Session 3: Corporate Behavior

Mexican Development Strategy and U. S. Multinational Company[1)]

Yoichi Tajima

Ⅰ. Introduction

Since the Debt Crisis in 1982, Mexican Development Strategy has changed from Import Substitution Industrialization to Export-Oriented Industrialization and the economic policies were drastically liberalized. In this term, neo-liberal economic policy dominated over a protective policy. Foreign investment policy also has changed from regulation to promotion. The reason why Mexico changed the policy was that the Mexican government expected foreign direct investment to bring a package of economic effect: capital inflow for economic growth, export promotion, job creation, and technical innovation.

This paper will review this change in Mexican foreign investment policy and empirically evaluate the outcome of policy change using data on U.S. Direct Investment Abroad.

Ⅱ. Foreign Investment Policy Changes

Since the Debt Crisis, 1973 the Foreign Investment Policy[2)] that restrictedly regulated foreign investment gradually was liberalized and at last was renewed as the 1993 Foreign Investment Law. In the term of President De la Madrid, Foreign investment policy corresponded to a first-stage of Export-Oriented Industrialization. In the term of President Salinas, Mexico arrived at full-dress Export-Oriented Industrialization.

[1)] An earlier form of this article first appeared in the Ritsumeikan Kokusai Kenkyu. See Tajima (1997)
[2)] On the 1973 Foreign Investment Policy, see Poder Ejecutivo Fedral y Secretaría de Hacienda y Credito Publico (1973), GATT (1993).

a. 1973 Foreign Investment Policy

The following are the basic elements of the 1973 policy:

1. In the first article of 1973 Foreign Investment Law, the purpose of the law, as stated, was to " promote Mexican investment and regulate foreign investment to promote just and even development, and to strengthen economic independence of the state. " Second article of the law gave a definition of foreign direct investments[3)] as an investment by foreign legal person, foreign natural person, foreign economic unit without legal person, and Mexican Company majority owned by foreign investment or managed by foreigner without regard to tubular.

2. 1973 Foreign Investment law divides economic activities in Mexico into three areas: activity occupied by state, activity occupied by Mexican, activity permitted foreign investment to participate under certain investment rates.

3. 1973 Foreign Investment Law did not permit foreigner to own a majority in Mexican Company as a rule and the Law gave them to the severe regulation. One of the reasons for the regulation was "Mexicanization" to protect and foster Mexican national industry. This law, however, permitted a lot of exceptions. For instance, the National Commission of Foreign Investment (La Comisión Nacional de Inversiones Extranjeras) can increase or decrease the rate decided by prior item when it is useful to the Mexican Economy.

4. 1973 Foreign Investment Law stretched the law to suit a changeable purpose of development strategy[4))]. Although Mexican Development Strategy changed from Import Substitution to Export-Oriented, the 1973 Foreign Investment Law remained the fundamental law of foreign investment for 20 years until 1993 when the new foreign investment law took effect. We will measure the stretch of the 1973 Foreign Investment Law in each time from chrysalis to full-dress Export-Oriented Industrialization.

b. Foreign Investment Policy in term of De la Madrid

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3) Poder Ejecutivo Fedral y Secretaría de Hacienda y Credito Publico (1973), p. 5.

4) GATT (1993), p. 69.

National Development Plan 1983-1988 (Plan nacional de desarrollo 1983-1988) was proclaimed in the term of President De la Madrid. It represented a switch of Mexican Development Strategy from rigid Import Substitute Industrialization to Export-oriented Industrialization and selective Import Substitution. This plan pointed out, although the regal framework of 1973 Foreign Investment Law remained appropriate, in the term of Import Substitution, Foreign Investment Policy was not systematic for utilizing foreign investment effectively for national development. As a result, "Transnational Company frequently got benefits by protection, used old-fashioned technique and facility in the host country, yielded excessive gain at the expense of national consumers". Excessive "Mexicanization" in the term of Import Substitution created concentration of industry, had a negative effect on price policy and resources available for the an investment [5].

The aim of economic policy of National Development Plan 1983-1988 was " maximally to use technological, management, financial resources and expand, diversify and modernize Mexican productive facilitates; in this sense, orient foreign direct investment toward prior area of development strategy." The purpose was to abandon Protected Policy and for the foreign investment policy to be "positive" and "systematic" [6].

