Industry, Science and Technology Canada
Industrie, Sciences et Technologie Canada

THE NORTH AMERICAN FREE TRADE AGREEMENT (NAFTA)

SERVICE SECTOR IMPLICATIONS FOR CANADIAN SERVICES TRADE WITH MEXICO

SERVICE INDUSTRIES

Canada

THE NORTH AMERICAN FREE TRADE AGREEMENT (NAFTA)

SERVICE SECTOR IMPLICATIONS FOR CANADIAN SERVICES TRADE WITH MEXICO

Business and Professional Services Directorate
Services and Construction Industries Branch
Industry, Science and Technology Canada
September 4, 1991

NAFTA

a. Executive Summary (i)

1. Trading Relationship 5 - 8
   ➡ North American Trading Relationships

2. Services Trade:
   General Issues for the NAFTA 9 - 17

ADDENDUM

3. The Mexican Case 19 - 34
   ➡ Services Trade: Issues of Concern

4. The Mexican Service Economy 35 - 57
   ➡ Profile of the Mexican Service Sector and Opportunities for Canadian Industry
   ➡ The Mexican Service Economy

EXECUTIVE SUMMARY

This document is intended to be informative, and deals with issues that may be relevant to Canada's position for a free trade association with Mexico; it does not consider issues that pertain to the U.S. within the same free trade association.

- *Mexico and Canada currently have a limited trading relationship, one which is not well developed in services; for this reason, and due to the geographical location, language barriers and that country's adjacency and trading relationship with the U.S., we conclude that the short term impact of a NAFTA on services trade will not be significant.*

- *The freer movement of goods and services in a North American marketplace is expected to enhance the efficient allocation of resources and raise productivity levels in Canada; opportunities should arise for Canadian services exporters as a result of freer access to a Mexican market which is currently experiencing deregulation and is moving toward greater privatization.*

- *Canada's position will be best served by recognizing the need to ensure and improve market access for the future by addressing issues and trade barriers that are common to all service sectors and which have the potential to reduce services trade opportunities.*

- *The Mexican government, which is pursuing an outward toward looking economic growth strategy, has made great strides toward liberalizing its economy — but much progress must still be made to align the Mexican economy with those of Canada and the U.S.*

- *By negotiating cross-sectoral issues, at least equal to levels agreed upon in the FTA, Canadian service firms will be presented with an optimal environment in which to take advantage of new trading opportunities. They include:*

  - ⇨ *transparency;*
  - ⇨ *national treatment;*
  - ⇨ *right of establishment & commercial presence;*
  - ⇨ *non-discriminatory accreditation procedures; and*
  - ⇨ *cross-border mobility of personnel.*

- *The rules governing the right of establishment of foreign enterprise in Mexico continue to present some concerns from the Canadian perspective due to state regulation of ownership of many service industries in Mexico.*

- *Current requirements for the accreditation of foreign professionals in Mexico are unknown - this issue may present significant problems for Canadian service providers.*

- *The barriers to cross-border mobility of service producers still have the potential to create significant problems for Canadian services trade with Mexico.*

NAFTA

1. **Trading Relationship** 5 - 8

➡ **North American Trading Relationships**

2. **Services Trade: General Issues for the NAFTA** 9 - 17

- NAFTA

1. Trading Relationship

➡ **Canada's total trade in goods & services with Mexico is low**

♦ The U.S. has a substantial trading relationship with Mexico.

Trade in North America, 1989

		as a % of total exports (imports)	GNP (1990) ($US, billion)	Population (million)
Canada:	exports to U.S.	70.7	$ 581.0	26.7
	imports from U.S.	63.6		
	exports to Mexico	0.4		
	imports from Mexico	1.3		
Mexico:	exports to U.S.	63.3	$ 173.7	88.7
	imports from U.S.	67.0		
	exports to Canada	2.4		
	imports from Canada	1.8		
U.S.:	exports to Canada	21.5	$5,424.4	251.0
	imports from Canada	18.1		
	exports to Mexico	6.9		
	imports from Mexico	5.6		
NAFTA:			$6,179.1	366.4

Source: C.D. Howe Institute Commentary and Latin Finance

⇨ Two-way merchandise trade between Canada and Mexico was $2.4 billion in 1990 (U.S. two-way trade with Mexico reached $58.6 billion in 1990).

⇨ Shipments from Mexico ($1.75 B) represented about 1.3% of Canada's total imports.

- ♦ Canada is Mexico's sixth largest export market (1.9% of total exports; the greatest majority already enter Canada duty-free), and fifth ranking source of imports.

➡ Canada's trade in Services with Mexico is insignificant

- ⇨ Canada's Business Service trade with Mexico was estimated to be in an $11 million deficit position in 1988
- ⇨ This accounted for 0.23% of Canada's total Services trade deficit

Trade Relations Summary:

- ⇨ Canada is not a significant trading force in the Mexican economy:
  - on the other hand, the U.S. has a significant presence in Mexico.
- ⇨ Canada does not have easy access to Mexico (the U.S. does)
  - geographically,
  - by air or sea transport.
- ⇨ Spanish is not as dominant a language in Canada as it is in the U.S.

Conclusions:

- **a NAFTA** is expected to have **little immediate impact** on Canada due to:
  - distant physical location;
  - language differences; and
  - current lack of presence of Canadian industry.
- The bulk of trade opportunities arising from NAFTA will flow to the U.S.
- Canadian industry can expect the bulk of its opportunities to arise in specialized niche markets.

- A number of Mexico's domestic problems may offer a number of **opportunities for Canadian service industries,**
  - especially in the economic infrastructure industries.
- Even though little immediate benefit is expected to accrue to Canada, negotiation of the NAFTA <u>cannot</u> be at the expense of the gains achieved in the FTA with the U.S.
- The FTA, between two countries with similar trade regimes and relatively unimpeded services trade, provided for a standstill in existing trade measures and set out obligations for each country to prevent future protectionist measures affecting services trade.
- Since the Mexican service economy has been significantly less open than those of the U.S. and Canada, the NAFTA must make provisions for the liberalization of the Mexican economy to levels comparable with those in the U.S. and Canada.

Conclusion:

Negotiating a NAFTA should be forward-looking, building on, and extending, successes achieved through the FTA.

- NAFTA

2. Services Trade: General Issues for the NAFTA

- Given the small volume of Canadian services exports and the level of Canadian direct investment in Mexico, few Canadian firms have yet to become established in Mexico — therefore, it is far too early to negotiate on a sector-specific basis.
- Mexican restrictions to services trade are general rather than specific.
- Our approach to negotiating a NAFTA should be one which addresses cross-sectoral issues:

  a. ⇨ transparency;

  b. ⇨ national treatment;

  c. ⇨ right of establishment & commercial presence;

  d. ⇨ non-discriminatory accreditation procedures; and

  e. ⇨ cross-border mobility of personnel.

The cornerstone of Canada's "trade in services" position must be non-discrimination, interpreted in its broadest sense.

Simply stated, this position argues that a Canadian bank, consultant or insurance company, for example, should have the right to establish a commercial presence in any other country (i.e. Mexico), and, once there, the company should be treated no differently from national suppliers of the same service and its operation should be governed by laws and regulations that are clear and unambiguous.

- NAFTA

➡ 2. Services Trade: General Issues for the NAFTA

a. ⇨ Transparency in establishing operating guidelines

- *Government measures, laws and regulations affecting service industries must be developed and maintained in a clear and predictable manner.*

- *Information should be published and readily-accessible to all interested parties on an equal basis.*

In the FTA, the U.S. and Canada have agreed to make publicly available all laws and regulations relating to services trade so that firms who may be affected will have an opportunity to make their views known. Such transparency will enable foreign firms to participate with domestic firms in the regulatory process.

In Mexico, general economic reform and liberalization have been ongoing since the mid-1980's. Despite recent improvements, difficulties still exist. With entry into the GATT, however, the way in which the Mexican government conducts business is more in line with the philosophy of the GATT.

