^{39}\) leaving the government with 73.36% of the shares in the banking system.\(^{40}\) The government has obtained, according to official figures, 43.7 billion pesos.\(^{41}\)

The banks were bought at 14.07 times profit and 3.07 book value. The same figures for banks bought in the United States in the last five years have been on average 14 and 2.2 times.\(^{42}\)

The prices paid by the new bankers, however, could be explained by hidden profits. As the new owners knew they could quickly improve profits, the price/profit ratio does not reflect the real price paid by the bankers. The profits of twelve banks, including the three most important ones, in 1992, were, in fact,
nearly 35% higher in real terms than the previous year. Banamex, the biggest bank, has been particularly successful in increasing its profits by nearly 45%. Private banks seem to be capturing new opportunities.

But the stock market seems to be unconvinced by the increase in profits. Share prices of most bank stocks went down after the sale of most banks. By January of 1993, as a result of the uneasiness with respect to the stock market, prices tended to be even lower.

It seems that one of the main reasons behind what I think can be labeled as a successful sale in terms of income and lack of conflict is that, for the Secretary of the Treasury in charge of the process, maximizing revenue and minimizing conflict was a crucial goal. On the one hand, it helped to reinforce the stabilization program, which is his direct responsibility. Due to the crisis of the 1980's, the government is quite aware of the cost of running a public deficit. This is one of the reasons behind the successful tax reform carried out by the Salinas administration. High prices for the banks has been an important aid in raising revenue.

On the other hand the smooth process of privatization has made it less conflictive with those sectors that were against it, and has reinforced the relationship between the public and private financiers. This relationship, as described below, can be important in deciding the PRI candidate for the presidency, who is expected, if there is no major economic shock, to be the next Mexican President.

If the nationalization was the result of the lack of government control over the economy and was done in secrecy, the privatization was carefully designed. The rules of the game devised by the government allowed for a minimum use of discretionary power. Privatization, moreover, was done in the midst of great optimism with respect to the future growth and stability of the economy. In this sense, the timing was perfect. A few weeks after privatization had concluded, the mood of confidence had changed as a result of a more pessimistic view of the current account deficit and of the international environment, which was reflected in the fall in the stock index and by the postponement of the international flotation of Banamex-Accival.

To understand the relative success of the government, one has to see also the buyers logic. Why did domestic investors decide to buy, at relatively expensive prices, an asset that had been expropriated less than ten years before?

The new banking law introduces an important change that increases the legal security of bankers. Banking is not considered a public service as before but one of general interest. In a public service the State is the only one endowed with the right to provide it, although it can concession it to the private sector. In services of general interest, anyone can give the service. Sometimes, however, as in the case of banks, only with the authorization of the government.

The difference is not only technical, but has important implications also. If concessions are cancelled, the State can get hold of the property needed to provide
the service, without compensation. In contrast, when an authorization is lost, this does not happen.\textsuperscript{48}

The expropriation, however, was achieved not by cancelling the concession, but by means of the Law of Expropriation. This law has not been changed, nor have the institutional features of the Mexican political system that made the nationalization possible.

Yet, the change in the economic project, by increasing the role of the market, has convinced businessmen that an expropriation is unlikely. By involving the United States and Canada, the signing of a North American Free Trade Agreement (NAFTA), which was seen as highly likely, increases the security of their investments.

Once confidence was reestablished, there were few other alternatives as attractive as the banks for the massive resources private financiers had accumulated during the eighties.\textsuperscript{50} Banks have been traditionally reserved to nationals, so a strong group of Mexican financiers existed.\textsuperscript{51}

Financial groups, permitted by the new banking law, allow the creation of the so-called “universal banking,” which will enable stock brokerages that bought a bank to boost productivity. There are also important growth possibilities as the banks are still underdeveloped, in terms of penetration, when compared to other countries. If the Mexican economy grows as expected, the banks will be one of the sectors that will benefit from it.\textsuperscript{52}

There was also an element of prestige. During the process of privatization it was mentioned, as a joke, that the high price being paid could only be explained by the fact that being a banker is the only aristocratic title in Mexico, as the Mexican Constitution does not allow nationals to have any title of nobility. To a certain extent, this perception has historical roots. Prior to nationalization, bankers enjoyed a position of prestige and power few other businessmen could boast. The two more important bankers, Espinoza Yglesias and Legorreta were sometimes referred to as permanent parallel Secretaries of the Treasury.