However, the term was transitional, from excessive protective Import Substitution to Export-Oriented Industrialization. Although non-selective Import Substitution was criticized, effective and selective Import Substitution was hung up together with export promotion. The plan of a foreign investment policy had changed, maintaining the legal framework of the "1973 Foreign Investment Law". Positioning of foreign investment as complementing the Mexico capital was specified, and a promotion-foreign -investment policy was regarded by "National Development Plan 1983-1988" as specifying the field and type of industry which receives foreign investment preferentially.

The materialization of the plan of the foreign funding policy of regime of President De la Madrid term was revealed in "the guideline for foreign investment and its promotion (Lineamientos sobre inversiones extranjeras y propósitos de su promoción)" which the national foreign investment committee announced in February, 1984. The main point of this guideline was to announce the field and type of industry accepting foreign direct investment preferentially, and to apply "1973 Foreign Investment Law" to those types of industry, and to make it flexible. On the other hand, this guideline showed clearly the advance recognition of National Foreign Investment Committee despite a priority industry in foreign investment.

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[5] Poder ejecutivo Federal (1983), p. 192.
[6] Peres Nuñez (1990), p. 41.

c. Foreign Investment Policy in the term of Salinas

"National Development Plan 1989-1994 (Plan nacional de desarrollo 1989-1994)", was effected when liberalization of a foreign trade policy progressed and the Mexico economy became more competitive under President De la Madrid Administration. "So that it may be avoided that a foreign company should enjoy excess profits from the protected market, and impart the burden to the consumer and offer products of low quality. It hesitates to use the technology that was outdated in its native country "[7]. The result of the Export-Oriented industrialization strategy advanced, taking President De la Madrid's administrative term as a turning point.

This plan hung up reservation of promotion of non-oil export, correction of distortion of resource allocation, and the route to an oversea market, and promotion of foreign investment and technology transfer as a purpose of foreign economic policy. And it appealed for promotion of further liberalization of the foreign economic policy begun by President De la Madrid[8].

It was with the initiation of features with a development strategy that the "selective and efficient" Import Substitute Industrialization disappeared under regime of Salinas President. Only export promotion was emphasized. The basic idea of the development strategy is based on the Export-Oriented Industrialization model of neo-classical development economics; therefore an export promotion policy took the form of drastic liberalization of foreign economic policy.

"National Development Plan 1989-1994" with such a fundamental target, foreign direct investment is caught with what plays a role much more important for promotion of Export-Oriented Industrialization[9]. And a foreign investment policy also followed the large frame of the whole foreign economic policy, and being converted into the positive introduction-of-foreign-capital policy which drew a line with President De la Madrid's term of more liberalization

We will look concretely at the foreign investment policy of the Salinas's government term. Ministry of Commerce and Industrial Development (Secretaría de Comercio y Fomento Industrial: SECOFI) announced the principle of abolishing the 5th article of the "1973 Foreign Investment Law" which did

[7] Poder Ejecutivo Federal (1989), p.88.
[8] Poder Ejecutivo Federal (1989) pp.85-86.
[9] Foreign direct investment that complements Mexican capital is considered to be useful in development strategy in the following four ways. First, job creation and the rise of wages, Secondly, supplying resources (finance) to solid business firm, Thirdly, supplying modernistic technology to a manufacturing industry section, Fourthly, encouraging export efforts. Poder Ejecutivo Fedral (1989), p.

not accept majority participation of foreign investment in a Mexican company[10]. And the way was greatly opened by 100% participation of foreign investment in Mexico companies Instead of directly revising the "1973 Foreign Investment Law" and inviting uncertainty, it changed the basic idea of "1973 Foreign Investment Law" substantially and the foreign investment policy to provide for Export-Oriented Industrialization.

Thus, from the early stages of the Salinas government, foreign investment was positioned as one of the fundamental elements for Mexico economic development, and a policy was drastically liberalized for the introduction of foreign capital. Before issue of the North America Free Trade Agreement and the government realized the revision of the Foreign Investment Law itself[11]. I will survey the main points below.

The purpose of the newly enacted "Ley de inversión extranjera" (Foreign Investment Law, below 1993 Foreign Investment Law) was to invite "foreign investment to Mexico and establish rule for contributing to national development (the 1st article). By the "1989 Foreign Investment Law enforcement regulations", the basic idea of the foreign investment policy itself was changing in fact.