The scope for operations which exist (i.e. 2/3 of the economy is now open for 100% foreign ownership, other sectors require joint venture participation with nationals) and how the ground rules have changed are now relatively clear to foreign firms who wish to enter the Mexican services market. Economic adjustment to an "export-oriented growth model" is by no means complete but numerous changes have occurred in the economy. For example, firms may invest directly in well-specified sectors of the Mexican economy with much less red tape than was encountered in the past. Investment criteria are well-documented and numerous service industries have been completely declassified (100% foreign ownership potential). Now, only an approval is required.

The major problem that still remains is the breadth of government participation in the economy and the ownership constraints on foreign firms — tax reform appears to have been well-documented and beneficial to business — on the other hand, stiff environmental regulations which have existed for a number of years have been ineffective due to intermittent enforcement.

Transparency provisions for the establishment and day-to-day operations of business, while more clearly in the open as a result of deregulations, privatizations and increased openness to FDI, apply to only two-thirds of the economy. Unlike both Canada and the U.S., Mexico is not governed by an explicit competition policy framework. Uncertainty in the enforcement of laws and regulations persists, due to administrative procedures witnessed in the past. The degree to which foreign firms will be permitted to participate in shaping further reform in regulated sectors is unknown.

In addition, some feeling exists that the Mexican government could quickly reinstate measures or anti-competitive changes that would once again make Mexico a less than desirable place in which to do business.

Conclusion: *Transparency provision should be a part of the NAFTA:*

- *The issue of transparency, as it applies to the NAFTA, the international trade of services and the Mexican service economy, has become one of diminished concern.*

- NAFTA

➡ 2. Services Trade: General Issues for the NAFTA

b. ⇨ Right of establishment & commercial presence

- *Allows foreign investors to establish branches, agencies, subsidiaries or representative offices.*

Establishing a physical presence in the foreign country may not only be the preferred method of providing a service but a necessary condition for doing so (i.e. retailing and wholesaling). Some form of direct investment will generally be required.

Mexico has recently liberalized foreign direct investment regulations in some 2/3 of the economy, yet numerous service industries are still either subject to ownership restrictions of foreign ownership is totally prohibited. However, like both Canada and the U.S., Mexico deems certain sectors closed to foreign ownership due to national interests, hence precluding competition from foreign service firms.

Economic liberalization after a number of decades of restrictive government guidance and control does not necessarily move smoothly in all sectors at the same time. Consequently, new opportunities which present themselves in one sector may be inhibited by rigidities that remain in other sectors. For example, franchisers, who have now been given a significant opportunity in Mexico due to changes in technology transfer rules, are seeing this opportunity impaired because Mexican banks focus on hard assets which may be minimal for many franchises.

Linked to the right of establishment and commercial presence is the right to sell across **the border** without establishing a local commercial presence to conduct business. Such requirements protect local firms from foreign competition across the border. Mexican customs and immigration continue to be very unaccommodating when processing temporary entry of business travellers, yet labour laws are relatively clear on the extent of participation of foreign personnel.

The right of establishment is well-defined yet restrictive in terms of which service sectors are open for business. Regulation, in turn, determines the allowable degree of FDI. Merger and acquisition (hence FDI) is governed by industry classification. Mexico does not have any specific competition policy governing monopoly combinations, price fixing, resale price maintenance and merger. Strong economic growth leading to more intense domestic rivalry could strain the ability of constitutional provisions to guard against restrictive trade practises, thus further limiting foreign competition.

Conclusions: *The right of establishment and commercial presence should be a part of the NAFTA:*

- *Significant deregulation, privatization and changes to FDI rules have made the right of establishment permissible and relatively unencumbered in a growing segment of the Mexican economy. However, a large number of service sectors remain classified thus excluding foreign competition. Negotiating the right for greater foreign participation in the service economy of Mexico is still a major objective.*

- NAFTA

➡ 2. Services Trade: General Issues for the NAFTA

c. ⇨ National treatment

- *Once a service and its provider have entered another country, they should receive treatment identical to that given to domestic suppliers; countries should not discriminate between suppliers of the same service from different countries within the free trade area.*

The national treatment clause in the U.S./Canada FTA assures that any new laws or regulations will treat the service provider from the other country no less favourably than the domestic provider of the same service. Such a provision promotes stability and predictability in the countries belonging to the agreement, and firms can plan for the future without the threat of new discriminatory regulations.

Nevertheless, direct acquisition is guided by review at a certain threshold and certain sectors, both in the U.S. (i.e. radio wave telecommunications and transportation) and Canada (i.e. banking and transportation), are exempt from the agreement. That is, all three countries, including Mexico, maintain restrictions on foreign ownership in strategic sectors for reasons related to the economy, culture and national security.

The treatment of foreign firms involved in services trade with Mexico is improving, yet numerous policies still exist which give preference to domestic firms. While privatization has moved at a relatively fast pace, ownership restrictions remain in many industries, thus minimizing foreign participation. Licensing, restrictive labour movement, joint venture requirements and environmental standards are only a few of the Mexican policies which continue to affect foreign businesses adversely.

The integrity of the Mexican government, the legal system and enforcement of policies and current regulations remains an element of uncertainty.

Conclusions: *It is difficult to forecast how relationships between the Mexican government and foreign firms will evolve; preferential treatment of domestic firms as far as obtaining government contracts may persist. It appears less likely that special treatment as far as laws and regulations will continue. No tax holidays are offered to either foreign or domestic firms but some favourable industrial investment incentives (e.g. depreciation allowances) are still available.*

Therefore, national treatment should be part of the NAFTA and, with few exceptions, should not prove contentious.

- NAFTA

➡ 2. Services Trade: General Issues for the NAFTA

d. ⇨ Non-discriminatory accreditation procedures

Are important because licensing requirements can be used to restrict admission, regulate performance and act as unjustifiable barriers to accreditation by foreign applicants.

Accreditation varies from state to state in the U.S. and from province to province in Canada. In the U.S., this has caused some artificial barriers to interstate reciprocity (parallel to state licensing requirements are, for example, the capitalization requirements of insurance firms). The situation is much the same in Canada.

The FTA, through the national treatment clause, is becoming the vehicle which is facilitating the imposition of some uniformity, not only within each country, but between the two countries (e.g. accountants and architects). Nevertheless, progress is slow.

A related concern regards technical standards, testing facilities and certification bodies. Progress towards greater compatibility between the U.S. and Canada is ongoing.

The state of the licensing requirements for professionals and other service sector employees wishing to work in Mexico requires further research. Licensing impediments, if real and not explicitly addressed, can present a major obstacle for professional individuals wishing to work in Mexico.

Conclusions: *The NAFTA would benefit from a clause regarding accreditation which parallels the FTA approach.*

- NAFTA

➡ 2. Services Trade: General Issues for the NAFTA

e. ⇨ Cross-border labour mobility (and the right to sell across the border)

is vital because the pure export of services can be difficult and trade often requires international labour mobility or some degree of direct investment or presence to deliver the services competitively in the foreign market.

Prior to the FTA, Canada and the U.S. permitted temporary entry for business purposes; however, the substance and application of the entry procedures differed between the two countries and were often cumbersome, time-consuming and a barrier to business travel across the border. The FTA made provisions for the free entry of individuals in a number of broad classes of business travellers — business visitors, traders and investors, intra-company transferees and certain professionals.

Mexico appears to have clearly defined categories for business travellers. On the other hand, federal labour laws appear to be quite onerous for working visas. Restrictive bonding and entry/exit requirements by Mexico customs prevent the efficient provision of services and the free flow and speedy delivery of goods. Excessively burdensome document requirements for temporary business travellers, investors and service providers pose an obstacle to doing business.

In addition, many Mexican companies feel that one of their principal operating problems is the serious shortage of skilled labour and management personnel, particularly middle and upper management.