The capacity of the buyers to sell a significant part of the shares in the international markets where ownership is pulverized without losing control over the bank, also explains the relatively high prices. Financial engineering allowed private financiers to secure banks without investing all the capital initially paid for the banks, and retaining only the controlling shares.

The new bankers will also face a less regulated environment with respect to the allocation of most credits.\textsuperscript{53} The \textit{encaje legal} (forced credits to the government) and other credit restrictions have disappeared.

The State, however, has devised a more restrictive regulation than before nationalization took place with respect to some of the more profitable activities, like credits to firms owned by the banks or by the principle shareholders, usually at below market rates. Credits to the firms of the members of the board are now restricted to 20\% of total bank credits and will have to be approved by two thirds
of the members of the board of shareholders type “A” (51% of total shares) and 60% of board members representing type “B” and “C” (shares open to foreigners). Banks are also limited in the ownership of firms not related to banking activity; they may never own more than 5% of total shares. Only in risk projects can this figure reach 15%, with the approval of the majority of the members of the board and the authorization of the Secretary of the Treasury. The government also has the right to approve the President, Managing Director, and all the officials of the next level of the banks.

The new banking law is also more restrictive with respect to the organic links between the financial sector and industrial and commercial firms. Only individuals or a Financial Group can own shares in a bank. No individual can have more than 5%. The same regulation applies to Financial groups, that are wholly owned by individuals. Before nationalization there was no limit. One single individual or firm could control the bank, as Espinoza Yglesias did with Bancomer of Visa with Serfin. The new law obliges the owners to manage the banks in a less autocratic way.

Property over many of the more important industrial groups is very concentrated. It is common for one family or even a single individual still to own more than 50% of the shares of an important business group. Under these circumstances, one powerful individual can assemble a group of investors to buy a bank.54

THE NEW BANKERS

Contrary to what was perceived in the 1980’s, the boom of the brokerage houses of the second half of the De la Madrid administration did not principally favour the former bankers. It allowed the emergence of a new group of financiers: owners of relatively small brokerage houses55 before nationalization took place, and not associated with the bankers before 1982.56 These financiers knew the stock market much better than former bankers, who, in the light of their control over the banks, had seen the stock market as a relatively unimportant business.

The relative winners of the boom are reflected in the privatization process. The banks have been sold basically to a group of people, mainly owners of brokerage houses,57 that include some of the former bankers, but which is not led by them.58

There is no evidence that there was a veto by the government against the former bankers.59 It seems many of them did not have enough money to buy the banks at the prices that were paid, or they were unwilling to pay such an expensive price.60 In the sale of many banks, the former owners participated and lost (as for example in the case of Multibanco Mercantil and Bancomer). As the government has recognized, privatization opened the “doors to a new generation of Mexican businessmen”.61
A crucial element in explaining the success of the winners is that they had believed privatization would take place and profiting from their position in the stock market had bought the shares of the banks already on the market, the so-called CAPS, before their announcement at a low price. Former bankers were less likely to buy CAPS.

Having enough CAPS enabled their owners to sit on the boards of the banks and to sell the shares of those banks they were not interested in at a higher price in order to obtain resources to bid for their preferred bank. The most obvious example of this is Accival, which after buying a lot of CAPS at relatively low prices, was able to buy the largest bank, Banamex.

A systematic analysis of the boards of the banks before nationalization and after privatization would lead to more precise conclusions. Yet there is sufficient evidence to conclude that a new group of bankers have at least partially replaced the old ones.

Of the 60 people mentioned by Sales Gutiérrez (former undersecretary of banking affairs) as representatives of the expropriated bankers, that include the four most important bankers Manuel Espinoza Yglesias (Bancomer), Agustín Legorreta (Banamex) Eugenio Garza Laguera (Serfin) and Eloy Vallina (Comermex), only 4 appear among the 44 most visible new bankers. Agustín Legorreta, who controls the second largest brokerage house, is back with a relatively smaller bank (Comermex), number four in the system. Eugenio Garza Laguera, former owner of Serfin now controls a bigger bank (Bancomer). Garza’s success is explained fundamentally by his success as an industrialist rather than as a former financier. With nationalization, Garza Laguera did not lose control over Visa. Although highly indebted, this group benefitted from the support of Ficorca, a government program devised to help indebted groups. The crisis also allowed this group to buy its paper back at a discount. When the government started to promote exports, Visa was one of the winners. A similar story explains the return of Adrián Sada, former owner of Banpaís, a small bank. Sada the owner of Vitro profited from the same three elements that were so favorable to Visa. The success of Vitro is exemplified by its acquisition of Anchor Glass Containers Corporation, the 307 US industrial corporation. The strength of Vitro, plus the problems of Operadora de Bolsa after the 1987 stock exchange crash due to its massive illegalities, gave Sada control over a powerful brokerage house which enabled him to buy Serfin, the third largest bank. The fourth old face is Antonio del Valle, former owner of Bancreser now the owner of Banco Internacional, the fifth largest Mexican bank.