That change of a basic idea was incorporated in the Foreign Investment Law itself, symbolizing the final-stage conversion to the Export-Oriented Industrialization from Import Substitute Industrialization.

Specifically, the "1993 Foreign Investment Law" clarified regulation of the indefinite foreign investment regulation in the "1973 Foreign Investment Law", moving further from the "1989 Foreign Investment Law enforcement regulations" as a whole, and easing the regulation on foreign investment. According to Article 4 of the law, except for regulation of the law, 100% participation to the capital of the Mexican Company of foreign investment, acquisition of fixed assets, establishment and management of a company, and expansion and rearrangement of the existing company were attained. And the "1989 Foreign Investment Law enforcement regulation about the second petrochemical field restricted to 40% was abolished, and the participation of 100% of foreign investment participating ratio was attained.

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[10] It was necessary that foreign investment should satisfy following conditions to own majority in Mexican Company. First, foreign investment was not replacement of Mexican Company but complement to it. Secondly, it is expectable to bring the positive effect of plus to international balance of payment by the increase in export. Thirdly, foreign direct investment brings about creation of employment, and the rise of wages. Fourthly, foreign direct investment contributes to growth of the area that was in development relatively. Fifthly, foreign direct investment contributes to research and development. GATT (1993), pp. 63-66.

[11] The "1993 Foreign Investment Law" corresponds to the investment rule defined by NAFTA. It is related with the investment rule of the North America Free Trade Agreement, and is THE NAFTA (1993) in detail. On the "1993 Foreign Investment Law", see Banco de México (1994), pp.187-192, SECOFI (1993).

The aim of revision can be summarized. Firstly, promotion of the Export-Oriented Industrialization strategy of introducing foreign investment and promoting export, Secondly, promotion of the improvement in the technical level of the Mexico manufacturing industry section and research and development, Thirdly, improvement in the job creation in Mexico and in wage level. In the following section, we examine how the manufacturing subsidiary of U.S. multinational company in Mexico is contributing to Export-Oriented Industrialization of Mexico using the data of U.S. direct investment abroad.

Ⅲ U.S. Multinational Company on Mexican Export-Oriented Industrialization

a. Foreign Investment Inflow

It is necessary to explain U. S. Direct Investment Abroad before undertaking our analysis. For United States, foreign direct investment is ownership or control by a single person of 10 percent or more of an enterprise's voting securities, or the equivalent, which is considered evidence of such a lasting interest or degree of influence over management. And foreign affiliates means the overseas company where such U.S. direct investment exists. Moreover, majority-owned affiliate (MOFA) is one in which the combined direct and indirect ownership interest of all U.S. parents exceeds 50 percent[12)].

The focus of analysis here is in the following four points. Firstly, how the trend of the U.S. foreign direct investment for Mexico is changing with conversion of a foreign investment policy? And how does the weight of the investment in the manufacturing industry sector in relation to the whole foreign direct investment change? Secondly, how much the amount of export from manufacturing affiliates industry sector in Mexico is increasing according to change in the foreign direct investment for Mexico? Thirdly, what is the job creation effect of foreign direct investment to the manufacturing industry sector? Fourthly, has research and development of affiliates in the manufacturing industry sector in Mexico met with progress?

We will look at transition of the whole foreign direct investment for Mexico from the United States that includes a bank (Table 1).

[12)] Unless referring to MOFA, I am examining data of a foreign affiliates that are directly or indirectly or controlled by one U.S. parent company to the extent of 10 percent or more voting securities for an incorporated business enterprises or an equivalent interest for an unincorporated business enterprises.

Analysis focus considers four points. Firstly, how had U.S. Direct Investment toward Mexico changed with change of foreign investment policy? Secondly, how exports increased manufacturing affiliates in Mexico? Thirdly, how foreign direct investments created jobs? Fourthly, How research and development of affiliates in Mexico progressed?

Changes of U.S. Direct Investment toward Mexico can be seen in Table1. The direct investment balance for Mexico of the United States was 5,019 million dollars in 1982 when President De la Madrid took office. It increased to 5,712 million dollars when he resigned in 1988. It increased to 15,714 million dollars in 1994 when Salinas resigned. 90% or more of the U.S. direct investment for Mexico was made from 1989 to 1994, which corresponded to the Salinas term mostly. In addition, the direct investment balance for Mexico increased for about 20 billion dollars in the term of President Zedillo, 35,414 million dollars in 2000. This increase corresponds to about twice Salinas's term.