Conclusions: *Well-defined immigration categories, reduced red tape and congestion at custom points, and skilled labour and management shortages in Mexico suggest that restrictions on the mobility of foreign labour will decline with time.*

However, a continuation of labour mobility problems may be expected for an adjustment period.

Mobility between Mexico and the rest of the world should be expected to be encumbered due to poor customs points services and reduced opportunities due to the continued regulation of service industries.

The movement of professional services personnel is expected to remain an issue due to accreditation asymmetries.

ADDENDUM

3. The Mexican Case 19 - 34

➡ Services Trade: Issues of Concern

4. The Mexican Service Economy 35 - 57

➡ Profile of the Mexican Service Sector and Opportunities for Canadian Industry

➡ The Mexican Service Economy

- NAFTA

3. The Mexican Case

➡ Services Trade: Issues of Concern

⇨ International trade in services almost always requires the service provider to invest directly in the importing country, consequently, foreign direct investment (FDI) may be the single most important factor regarding the trade in services.

- Liberalization of restrictive foreign investment policies began in 1985, but Mexico's Constitution still forbids foreign control of parts of the "national patrimony".
- By 1990, the standardization of FDI rules had begun to attract considerable foreign investment.
- Foreign investors, led by the U.S., favoured goods industries over services by a 2:1 ratio in 1990 (*Maquiladora* [manufacturing] establishments can be 100% foreign-owned).
  - These events have particular importance for telecommunications services, financial services utilities and land transportation.

Foreign Direct Investment

- In May, 1989 the Mexican government significantly relaxed its traditional tight control over foreign investors by removing much of the red tape involved in various legal and administrative mechanisms, reducing local content requirements, modifying ceilings on foreign equity and eliminating most import licences.

Foreign Direct Investment in Mexico, 1989
($US, millions)

Source	Flow of Investment		Stock of Investment	
U.S.	$1,733.3	72.2%	16,649.5	63.0%
Switzerland	171.0	7.1	855.3	3.2
West Germany	78.2	3.3	1,660.0	6.3
France	48.6	2.0	802.9	3.0
Netherlands & Belgium	44.4	1.8	261.9	1.0
Canada	44.5	1.9	353.4	1.3
U.K.	41.6	1.7	1,809.8	6.8
Spain	40.6	1.7	1,245.6	4.7
Japan	22.9	1.0	1,333.0	5.0
Others	176.1	7.4	1,476.3	5.6
Total	2,402.2	100.0	26,447.7	100.0

Source: C.D. Howe Institute Commentary

- The U.S. is the largest foreign investor in Mexico (and Canada) and accounts for $17 billion or 63% of FDI in Mexico.
    - Mexican investment in the U.S. is approximately $1 billion.
    - The stock of Canadian investments in Mexico totalled $US 372 million in 1989 and has grown by over 12.5% in the 1980's; in 1989 Canadian firms invested $US 37 million in Mexico and $US 50 million in 1990.
    - Some 9,000 foreign firms have investments in Mexico, an increase of about 2,000 in the last 5 years; most are from the U.S.
        - There are currently 214 Mexican companies with Canadian capital, of which 154 are minority-owned and 60 are majority-owned.

- American Express (U.S.), the 22nd largest corporation in Mexico, has made the largest foreign direct investment in the service sector in Mexico.
- Moore Corporation, through Moore Business Forms de Mexico, S.a. de C.V., is the largest Canadian company with a service sector presence in Mexico.

- Mexico accounted for only 1% of U.S. cross-border direct investment in 1987; this figure rose to 3.6% in 1988 and 4.3% in 1989.

U.S. Direct Investment in Mexico, 1984 & 1989
Major Service Sectors ($US, millions)

	1984	1989
Wholesale Trade	443	395
Banking	-3	0
Finance, Ins. & Real Estate (excl. Banks)	195	130
Services	-26	138
Total	34,598	7,079

Source: Investment Canada

Unclassified Industries

- Foreign investment regulations now require only a simple registration process for up to 100% foreign ownership of qualifying investments in roughly 2/3 of the economy —
  - to qualify:
    - the investment must not exceed $100 million;
    - funds must come entirely from abroad;
    - the project must be outside the industrial zones;
    - imports and exports must balance for the first three years;
    - the investment creates jobs and provides training, educational and personal development programs for workers; and
    - the investment must comply with existing environmental standards (these criteria are interpreted liberally: 94% of foreign investment applications were approved in 1989 and 100% during the first five months of 1990).

Classified Industries

- Restrictions on foreign investment apply.
- Investment regulations specify six categories of "classified" areas and apply to 141 activities:

1- Activities reserved to the state (11 activities)

- Mexico currently prohibits private investment — foreign and domestic, in:
    - generation and transmission of electric energy;
    - railroad transportation services;
    - telegraph and radio communications;
    - financial trusts & funds; and
    - a number of natural resource sectors.

2- Activities reserved exclusively for Mexicans (33 activities)

They are:
- radio and television;
- urban and interurban transportation on federal highways (including buses, taxis, cargo);
- air and sea transport;
- port management;
- public warehouses;
- gas distribution;
- brokerage and exchange houses;
- notary public services;
- credit unions;
- fixed income societies (mutual funds);
- social work societies; and
- forestry and fishing cooperatives.

- But foreign participation is permitted in gas distribution, domestic air, sea transportation and forestry, via a 20-year temporary trust.

3- Activities in which foreign investment is limited to 34%

- 4 mining activities

4- Activities in which foreign investment is limited to 40%

- 8 manufacturing activities

5- Activities in which foreign investment is limited to 49%

- 26 activities, including:
    - river, lake and harbour transportation services;
    - financial leasing;
    - telephone services;
    - retailing of firearms and ammunition;
    - insurance; and
    - finance leasing companies.

6- Activities in which foreign investment is permitted up to 100%, only with approval

- 58 activities, including:
    - educational services;
    - publishing;
    - most forms of construction;
    - legal services;
    - management of bus terminals, toll highways, international bridges;
    - management of air navigation and airports;
    - securities and investment consulting; and
    - bonding agencies.

⇨ A number of other economic and political factors will determine the future level of foreign investment in Mexico:

- high rate of inflation;
- competition for investment capital;
- high foreign debt (ability to repay);
- rate of capital repatriation;
- high interest rates (36% in 1990);
- unstable political climate;
- high rates (18% in 1990) of unemployment; and
- wage and price controls.

Hence the development of the service economy in Mexico as well.

- NAFTA

3. The Mexican Case

➡ Services Trade: Issues of Concern

⇨ Right of establishment

- Mexico has all the usual forms of business organization; foreign companies are generally subject to the same laws as local firms.

  ➢ **Foreign branches:** although a few companies have set them up, branches have disadvantages:

  - they cannot own real estate;
  - they cannot deduct payments to the parent companies for royalties, interest, fees or other services;
  - they are not well-regarded by the Mexican authorities;
  - establishing a branch takes more time and money than establishing a corporation; and
  - branch charters usually contain more restrictions than corporation charters.

  ➢ **Mergers and acquisitions**

  - Rules limiting acquisitions of local companies by foreign investors were relaxed in May, 1989, and no authorization is needed if the resulting foreign participation is less than 49%.

  - Acquisitions resulting in majority foreign ownership will require approval through May, 1992.

  - Through May, 1992, a foreign investor may acquire up to 100% interest in an existing company not engaged in a "classified" activity.

➢ Competition policy

- Mexico has no specific antitrust law although there are constitutional provisions against price fixing and other monopolistic practices.
- Mexico has no specific legislation covering mergers.
- There are no regulations regarding resale-price maintenance.

➢ Local content requirements

- Local content requirements are being de-emphasized, with export requirements becoming far more important.
- Mexico's entry into GATT calls for no discrimination between local and foreign content.
- It would appear that this issue is more product-oriented.
- Local content is still used to determine eligibility for public-sector sales put to bid.
- 50% domestic content is considered Mexican for this purpose.