Having said this, one should not conclude that the most important shareholders have changed so much. Many of the most important businessmen that participated in the banks prior to 1982 are participating again. While the financial sector witnessed important changes the ownership of major industrial and commercial firms remained relatively stable. The more notable exception
is probably Carlos Slim, owner of Grupo Carso and Telmex who made his fortune as a financier in the 1980's, but who latter decided not to buy a bank, although he participates as an important shareholder in at least one of them. What has changed more significantly is the leadership of the banks.

A Reciprocal Relationship

If the new bankers were willing to pay relatively high prices for the banks, it was in many ways due to the relatively underdeveloped Mexican financial markets and to the importance of banking in an economy that is expected to grow in future decades, but it was also the result of the high barriers of entry to the Mexican financial system, which leads to higher profits than in other markets. In spite of the liberalization of the economy, the financial system remains relatively protected. Although big corporations have access to the services of foreign banks, and many wealthy Mexicans keep part of their savings abroad, it is still a protected industry. This is reflected in the price of financial services. The differential between passive and active interest rates in Mexico, for example, remains very high. The profitability of Mexican banks is nearly three times higher than that in Canada and the United States.

These barriers were, however, easy to change by means of new legislation. The government could, having completed the sale of the banks, authorize new banks, or open the market to foreign competition. Both measures would have diminished the real value of the banks sold.

This has not yet happened. It seems there was a tacit agreement with the bankers which was respected by the government. Since privatization started, for example, it was stated that one of the government’s objectives was “to assure that the Mexican bank is controlled by Mexicans”. This was perceived as very important in order to have some basic control over the economy.

The government did give the bankers relative protection. It seems that the Secretary of the Treasury fought successfully for a relatively good treaty for the bankers. The United States bank’s wanted a quick opening and the creation of branches, not subsidiaries. According to the agreement, foreign banks will have to operate through subsidiaries and will be limited to an individual 1.5% of the market and a total from 8% to 15% in the first six years of the treaty. Temporal protection will be given afterwards in the next four years if foreigners control more than 25% of the market. Although the bankers were seeking more permanent protection, they remain in the light of NAFTA, one of the more protected domestic groups.

Moreover, the recently created Sistema de Ahorro para el Retiro (SAR), a compulsory pension fund amounting to 2% of wages paid by the employer and the new management of the housing fund 5% of wages (formerly managed by In-
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fonavit), is reserved for the banks. A similar project that would have allowed brokerage houses to participate would have expanded the alternatives of savers and would have capitalized the stock market. The decision to reserve it for the banks seems to be a way of favoring the new bankers.78

What made this game stable? First it is not the first move of the game. The game started when De la Madrid took power and while not reversing the decision of López Portillo to expropriate the banks (nor allowing the Supreme Court to concede the amparo demanded by the bankers), he devised a series of policies aimed at reestablishing a good relationship with private financiers.

The success of this policy led to a spectacular growth of the stock market. This boom however, ended in a dramatic crash. The dubious legality of some brokers, and the government's lax supervision, made the relationship between the financial sector and the government closer. The government did not want to destroy the new financial sector, and decided not to strictly apply the relevant regulations.79

The financiers knew that the government had collaborated with them when in a position of strength, so they felt they could trust the authorities. Government collaboration was not altruistic: the cost of a scandal and the weakening of the financial sector was very high.

The boom and the way they managed the crash, moreover, helped these financiers to obtain the resources to pay handsomely for the banks. This expropriation of savers was apparently socially more legitimate than the one conducted by the government in 1982 through inflation, devaluation and the mex-dollars.