To which section did foreign direct investment go? The share directed to the manufacturing industry sector fell from 78.1% in 1982, 63.6% in 1994, 57.5% in 2000. Although the weight of U.S. direct investment for Mexico moved from manufacturing industry sector to third industry, the share of manufacturing industry sector remained large. The sections with the large amount of acceptance of foreign direct investments in manufacturing industry sector were food and kindred products, chemistry and allied products, and transport equipment.

b. Exports promote and job creation

We will examine the trend of export of manufacturing affiliates in Mexico by seeing import from affiliates in U.S. (Table 2). It is characteristic that the ratio of the manufacturing industry sector to total import amount is very high. The total import amount from affiliates of U.S. manufacturing industry sector in Mexico increases from 2,267 million dollars in 1983 to 11,217 million dollars in 1992; it has risen by about 5 times. More recently, the total import reached 27,223 million dollars in 1998; it has risen by about 2 times during six years. And it has made up the 82.0% of total imports in 1983. In recent years still higher 95.7% in 1992, 99.6% in 1998. The total imports were almost manufacturing. Electric and electronic equipment and transport equipment have especially contribute to the large amount of imports, and when both are combined, it turns out that decisive specific gravity calls up about 3/4 of the total import amount from U.S. affiliates in Mexico.

Next, we will look at the composition of the job creation effect and the employment of affiliates in Mexico (Table 3). The manufacturing industry sector occupies the big share in employment of affiliates in Mexico. There were about 302,800 persons (19.3% of the employer total of the Mexico manufacturing industry sector) in 1977, 344,900 persons (16.5% of this rate) in 1983, 493,700 persons (this ratio is 16.4%) in 1992, 546,300 (19.0%) personas in 1995.[13)] The industries, in which the number of employers increased greatly in the manufacturing sector, were food and kindred products, electric and electronic equipment, and transport equipment. However, in terms of wages of productive laborers of MOFA, the global average hourly pay was 10.37 dollars. The average in Canada was 16.71 dollars, 14.45 dollars in European countries, 3.25 dollars in Latin America, only 2.28 dollars in Mexico. When this level was compared with the other industrializing developing countries, 4.17 dollars in Brazil, 3.78 dollars in Asia NIEs and 1.56 dollars in ASEAN4, the wage level in Mexico was the worst of NICs.

Job creation by foreign direct investment and component of U.S. affiliates in Mexico is also detailed (Table 3). Manufacturing sector shared a high proportion of jobs of U.S. affiliates in Mexico. Employment in this sector was 302, 800 in 1977 (19.3% of total jobs in Mexican Manufacturing sector), 344, 900 in 1983 (16.5%), 493, 700 in 1992 (16.4%). The industry that increased employment was food, electric and electronics and transportation.

However, hourly payment of assembly line labor of majority-owned foreign affiliates in 1994 was 12.57 U.S.dollars on average world total, 19.69 dollars in Canada, 4.66 dollars in Latin American countries, 3.57 dollars in Mexico. Comparison with other industrializing countries, Brazil (Latin American NICs) was 6.35 dollars, average Asian NIES was 6.24 dollars, average ASEAN4 was 2.19 dollars[14))]. Wage level of Mexican productive labor was worst of the NICs. That is, it turns out that the wage level of the productive laborers of Mexico was the lowest in the development countries classified as NICs.

c. Research and Development

We will see the degree of research intensity (the ratio of research and development workers with regard to all employers, and ratio of research and development expense in total sales). And we will examine the role that affiliates of U.S. multinational companies in Mexico have played in improving the technical level of the Mexican manufacturing industry.

[13)] On the employer total of the Mexico manufacturing industry section, see Poder Ejecutivo Federal (1994), p.560; Only 1995, Poder Ejecutivo Federal (2000), p. 45.

[14)] United States Department of Commerce, BE A (1998), p. 227.