➢ Mandatory membership

- Every business in Mexico must belong to at least one of the many local chambers of commerce and industry; the cost is usually small and the obligations limited.

3. The Mexican Case

➡ Services Trade: Issues of Concern

⇨ Intellectual property

- Mexico's restrictive intellectual property legislation is undergoing significant modifications that should provide stronger protection for technology and trade secrets; Mexico has begun to introduce new regulations to strengthen intellectual property protection.
- New technology transfer regulations were published in Jan. 1990.
- A new law governing intellectual property (the law of Promotion and Protection of Industrial Property) was passed by Mexico's Senate in May 1991 (the law must still be approved by the Chamber of Deputies).
- **Patents of invention or improvement** last for 14 years and cannot be renewed.
  - The new law is expected to extend the term for patents from 14 years to 20 years from the filing date.
  - It may also authorize patents in areas not previously permitted; at present, companies operating in sectors without product patents may apply for inventor's certificates which provide for royalties but also make the technology available to all who want it.
  - The new law may also increase transitory protection for products and processes registered outside Mexico that have not been registered in Mexico within the one-year period provided for under the World Intellectual Property Organization (Paris) Convention.
  - It is likely to limit compulsory licensing to products for which a critical shortage exists, or to cases of flagrant abuse in the production or commercialization of a patent.

- **Trademarks:** the new law is expected to lengthen the initial term to a ten-year renewable period, up from the current five-year renewable period, as long as marks are commercially used; it should also permit greater variations in the use and exploitation of a trademark without the loss of protection.

    - Right is established through use and marks not put to use within three years are voided.

- **Trade secrets:** consist of confidential physical information of industrial application (see piracy below).

    - Protection of industrial secrets has been expanded for a period of up to 10 years; technical knowledge or "know-how" has been included.

    - The Mexican Senate has modified the law to limit the very broad definition provided in the draft version of the law.

- **Industrial designs and models:** the new legislation grants protection for a duration of 15 years (currently seven years); the application procedure is the same as for patents.

- **Franchising**

    - Once looked upon with disfavour, the new Transfer of Technology law specifically deals with franchise agreements for the first time and reflects the present government's belief that franchising may have significant benefits for Mexico; it removes the government from a supervisory role to an advisory role.

        - A provision clearly establishing the conditions relating to franchises has been introduced; regulations list permissible and prohibited contract provisions and also allow registration of agreements containing prohibited provisions if the agreement benefits Mexico in one of nine special ways.

- **Franchise agreements** have a maximum duration of 10 years.

- **Licensing**

  - 1990 technology transfer regulations make the approval process virtually automatic if a contract does any of the following:

    - creates new permanent jobs;
    - improves the technical skills of employees;
    - provides access to new export markets;
    - allows for the manufacture of new products in Mexico that replace imports;
    - improves the balance of payments;
    - lowers unit production costs;
    - develops local suppliers;
    - uses nonpolluting technologies; and
    - establishes or expands local R&D.

- **Application Fees**

  - **Patent fees** are subject to periodic adjustment and apply to:

    - examinations for novelty use;
    - reconsideration of a negative response;
    - review of application or completion of missing information;
    - expedition of titles; transfer, modification of contract or change of name;
    - a schedule of rising annual fees applies to patents granted.

  - **Inventor's certificate fees** are payable for application, modification of contract, examination of novelty, transfer, document replacement or submission of additional information and for transferral of patent application to inventor's certificate information.

- **Trademarks fees** are based on the number of products covered; there are also fees for the recognition of prior rights, verification of use, renewal (rates vary depending on the class of the mark), transfer, modification of contract or change of name.

- **Industrial designs and models** application fees vary according to the number of rights granted; there are also fees for the initial expedition of title; annual coverage; transfer, modification of contract or change of name; examination of novelty; and review of application.

- **Royalty and Fee Patterns**

  - 1990 technology-transfer regulations liberalized the rules governing royalty payments and fees charged for the use of patents, trademarks and tradenames and for services or technical assistance rendered.

  - Royalty payments may be negotiated freely between the contracting parties (percentage ceilings have been eliminated).

  - Under previous rules, the government often required companies to make substantial contributions to domestic R&D.

- **Piracy**

  - Legal red tape and corruption have in the past made it difficult to halt pirate operations (the current law provides pirates with two to six years in prison and goods and services may be seized at the time an initial complaint is filed).

  - Possible pirates are pursued under Mexico's tough copyright laws (enforced by the Secretariat of Public Education); this approach has proven successful against videocassette and software pirate (Mexico is also a signatory to the Universal Bern Convention on Copyrights and to the Ley de Derechos de Autor).

➢ Corporate Taxation

- A sweeping tax package including full implementation of the new tax law was introduced in Jan. 1989 — two years ahead of schedule.
- Income generated by branches or agencies of foreign firms is subject to the same federal tax as corporations:
  - 36% for 1990 and 35% for 1991.
- The costs & expenses relating to income vary arbitrarily, i.e. rental expenses of luxury autos are deductible but restaurant and bar entertainment are not; legitimate promotion and travel expenses are also deductible.
- Technically, corporations not domiciled in Mexico are taxed only on their Mexican-source income.
- The source of income from services rendered in Mexico and income from Mexican branches of foreign corporations is always deemed to be Mexican; the same holds true for interest payments, royalties etc. when one party to the contract resides in Mexico.

• Intellectual Property Taxation

- Royalties and patents are taxed at a rate of 40%.
- Copyright and technical assistance are taxed at a rate of 15%.
- Payments abroad for technical assistance, know-how, use of models, plans, formulas, and similar technology transfer are subject to a 15% withholding tax; royalties paid to foreign licensors of patents, trademarks and trade names without the rendering of technical assistance are charged a withholding tax of 36%.

➢ Turnover, Sales and Excise Taxes

- A value-added tax applies to both goods and services at various rates:
  - 15% for most goods;
  - 6% for certain food items;
  - 20% for luxury goods;
  - medicines, doctor's services, land and residential buildings, books and periodicals, share transfers, and such services as public transportation and education are exempt;
  - exports are exempt as are supplies for maquiladoras;
  - a special tax on production and services is charged to manufacturers and wholesalers of certain goods, including soft drinks, alcoholic beverages, tobacco and gasoline; levied on the different production and sales stages, it is not charged to the consumer; the tax varies by product, from 3% on life insurance to 160.3% on cigarettes; and
- Other taxes include 1% levies payable by the employer and the employee on total monthly salaries, a 5% payroll to support worker housing and an export tax on certain commodities, including oil.

➢ Incentives

- The Mexican government has curtailed the use of both tax and non-tax investment incentives in recent years.
- The remaining incentives are designed to encourage the growth of small- and medium-sized Mexican companies, stimulate export production, expand the tourist industry and develop the northern border with the U.S.
- No foreign majority-owned companies are eligible for regional incentives.
- Mexico now offers no tax holidays for local or foreign investors; favourable depreciation is available on certain assets to companies located outside the three major metropolitan areas.
- While no direct incentive exists, new regulations for the computer industry encourage R&D; regulations provide for duty-free imports of finished computer parts and accessories up to 80% of the sum of local value-added plant investment and two times the amount spent on R&D.

- Under Bacomext's pre-export financing program for manufacturing and services, developing companies (classified as those with export sales of less than $2 million per annum, can obtain financing of 100% of the f.o.b. price.

- Small- and medium-sized firms are being assisted, especially in the tourism and tourism-related sectors (i.e. food and beverage facilities, travel agencies, car rental and guide offices) through favourable rate and repayment loans.

➢ Labour Mobility

- At least 90% of a firm's skilled and unskilled workers must be Mexican nationals (Section I of the Federal Labour Law).

- Section III of the law requires that employers favour Mexicans over foreigners and unionized personnel over nonunionized employees.