Not only was the previous move of the game important. One should also focus on the need of the government to establish a long-term working relationship that would allow the appearance of a new bankers' alliance. This was very important in government's overall economic strategy. The government has been seeking for nearly ten years to generate confidence in its actions. To affect the bankers who had accepted to pay a high price for the banks with new authorization or a very liberal agreement in this sector would have sent a signal to domestic savers that they could follow the new banker by means of an abrupt devaluation or the monetization of public debt. There was, moreover, the need to give some protection to the recently privatized banks and to modify many domestic regulations before allowing foreigners to participate in the Mexican market.80

The new alliance is also important for the political career of the Secretary of the Treasury, Pedro Aspe. Aspe has made evident, in the light of the presidential succession, his strong links with private financiers.81 This link is by no means enough, nor does it ensure that the financiers are only loyal to Aspe. It does, however, give the Secretary of the Treasury a robust starting point.
The new alliance faces the problem of constructing a coalition that includes other social sectors. In the 1960's, in spite of the inclusiveness of the Mexican political system, it was the exclusion of some groups that eventually precipitated a wider State intervention in the economy, financed partially by inflation, and conducted in a very incompetent way, which led to economic and political crisis.

The new model seems even less inclusive than the previous one. Although small and middle size firms had little credit made available to them by the bankers in the previous model, they did count on the support of trade protection and various measures of industrial promotion that amounted to some kind of industrial policy.

There are less supports in the new model. The centerpiece of the alliance is more clearly the financiers, as I have analyzed, and the largest export firms and commercial houses which have not been considered in this work.

From the economic point of view, there is, firstly, a potential tension between financiers and exporters as the former tend to favor a stable currency and positive real interest rates and the latter prefer a margin of undervaluation and cheaper credit. Secondly, and more important, the new alliance could not be enough to promote development. Control over inflation and a stable currency that tends to be overvalued could lead to very low levels of growth, a too large current account deficit, and to a further concentration of wealth.

Moreover, maximizing revenue by accepting the highest bid for the banks has not been free of cost. First, in spite of the 5% limit on individual shareholders some individuals have reinforced their control over domestic savings, and some have situated themselves on a significant number of banking boards so as to enjoy a very powerful position. Moreover, the concentration of the Mexican financial sector has been accentuated as the result of the merger of Accival, one of the most important brokerage house, with Banamex, the most important bank. Second, the high price paid by the bankers have led them to overprice their services. The government needs to ensure that privatization is sustainable and has allowed them to profit from their position. This certainly has a cost for the rest of the economy.

As the new bankers face less regulations than before, and with nationalization in the allocation of resources, credits might concentrate in those sectors that have already benefitted most from the process of economic reform. Some members of the government are aware of this risk and have asked the banks to allocate credits to the farming sector as the best way of achieving social peace. This could be, in the words of Carlos Hank González, Secretary of Agriculture and Hydraulic Resources, the best investment.

But if the market rewards more investments in the large modern industrial and commercial sector, each bank will find it profitable to lend there. And the government has hardly any control over the resources managed by the private
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financier, and therefore few resources to induce cooperation. The government still holds the development banks. Two of them, Nafinsa and Bancomext, enjoy a very strong position, although it is still too soon to know whether they will be able to promote correctly those activities not financed by private bankers. As the State’s reforms continue, the direct economic role of the government will diminish even more. In the last Annual Bankers Convention, the President made explicit that public spending will not reactivate the economy. This means that private resources are responsible for the future growth of the Mexican economy, and the private financiers will therefore play a central role. In the words of Antonio del Valle, the new Managing Director of Banco Internacional, bankers have the responsibility of managing the financial resources of the country in an efficient way. This is yet to be seen.

Incorrect practices by the new bankers are, however, in theory more restricted than before nationalization took place. The State showed its capacity to act with autonomy when selling the banks. Privatization made evident that the Mexican government can manage certain issues with a minimum of discretionary power. Such an “island” of legal rationality, however, can be difficult to maintain in the absence of social controls over the Mexican government. Now that the banker’s alliance has been created again, the government will find its role of supervision more difficult. For example, new rules with respect to credits given to the owners of the banks have been devised. This could lead to a poor allocation of credits.

As the game is reiterated both parties tend to grow progressively closer. Whether “embedded autonomy”, following Evans, has been developed is yet to be seen. If it has not, it can have a negative impact on the economic rationality of the current State reform.

Politically, the new alliance also faces potential problems. In the absence of a legitimate democratic process, the new model can have difficulties in incorporating political discontent. The government has devised a program of social spending to give support to the worst off and to generate political support from this very numerous social group. In the same forum, in which Salinas celebrated the end of privatization, he celebrated weeks later the Solidarity Program, devised by the government as way of promoting social spending in a more efficient way both politically and economically. This program, however, cannot be working as the government affirms. It is also probably insufficient. Vast sectors of the population are probably left without government support.