- A special provision permits temporary employment of foreign technicians (up to 10%) if firms can prove that skilled workers are not available locally (does not apply to managers, directors, or other key officers who must secure special immigration permits).

- Foreigners may enter Mexico with either non-immigrant or immigrant status.

- **Three categories of immigrants are of interest to foreign investors:**

  - *Cargos de confianza* may be obtained by foreigners who fill key executive positions or other positions of responsibility in established corporations;

  - *Inversionista* status may be obtained by foreigners who invest in industrial activities that contribute to the economic and social development of the country; and

  - *Tecnico* status may be granted to people who undertake research, technical or other specialized activities for which no qualified residents are available.

- Mexico also has provisions for scientists, professionals and people with independent income.

- Labour training legislation (1978) obligates companies to set up training programs for all workers, but the requirements are hazy.

- Calls for training at all levels, from top management down to the least skilled worker; training is to be conducted on company time and may be in-house or in conjunction with registered instructors or institutions; excessive red tape has reduced the program's impact.

- Cost of training is tax deductible.

- Several executive-recruiting services are available for companies seeking to contact top managers; recruitment of skilled labour is done through unions, newspaper advertisement, employment agencies or industrial chambers; unskilled labour is usually recruited at the factory gate, through unions or by word-of-mouth.

➢ Environmental Law

- Various approvals must be obtained before any actual building takes place.

  - Tougher environmental rules and enforcement are expected; the ecology and Urban Development Secretariat temporarily closed 32 plants in the Mexico City area, mostly owned domestically, but some are MNC's.

➢ Privatization

- In 1985, the Mexican government began to privatize, and while some 800 entities were divested, over 300 remain.

- In the service sector, Mexico has stated that CFE, the publicly owned electricity company, is not for sale.

- In Feb. 1991, it was announced that Mexico's largest commercial bank, Banamex, will be privatized along with three smaller banks.

- The Mexican Postal System agreed to permit a U.S. firm, Mail Boxes, to own and operate 80 privately run post offices in Mexico City and another 420 around the country (excluding mail delivery, the firm will sell stamps, receive letters, rent post office boxes and take over all express mail service).

➢ Infrastructure

- Almost all elements of the Mexican infrastructure are poorly developed, including:
    - the system of land transportation;
    - ports and water transportation;
    - telecommunications; and
    - utilities, power and sewer.

4. - NAFTA

The Mexican Service Economy

➡ **Profile of the Mexican Service Sector and Opportunities for Canadian Industry**

MEXICO: The Structure of the Economy

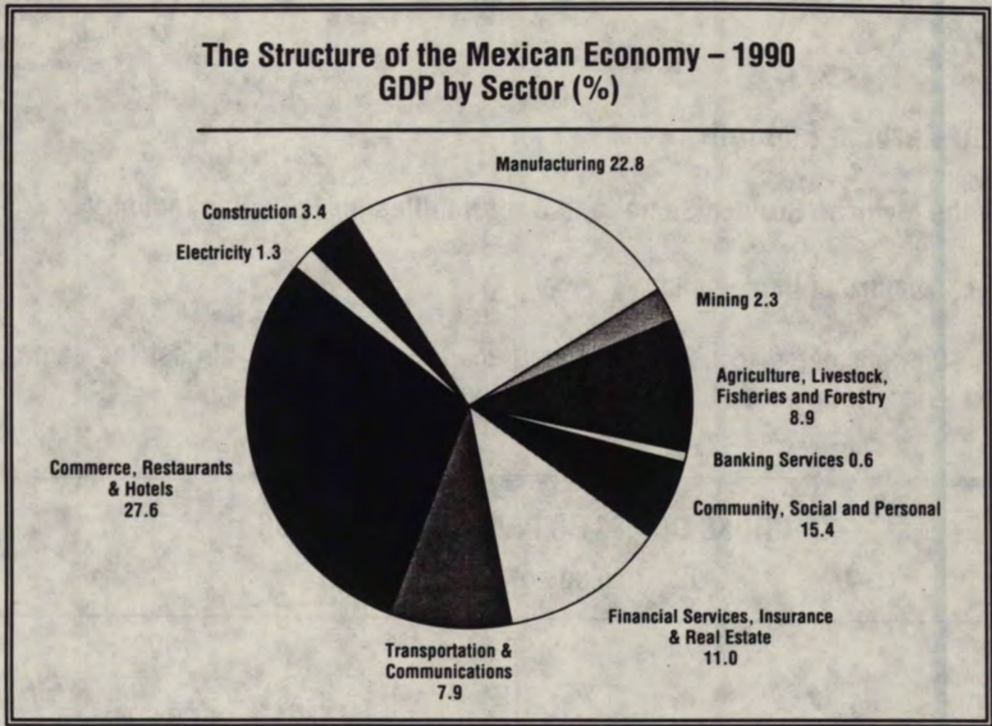
- Mexico is still considered to be a developing economy, yet it has almost the same share of services in its economy as do both Canada and the U.S.

GROSS DOMESTIC PRODUCT BY SECTOR

GDP - (billions of current Pesos)

	1989	%	1990	%
Total GDP	516,710	100	668,691	100
Agriculture, Livestock, Fisheries and Forestry	44,021	8.55	59,271	8.9
Mining (incl. Petroleum)	13,621	2.6	15,501	2.3
Manufacturing	125,875	24.4	152,794	22.8
Construction	18,379	3.6	22,457	3.4
Electricity	6,742	1.3	8,992	1.3
Commerce, Restaurants & Hotels	139,131	26.9	184,260	27.6
Transportation & Communications	38,659	7.5	52,931	7.9
Financial Services, Insurance & Real Estate	52,645	10.2	73,543	11.0
Community, Social and Personal	80,643	15.6	102,894	15.4
Banking Services (imputed)	3,006	0.6	3,952	0.6

Source: Banco de Mexico, The Mexican Economy 1991



Figure

Service Sector Share of GDP
(including electricity)

CANADA	66.0
U.S.	68.0
MEXICO	63.8

MEXICO: The Performance of the Economy

⇨ Mexico experienced real economic growth of only 0.80% in the 1980-87 period. GDP reached P890 trillion.

- In 1989, real GDP grew by 3.1% and preliminary figures show that GDP grew by 3.9% in 1990.

- The most significant factors influencing the favourable results in 1990 were:

  - a higher level of economic activity, employment and investment;
  - restructuring of Mexico's external debt;
  - divestitures and privatizations; and
  - higher than anticipated oil export prices.

- **Inflation**

  - The inflation rate reached 29.9% in Dec. 1990, significantly higher than the 19.7% recorded a year earlier.

ECONOMIC OUTLOOK: 1991

- Foreign investment, which rose 13.4% in 1990, is expected to rise a further 10% in 1991.

  - Foreign direct investment is expected to reach $US 4-5 billion in 1991.

- Mexico's GDP is expected to grow by 3.5-4% in 1991, fuelled by increased investment and consumer spending: growth in 1990 was a strong 3.9%.

  - Manufacturing: growth is forecast at 4-5% in 1991.

  - Construction: the construction sector is expected to undergo the strongest growth; 7% growth is predicted in 1991 after the 7.7% growth in 1990.

SERVICES

⇨ The broadly defined service economy of Mexico grew at the same rate as the economy as a whole in the 1980-87 period.