The government also faces the problem of building enough political support at the expense, perhaps, of weakening the bankers’ alliance. This happened in a virulent way in the 1970’s, with very costly implications. The prevailing risk is that these historic lessons may make government policies too cautious with respect to inflationary pressures and too intransigent in the face of those political forces ideologically close to the previous economic project, at the expense of being unable to manage peacefully the demands of Mexican society.
NOTES

1 An early version of this paper was presented at the Latin American Studies Association XVII International Congress, Los Angeles, United States September 23-27, 1992. Carlos Bazdresch, Blanca Heredia, Yemile Mizrahi, Ben Ross Schneider and John Scott read this version and gave very useful comments. All shortcomings are my responsibility.


3 In some areas, as Chihuahua's study by Yemile Mizrahi shows, this group of businessmen have still been pivotal in electorally defeating the PRI. See Yemile Mizrahi, The New Conservative Opposition: The Political Organization of Entrepreneurs in Chihuahua. Ph. D. Thesis in progress, University of California at Berkeley.

4 For a historic account of this up to the first half of the De la Madrid administration see Sylvia Maxfield, Governing Capital: International Finance and Mexican Politics, Ithaca, Cornell University Press, 1990. For a Marxist perspective see Russell N. White, State, Class, and the Nationalization of the Mexican Banks, New York, Crane Russak, 1992, who makes a brief analysis of the initial stage of the privatization of the banks.


5 See Maxfield, Governing Capital, chaps. 1-2.

6 In particular with those firms with the capacity to export, as the economic opening affects firms concentrated in the internal market.

7 Ibid., p. 9.

8 Maxfield, Governing Capital..., op. cit., chap. 2, argues that the role of private financiers in the foundation of the central bank is very important to understand the close personal links between monetary authorities and private financiers and the propitious economic policy making institutions for bankers' interests. Personal links strengthen the position of monetary authorities vis à vis the rest of the bureaucracy. I give, however, less importance to the personal links, and to the economic policy making institutions, and more to the structural power of holders of capital than Maxfield does.

9 Whether this is true is beyond the purpose of this work.

10 For a brief review on the literature of "structural dependence" see Adam Przeworski and M. Wallerstein, "Structural Dependence of the State on Capital", American Political Science Review,
The power of a social group is not only present when they stop a policy, it also exists when government officials anticipate the reaction of those with power and do not suggest or implement a policy that would affect them. To induce private investment, government officials take decisions they anticipate will have such an effect. For an analysis on the different dimensions of power see Steven Lukes, *Power: A Radical View*, London, McMillan, 1974, and William E. Connolly, *The Terms of Political Discourse*, Oxford, Martin Robertson, 1983, chap. 3.

There were some criticisms to this policy of selling to the highest bidder instead of selling back to the previous owners. See for example Luis Pazos, "Expropiación y venta de bancos", *El Financiero*, April 27, 1992.


A description of business-government relations in the López Portillo administration can be found in Rogelio Hernández, *Empresarios, banca y Estado: El conflicto durante el gobierno de José López Portillo, 1976-1988*, Mexico, Miguel Ángel Porrúa, 1988. In my view, the relationship was less conflictive than what this book suggests.


This is the ranking that came out in the questionnaire conducted by Story in the Summer of 1980. Dale Story, *Industry, the State and Public Policy in México*, Austin, University of Texas Press, 1986, p. 121.


Whether the compensation represented the real value of the banks is, however, difficult to assess. The compensation was more than the stock market value before nationalization. Yet, the market was very depressed and its price did not reflect the value of the whole firm, as in any take-over the price of the shares escalates. When compared to the price the banks are being sold at, the government made a spectacular deal. Banamex and Bancomer, the two largest banks were
bought at 1.36 and 1.55 of their book value. The expropriated bankers were demanding at least 3 times that. Banks with problems were bought at a price lower than book value. The government decided not to pay the intangible value of the banks, as demanded by bankers, such as reputation, human capital, market share, etc. In real terms, the profits of the banks allowed the government to absorb the compensation including interests by 1985. See “Empresa”, La Jornada, February 11 and 14, 1992; Tello, La nacionalización de la banca..., op. cit., p. 168; and Carlos Sales Gutiérrez, Indemnización bancaria y evolución del sistema financiero, 1982-1988, Mexico, Páginas del Siglo XX, 1992., pp. 21-29 and 186-189.


28 When these credits were incorrectly classified by the government, it compensated the new owners. See note 41.

29 For the official justification of the privatization see the initiative to reform article 28 of the constitution in Revista de Administración Pública, no. 81 (1991).

30 One billion pesos in Mexico is one million of millions, that is one trillion in English. It is equivalent to roughly one third of one US billion dollars.

31 Data from the Banco de Mexico quoted in El Financiero, September 9, 1992.


34 This was apparently the case, for example, in the case of the decision to give Banamex to the largest stock broker, Accival. The difference with the other offer was very high, higher than expected. Alberto Aguilar, “Hombres de Nombre”, El Economista, August 27, 1991.

35 Abedrop, for example, argued he would become a banker again in the second round. As the new bankers have paid so much, he thought, they will get broke or need new partners. At the prices being paid he was not interested. He thought that high prices could be paid for the small banks. He predicted no one would pay more than 2 times book value for Banamex. Interview in Uno más uno, August 25, 1991. The winners of Banamex paid 2.6, and not only for the 31% needed to secure the bank, but for the 70% of the shares in the hands of the government.


39 As the shares were sold at a relatively low price the buyers won a lot of money.


41 This figure includes the minority position of the government in some banks shares still in the hands of the government, equivalent to 8.8% of total shares. Quoted by Pedro Aspe in his speech July 16, 1992, of the “Reunión de evaluación del proceso de desincorporación bancaria”, in El mercado de valores, no. 15, 1992, p. 7. Due to incorrect debt valuation, the government has returned to the buyers 2.53% of the value paid by the bankers. El Financiero, February 5, 1993.

42 Sandor Valner representative of First Boston Bank, one of the banks that advised the Mexican government in the privatization process. El Financiero, July 8, 1992.


44 According to Grupo Financiero Prime, by the end of February of 1992 the price of the shares of only 2 out of 8 banks was higher than before the sale to the private sector. Reported in La Jornada, March 3, 1992.

45 A detailed analysis would be important to determine the relative performance of the financial sector vis à vis other sectors.
The process was controlled by the undersecretary, Ortiz, with close personal links with José Córdoba and the President himself. This made a collusion between the Secretary of the Treasury and buyers more difficult.

I analyze this in “In Search of Revenue: Tax Reform in Mexico under the Administrations of Echeverría and Salinas”, 1992, (mimeo).

The shrewd strategy of the government was also reflected on the way in which they managed the supply of banks being sold. Initially buyers did not know whether the government would sell all the banks. In the initiative of reform of article 28 it was mentioned that a mixed regime was to be established. In such a regime, as the one that existed prior to 1982 the government owned some commercial banks. See initiative of reform in Revista de Administración Pública, p. 174.

Francisco Borja Martínez, El nuevo sistema financiero mexicano, Mexico, Fondo de Cultura Económica, 1991, pp. 112-114.

The more attractive was probably Telmex, bought by Carlos Slim who defeated the group that afterwards bought Banamex.

The current law allows foreigners to own 30% of the shares. Only one foreign bank, Citybank, operates in Mexico under very restricted conditions. Many others have offices that are used for doing private banking. This will slowly change with NAFTA, as discussed below.


See “Ley de Instituciones de Crédito” and “Ley para Regular las Agrupaciones Financieras”, in Diario Oficial, July 18, 1990.

This explains why the owners of Visa and Vitro own Bancomer and Serfin.

When nationalization took place, Casa de Bolsa Banamex now Inverlat, controlled 20.77% of the capital market, and Operadora 19.18%. Accival only 6.67%. Probursa had 2.86%. In 1991 Accival was the most important firm in the market with 21% of stock portfolio and 18 of total profits. It was followed by Inverlat and Probursa with 11% and 10% of stock portfolio and 12% and 8% of profits. Bolsa Mexicana de Valores, Anuario Financiero y Bursátil, 1982, pp. 49 and 50. Expansion, vol. XXIV, no. 597, 1992, p. 391.


Owners of brokerage houses are more inclined to take risks than orthodox bankers. This helps to explain their success when bidding for the banks, but it could be an obstacle for managing them with prudence.

The other important privatization, Telmex, the national telephone company, was bought by a group led by Carlos Slim, owner of a brokerage house, and not a former banker.