- In 1989, the service economy made up 62.8% of the economy.
- The Service sector share of GDP in the economy is as follows:

Mexico's Service Economy

Sector, GDP (millions, Pesos)	1987	1988	1989	share (1989)
Total Services	3,014.7	3,058.11	3,141.1	62.8%
Retail Trade, Restaurants and Hotels	1,233.0	1,248.1	1,289.6	25.8
Transportation, Storage and Communications	303.7	312.1	331.2	6.6
Financial Services, Insurance and Real Estate	518.4	532.4	545.7	10.9
Social and Personal Services	893.8	897.6	905.7	18.1
Banking	65.8	67.9	68.9	1.4
Total	4,802.4	4,857.2	5,000.3	n/a

Source: Banco Nacional de Mexico

⇨ Sector Growth 1990

- **Commercial sector** output grew 3.2% in 1990.
- **Restaurant sector** output rose 6.6% largely due to the increase in tourism.
  - Large restaurant chains affected substantial investments in new units in the main cities and tourist resorts.
- **Hotel sector activity recorded a 12.5% increase in 1990.**

- **Financial services and real estate leasing** increased 2.5%.
  - The former grew 3.3% due to the growth of financial resources of credit institutions etc.
- **Educational services grew 1.9% during 1990.**
  - Public sector services rose by 1.6% while private sector services increased by 3.7%.
- **Medical services recorded 2.1% growth.**
  - Public sector health services increased by 1.7% due to wider coverage by preventative and care programs for the poor.
  - Private sector medical services increased 2.8%.
- **Construction** - the sector grew by 7.7% in 1990.
- **Electricity, gas & water** - the sector grew by 5.2%.

FORECAST

⇨ Services growth is forecast at 3.5%, marginally higher than the 1990 figure of 3.2%.

- The best performance should be in the transportation and communications sector — 6.3% in 1990.
- Retailing, restaurants and hotels are also expected to do well — 3.9% in 1990.

EMPLOYMENT

⇨ The employment share in the broad service economy of Mexico was over 51.5% in 1986.

- Employment growth in the 1980-87 period was 1.1%.
- The broadly defined service sector grew faster — 1.7% in the period.
- The share of employment in the service economy in 1989 was estimated as follows:

Mexico — Economically Active Population by Sector

Sector	Employment, 000	Share (1989)
Services	25,570	12
Transportation	3,110	4
Trade	2,400	9
Undefined Activities	7,650	30
Transformation, Construction and Electricity	4,830	19
Extractives	550	2
Agriculture	5,980	24

Source: Banco Nacional de Mexico

Industrial Employment and Economic Establishments

⇨ According to the 1989 Census (which was reported to have recorded 96% of all economic activity in Mexico) carried out by the National Institute for Statistics, non-agricultural employment in Mexico was divided according to the chart which follows.

- The services share of employment, excluding construction but including electricity and water was 71.2%.
- The service sector accounted for 90% of business establishments.

Non-Agricultural Employment by Sector

Sector	Establishments	Employment
Fishing and Mining	1,637	148,881
Manufacturing	162,966	2,677,229
Electricity and Water	2,339	89,239
Construction	7,872	232,273
Commerce	913,730	2,374,401
Transportation and Communications	16,277	332,951
Services (excl. Financial)	607,271	4,513,357
Financial Services	9,789	239,665
Total	1,721,841	10,601,996

- Significant differences exist in the structure of employment between Canada, the U.S. and Mexico.
  - Major differences in professional, technical, administration, executive and management as well as service industries may signal opportunities for Canadians in the future.

Employment by Status — a Comparison, 1987 (% of total)

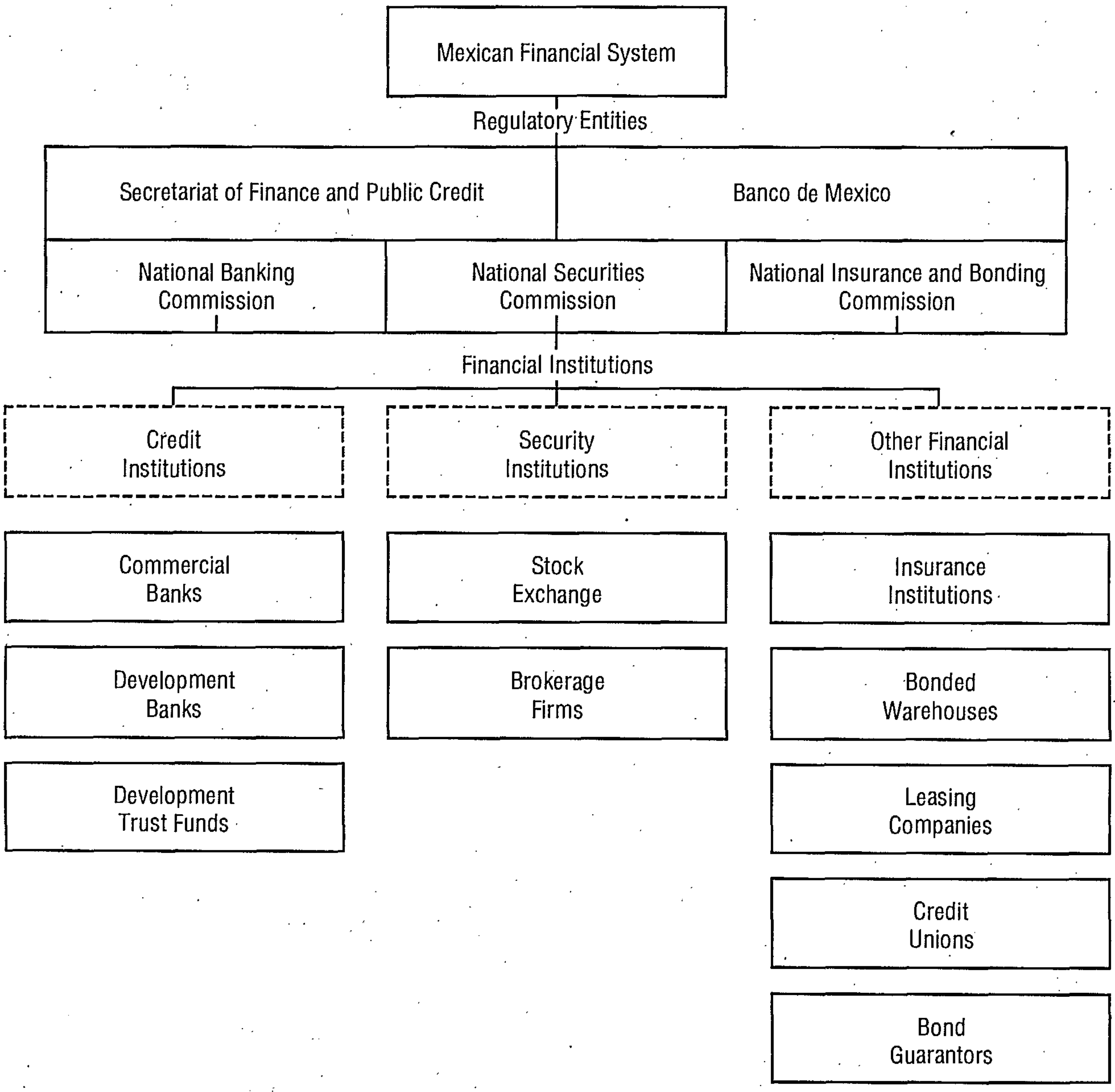
Status	Mexico	Canada	U.S.
Professional & Technical	7.3	16.0	14.9
Admin., Executive, Managerial	1.0	11.5	11.3
Clerical	9.2	16.4	15.7
Sales	7.3	9.3	11.6
Service Industries	8.3	13.6	13.4
Agriculture & Fishing	25.0	5.4	3.1
Production & Related	25.6	27.1	27.8
Others	15.7	—	—

Source: Statistics Canada, U.S. Dept. of Commerce and INEGI International Review

The Mexican Service Economy

➡ Industry Profiles of the Mexican Service Sector

The Structure of the Mexican Financial System



➡ The Mexican Service Economy

Banking

- **In 1982, Mexican banks were nationalized and foreign banks were permitted to maintain representational offices only; consolidations in the private commercial banking system reduced the number of institutions from 60 in 1982 to 19 in 1988.**

    - Representational offices of foreign banks serve primarily to facilitate the introduction of banking services that can be obtained outside Mexico from foreign banks.

    - Foreign banks were prohibited from taking deposits or making loans in Mexico and from competitively providing a full range of financial services and products directly to Mexican individuals and entities.