Some argued Manuel Espinoza Yglesias was vetoed, although he publicly admitted there was no veto against him and he bid for Bancomer and lost by a large margin. El Financiero, December 21, 1990.

For example, Eloy Vallina, former owner of Comermex, preferred to buy a bank in Texas, which was cheaper than a Mexican bank.

Words of President Salinas quoted in El Economista, August 17, 1992.

A detailed description of the sale of each bank can be found in González, “Análisis de la reprivatización”, pp. 77-101.


Based on data of Uno más uno, September 1, 1992.

Expansion, August, 1992.

As Nuevo León retained Serfin the third largest bank and gained Bancomer, the financial power of this state has increased. Three other relatively small banks were also bought by people of this state.

See for example the list of businessmen quoted by Hernández as members of Bancomer Councils before nationalization. They are still the same people in the board of the new banks as reported by
the press. See Hernández, “Empresarios y empresas”, p. 83. A more systematic analysis of the boards of old and new banks is needed in order to be more precise.

68 Slim, Hernández and others that profited in the eighties, thought the economic crisis was less critical and bought domestic assets after 1982 at very low prices. Slim is likely to be given an authorization for opening a new bank.

69 See Asociación Mexicana de Bancos, “La banca mexicana en transición…”, op. cit.


71 The implicit protection with respect to Canadian banks is 32 to 94% depending on the methodology used. Ibid., p. 221.

72 The difference between the average cost of the funds of the Mexican banks (Costo Porcentual Promedio, CPP) and the interest rate for credits was 17.43 in 1988, 12.32 in 1989, 7.88 in 1990 and 6.06 in the first eight months of 1991. Data from the document of the Secretary of Budget and Planning, SPP, 1991. This downward trend seems to have changed since privatization.

73 Different accounting practices make comparisons difficult, see Gavito, “El sistema financiero…”, op. cit., p. 223.

74 Seven groups have already asked authorization to create new banks. The government will reply in May. El Financiero, February 5, 1993.

75 First Article of “Acuerdo que establece los principios y bases del proceso de desincorporación de las sociedades nacionales de crédito, instituciones de banca múltiple y crea el comité de desincorporación bancaria”. Published in Revista de Administración Pública, no. 81, 1991, pp. 179-183.

76 See for example parts of the letter by the United States Banks Association quoted by El Financiero, October 3, 1991.

77 The complexities of the treaty and its economic impact are beyond the purpose of this work.

78 The General Director of Serfin, however, has argued the SAR is only a disguised tax that is very costly to the banks and profits will not appear before 8 years. (El Financiero, September 11, 1992.) It is true that the SAR is a disguised tax, but one that is managed by the banks. The fight among all the banks for the accounts of the SAR show the interest of the banks in the SAR. According to some analysts it could become a major source of long-term funds managed by the banks. According to Bancomer, by 1996 the SAR will have increased financial savings from 40% of GDP to 54%. El Financiero, June 1, 1992.

79 The exception came when Salinas took power and he sent to jail one of the most important brokers, Eduardo Legorreta president of Operadora de Bolsa and brother of Agustín Legorreta president of the more important business organization, the CCE (Business Coordinator Council). The imprisonment of Eduardo Legorreta made their vulnerability more evident. The open illegality of Legorreta made his case difficult to defend and could be used by the government as a scapegoat. His brother did not change his pro-Salinas attitude.


81 See for example the open support of some financiers in the first annual meeting of the Bank Association after privatization for Pedro Aspe as the best candidate for the Mexican presidency. Other financiers were more cautious and remained silent, but there seems to be an agreement on the need of continuity in economic policy, which is indirect support for Pedro Aspe. See El Financiero, July 27, 1992.

82 See Maxfield, Governing Capital, pp. 103-108.

83 Banamex-Accival has 28.75% of the resources of investment funds, followed by Inverlat-Comer湄x with 10.35%. The five largest groups have 66.17%, data of August 28, 1992 in El Financiero, September 18, 1992.

84 See some of the measures taken by the government to make life easier for the bankers in Gustavo Lomeli, “Para su información”, El Financiero, February 8, 1993.

85 See the words of Carlos Hank González at the last Annual Bankers Convention. El Universal, August 26, 1992.
Weeks after privatization was concluded, there were some private financiers demanding the right to buy the development banks. The government emphatically said it was not contemplating such a change.

The State, however, is still the motor behind an economic reform devised as a way of enhancing the role of the market.

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