    - Citibank is the only privately owned foreign commercial bank with a government charter that allows it to accept branch deposits; it has a network of five branch offices.

    - At the end of 1989, 27 U.S. banks and 60 other foreign banks maintained representational offices in Mexico.

- **Significant changes are now underway in the Mexican financial services market but there appears to be limited opportunity for the Canadian industry.**

    - In Aug. 1990, the Mexican government announced the formation of a committee to oversee the sale of most of Mexico's 18 commercial banks which had been majority-owned (66%) by the government since 1982; as of July 1, 1991, two banks, Multibanco Mercantil de Mexico and Panbais, sold for $203 million and $182 million respectively (or about three times book value); banks in Mexico offer banking, brokerage and insurance services.

    - The commercial banking system currently consists of:

        - 6 nationwide banking institutions;
        - 5 regional banks; and
        - 8 multiregional entities.

    - At the end of 1990 commercial banks had 4,487 domestic branches, 222 foreign branches and 17 representative offices abroad.

- 3 of the 18 Mexican banks account for 80% of Mexican banks' total assets; the market capitalization of the banking system is about $7 billion.

- Mexican investors will continue to hold controlling interest; direct or indirect **foreign participation will be limited to 30%** of a Mexican bank or financial services' holding company.

- Financial services' share of Mexico's GDP in 1989 averaged 3.26% — up significantly from 1.85% in 1983; growth stemmed primarily from Mexico's progress in revitalizing the financial services industry through privatization, liberalizing foreign investment laws and restructuring foreign debt.

  - The financial system is complemented by:

    - 27 insurance institutions;
    - 142 credit unions;
    - 26 leasing companies;
    - 14 bonding guarantors; and
    - 17 bonded warehouse companies.

- While the Mexican government's divestiture of the banks and change in ownership laws are considered to be a significant step in liberalizing the banking system, **the ability of foreign banks to establish and maintain operations** and provide capital to Mexican and foreign business for investment in Mexico **will continue to be restricted** unless all barriers to entry are removed.

Non-Bank Financial Intermediaries

- The Secretariat of Finance and Public Credit is empowered to grant concessions for the establishment and operation of brokerage firms.

- The National Securities Commission is the agency in charge of inspection and surveillance of operations in the Mexican Stock Exchange, brokerage firms, stock exchange specialists and dealer agents.

Brokerage Firms

- Brokerage firms provide four basic services:

    - investment banking;
    - the principal in the purchase and sale of securities;
    - act as agents for other investors; and
    - mutual funds management.

- They are permitted to form financial groups under conditions similar to those for commercial banks, but may not hold an interest in commercial banks, insurance or bonding companies.

- In 1990, there were 25 brokerage firms with 208 offices employing 9,451 people; their aggregate capital totalled $1.25 billion.

Bonded Warehousing

- 17 bonded warehouse companies, only one of which is government-owned.

- Volume of merchandise stored totalled 4.7 million tons (to Sept. 1990) with a value of 3.1 trillion pesos.

Insurance

- The Mexican insurance industry has been effectively **closed to foreign investment** since 1935.
  - Despite a new insurance law aimed at revitalizing the market via privatization and increased competition, the Mexican insurance industry remains undercapitalized, technologically weak and relatively inefficient.

- The Mexican insurance industry consists of 39 firms, two of which are government-owned but slated for privatization.
  - Seven companies, including the 2 state-owned firms, control 80% of the market.
  - Mexican insurance firms tend to be small with limited capital bases and reserves and many simply reinsure almost all of their business.
  - Total premium volume of the Mexican insurance market is approximately $2.3 billion (7.7 trillion pesos in 1990) or just over 1% of GDP.
    - premium structure:

life insurance	-	36.5%
automobile insurance	-	28.6%
maritime & transport	-	7.2%

- Foreign trade with Mexico in insurance is low due primarily to restrictions on the establishment of foreign firms and restrictions on Mexican firms that limit or prohibit the buying of insurance outside of Mexico.
  - **Four major non-tariff barriers:**

    1- The most significant is the limitation to only 15% equity for foreign firms in joint ventures with a Mexican firm.

    2- Mexican insurers are required to place at least 50% of their reinsurance in Mexico; this denies foreign reinsurance business that would tend to flow outward and to take advantage of the greater efficiency and lower premiums in foreign reinsurance markets.

3- Mexican law requires that import and export insurance (e.g. marine insurance) purchased by Mexican buyers or sellers of all shipped goods be placed in Mexico.

4- Both foreign and Mexican motor vehicle travellers crossing the border are often not covered by vehicular insurance for any losses or damages incurred; this has allowed small, inefficient providers of auto insurance to exist at border crossings in order to sell temporary policies that may not provide the coverage requested.

Transportation: Commercial Trucking Services

- The Mexican constitution prohibits foreigners from operating commercial vehicles in Mexico.
- In 1955, the Mexican government issued a decree establishing the legal basis for the operation of foreign motor carriers within Mexico's border area.
    - It has not been uniformly applied across the border and foreign motor carriers are effectively denied access to most areas of Mexico.

Infrastructure

- Mexico's transportation infrastructure has proved inadequate for handling the large increase of trade in recent years.
- Mexico's roads and highways are considered potentially dangerous.
- Only 8.5% of the few miles of primary roads are four-lane highways; curves are two times as tight as in the U.S.

Construction & Engineering Services

- Mexican law states that the federal government and state-owned enterprises must conduct an open bidding process for contracts concerning purchases, leases and the provision of services connected with goods.

    - However, due to a law which gives preference to Mexican providers of goods and services in order to promote national development, foreign construction firms (with a few exceptions) **have not operated in Mexico.**

- Construction services account for about **5% of Mexico's GDP.**

    - It was estimated that U.S. firms engaged in construction, engineering, architectural and mining services did $2 million worth of business in Mexico in 1989.

- In 1989, the Mexican government initiated a program to revitalize the construction sector by **privatizing most, if not all, industries.**

    - About 80% of the Mexican construction market is controlled by the 5 largest firms.

- Foreign construction and engineering firms face heavy regulation and protection of these sectors by government and Mexican regulations stating that firms who wish to do business on a regular basis must enter into joint ventures with Mexican firms.

    - Engineers trained and registered outside of Mexico may only practise in Mexico in a joint venture situation and only if they are highly specialized, technical or administrative personnel.

    - The number of such foreign personnel must not exceed 49% of the total technical staff.

- Construction opportunities in Mexico are currently reported to abound in the airport, highway, port and tourism areas .

Telecommunication & Information Services

- The growth and competitiveness of the Mexican telecommunications and information services industry has been constrained in the past due to restrictive regulations and to an outdated infrastructure.
  - This situation is about to change with the announced intention to privatize the Mexican telecommunications authority, Telephonos de Mexico (TELEMEX).
  - TELEMEX had profits of $773 million on revenues of $2.2 billion in 1989.
    - Telephone density in Mexico is estimated at 4.9 lines per 100 people (compared to 48 per 100 in the U.S.).
    - The cost of upgrading the Mexican telephone system has been estimated at $14 billion.
    - In Dec. 1990, the Mexican government announced it would sell TELEMEX for $1.76 billion to the consortium consisting of Southwestern Bell, France Telecom and Group Carso.
- Reorganization of government-owned enterprises in 1989 created TELECOM which combined the national telex network (TELENALES), the packet-switched data network (TELEPAC), the airline reservations services network (SERITEL) and INFONET, an electronic mail provider — it is expected that these services will be privatized in the future and that the government will become a regulator of these services.

- **Cellular Telephone Service**
  - In the next few years the market for cellular services is expected to grow to 400,000 subscribers and reach an estimated value of $600 million.
    - This type of telecommunications is likely to be less costly and quicker to put into place (it operates on radio frequencies rather than on copper or fibre optic cable) than a land-based telecommunications infrastructure.

  - Because foreign participation in telecommunications is limited to 49%, foreign cellular companies (including Bell Canada) have joined with local Mexican investors in these projects.
  - Twenty-year concessions for cellular telephone operations were awarded to eight groups in regions outside of Mexico City; investment by these groups is estimated at $250 million over the next three years.

INFORMATION SERVICES

- The Mexican information services industry is relatively small and the latest figures show revenues of $130 million in 1987.
- Software and data communications software are two industries that are relatively underdeveloped and would have a large growth potential.
  - Domestic software sales in Mexico increased at an average annual rate of 26%, from $59 million to $117 million between 1984-88, with imports representing 72% of total sales (the U.S. has 90% of the import market).
- Most of the trade between Mexico and the U.S. and between Mexico and Canada is in the form of basic telephone services.
  - Basic telephone services trade is governed by a series of bilateral operating agreements between countries.

Basic Telecommunications Infrastructure

	1985	1986	1987	1988
Telephones (millions)	7.3	7.7	8.2	8.6
Telephone Cables (000 kms)				
Long Distance	39	40	41	43
Urban	1,489	1,711	1,896	2,102
Radio Stations	887	898	915	1,000
T.V. Stations	430	442	512	554
Telex Service Connect Lines	23,319	23,916	24,916	24,621

Franchising

- Although the prospects for doing business through franchises changed with the new technology transfer rules, franchising is still relatively unknown in Mexico.
- Franchising was viewed negatively by government regulators who saw limited value in protecting foreign systems of business.
- Prior to the revision of the rules, franchise agreements were treated as technology agreements, burdened with requirements aimed primarily at hard technology transfers; royalties were limited, required supply clauses were prohibited and confidential information had little protection.

Obstacles remain:

- Some franchisers still believe that the new rules are administrative regulations which can be changed with a simple presidential decree.
- Obtaining local financing can also be difficult since Mexican banks focus on hard assets which are usually kept to a minimum in a typical franchise; equipment and commercial space is often leased, and inventory is kept to a minimum.

Suppliers: Hotel & Restaurant Equipment and Consulting Services

- Trade liberalization has meant the elimination of import permits for all but 325 of the total 11,960 tariff items; official import prices are no longer applicable; the maximum import duty has been lowered from a maximum 100% to 20%.
- The tourism industry has been given priority status by the Mexican government.
- Industry estimates indicate that the total investment in hotel and restaurant equipment in the next five years will total $800 million.
- Canada had a reported 2.2% import market share in 1989.
- Such events also present an opportunity for those firms engaged in design, quality control and new product introduction.

Mexico City: A Focus for the Problems Facing Mexico

Canada's service industries have not been motivated to enter Mexican markets in the past, nor has Mexico been an environment conducive to free market forces. Consequently, Canadian firms do not currently have a significant presence in the Mexican economy. Numerous changes have occurred in Mexico in the 1980's, changes that will permit foreign firms to conduct business more in a manner to which they are accustomed in their home markets.

Due in part to the overbearing influence of the government in the workings of the economy, social and economic conditions in Mexico have deteriorated over time. With the freeing up of market driven forces there is now some expectation that the worst of Mexico's problems will be corrected. Opportunities are being uncovered for foreign firms in Mexico and, through direct investment, joint ventures and specific aid packages, foreign firms have the potential to enter the market profitably.

A representative picture of the problems that exist in Mexico and the opportunities that await Canadian service sector firms is provided by the case of Mexico city. What follows is an incomplete picture of the predicament in which the city finds itself, a partial account of how it plans to rectify the situation, hence a number of direct examples of how some Canadian service sector industries might profit, as well as numerous indirect ideas for service industry participation.

The Problem:

- Mexico City is the largest city in the world with a metropolitan population of almost 20 million, which is growing at an annual rate of 4.4%.

- Such a large population (7,300 per km^2), the geographical setting (an earthquake-prone lake valley on a central plateau), poverty (minimum wage of $4 per day) and business environment (60,000 industrial plants) have stressed all aspects of the infrastructure, including:

    - transportation;
    - water supply and sewage;
    - housing; and
    - environment.

- In addition, Mexico City has an unstable foundation into which the city's buildings are steadily sinking.
- The social and economic predicament in which Mexico City finds itself has already opened doors for foreign firms offering assistance, aid and specialized solutions, especially since the introduction of political reforms in the country.

The Strategy:

- **Transportation Overhaul:**
  - The subway system, built by the French 20 years ago, is inadequate and fails to service the "new towns" (slums) in the Federal District of Mexico where the population is growing fastest.
  - Ancient and overcrowded bus system.
  - Most who can, 17% of the population, drive private automobiles.

  The Solution:

  - The electric subway lines will be extended from 140 km to 201 km over the next five years (through French tied aid).
  - A master public system plan is being devised to ensure that small vehicles servicing outlying areas feed into the larger subway and bus arteries.
  - Private operators will be granted concessions to run luxury bus services to attract the wealthier citizens to the public system.
  - These programs are being paid for through increased fares.

- **Water and Sewage Program:**
  - Mexico City is running out of water from its underground aquifer and in the central city much water is lost due to old and broken pipes.
  - Water consumption, which is significantly higher than European or Japanese standards, is subsidized.

The Solution:

- Recycling; 10-20 new sewage treatment plants are planned.
- Replacing all the old toilets (1.2 million) in the city — discharge will decline from 16-20 litres to 6 litres.
- These programs will be partially financed by water tariffs to corporate and recreational users (the costs for human consumption will not rise).

Air Pollution

The Solutions:

- To improve fuel efficiency and emissions control, new regulations are encouraging the substitution of gas for fuel oil, which has a high sulfur content.
  - Gas engines are being installed on 3,500 city buses and gas carburettors on 45,000 city cargo delivery trucks.
  - Ether is being added to gasoline to improve combustion efficiency.
- $1.5 billion is being spent on six new plants capable of producing unleaded gasolines and three plants that will desulfurize diesel and fuel oil.
- Emission control equipment will be installed in automobiles and factories, beginning with public transport vehicles and delivery trucks; catalytic converters will be required on all new automobiles sold in Mexico; factories must either relocate polluting processes outside of the city or install scrubbers and adopt cleaner technologies.
- These measures are to be financed through general city revenues and increased property tax.
- The Salinas government has budgeted $2.5 billion over several years for anti-pollution programs.
- The Japanese government has also agreed to an aid package of $786 million for fighting air pollution.

The Environment

- **The Problem:**

  - 90% of the original lakes in the Valley of Mexico have dried up and 75% of the first cover has been lost.

The Solution:

- Key properties have been expropriated to create permanent parkland within and around the city.
- A massive reforestation program will plant 1.5 million new trees in the city, and another 128 million trees will be planted in the surrounding valley over the next 4 years.
  - Some of the areas to be reforested are old lake sites or are lying on top of porous volcanic rock and will act as natural sponges for the aquifer beneath the city.

Sources:

United States International Trade Commission, Feb. 1991, *The Likely Impact on the United States of a Free Trade Agreement with Mexico*, USITC Publication 2353, USITC Washington D.C.

Business International Corporation, ILT Mexico, Sept. 1990.

ibid., Business Latin America.

Weinttraub, Sidney, 1990, *Transforming the Mexican Economy: The Salinas Sexenio,* National Planning Association, Washington D.C.

Financial Times, Wednesday May 8, 1991.

World Link, various.

Bank of Mexico, various and *The Mexican Economy 1991.*

National Institute for Statistics, Mexico, *Mexico: Economic and Social Information.*

Investment Canada, 1991, *The Opportunities and Challenges of North American Free Trade: A Canadian Perspective,* Working Paper No. 7.

Euromonitor Plc 1991, *International Marketing Data Statistics.*

Latin Finance, March 1991.

U.S. General Accounting Office, Report to the Chairman, Committee on Commerce, Science and Transportation, U.S. Senate, various, May 1991.