While the employer total of manufacturing affiliates in Mexico increased greatly as mentioned above, the number of employers engaged in research and development does not increase. For example, although total employers of a manufacturing MOFA in Mexico increased by 119,057 persons in the period from 1977 to 1989 and 124,900 persons in the period from 1989 to 1994. The number of employers engaged in research and development decreased from 1299 in 1977 to about 1000 in 1989 and increased to about 1300 in 1994[15)]. The share of employers engaged in research and development fell from 0.8% in 1977 to 0.3% in 1989 and 1994. Next, we will look at the change in the ratio of the research and development expense occupied in sales (Table 4) . With the whole world average rising from 1.2% in 1982 to 1.4% in 1992, and the developing country average going up from 1982 to 1989 from 0.5% to 0.8%, Mexico tended to decline from 0.4% in 1982 to 0.3% in 1992.

Thus, while the degree of research intensity of manufacturing affiliates in Mexico showed little movement, the research and development amount disbursed through affiliates in the Asia NIEs countries especially Singapore and Taiwan increased in recent years. The research and development amount disbursed of the Singapore's affiliates in 1992 exceeded Mexico, and its ratio of research and development expense occupied in sales also was double that of Mexico at 0.7%. Moreover, the ratio of the research and development expense occupied in the sales of affiliates in Taiwan was 0.8%. As a developing country, the rate of Taiwan equals the rate of Brazil and represents a high level.

When the degree of research intensity is seen as an index, a U.S. multinational company raises the degree of technical intensity of oversea production globally, Such a tendency is not found in Mexico. It can be said that the degree of technical intensity of production in Mexico is its tendency to fall from the beginning of the 1980s to the beginning of the 1990s[16)].

I will now evaluate the contribution of a U.S. multinational company in Mexico. The U.S. multinational company performed direct investment in Mexico at a pace exceeding before the Salinas term when

[15)] U. S.Department of Commerce, BEA (1981), p.294, U. S.Department of Commerce, BEA (1992), p. 216, p. 218, U. S. Department of Commerce, BEA (1998), p.219,p. 227.

[16)] Lately, the whole world average decreased to 0.7% in 1998, which was half of 1992. The level of the developing country average going down to 0.3% that was lower level than in 1982. Mexico and Brazil maintained the level of 1992 on the other hand. The research and development amount disbursed of the Brazil and Mexico surpassed an own level in 1992 and Asian NIEs's in 1998. The following is thought as a factor that the research and development expense of Asian NIEs nations greatly falls below the level in 1992. It is in the first because of an Asian monetary crisis. The second reason was that the stage of the export-oriented industrialization by the multinational company was to have graduated in Asian NIEs.

foreign investment policy was liberalized sharply in only six years. And the manufacturing affiliates in Mexico increased export and employment mainly on electric and electronic equipment, and transportation equipment in the regime of De la Madrid and Salinas.

Therefore, concerning export promotion and job creation by the introduction of foreign investment hung up as an aim of liberalization of a foreign investment policy, it could be said that a fixed-grade achievement was able to be carried out. The increase in employment, however, can hardly be referred to as accompanying an improvement in a wage level.

The increase in employment depended on the increase in laborers engaged in assembly production that is minimum wage labor in NICs. And number of research and development exclusive workers in manufacturing affiliates in Mexico tended to decrease. The tendency for the ratio of research and development expense occupied in sales to fall was also noted. It was shown that the technical level of manufacturing affiliates in Mexico did not improve.

NAFTA tends to extend the tendency before coming into effect. The tariff of the manufacturing product between Mexico and the United States was lowered considerably before NAFTA by Maquiladora in Mexico and HTS9802[17)] of the United States (Table 5). In that sense, it is thought that NAFTA aims in making economic integration between the U.S. and Mexico far stronger. It is represented that the sales of manufacturing affiliates in Mexico increased to the United States since the start of NAFTA (Table 6). It can be said that NAFTA accelerated to the North America economic bloc of the Mexican manufacturing export section by the initiative of U.S. multinational companies.

Ⅳ. Concluding Remarks

When we evaluated how what foreign investment laws accomplished, we considered the strategy of U.S. Multinational Companies in the manufacturing sector. The U.S. Multinational Companies moved to Mexico because trade and foreign investment policy was liberalized and labor was cheaper than in the U.S.A. The companies intended to maintain capital and technical intensive production processes in U.S.A., and transfer labor intensive product process to Mexico. They exported intermediate goods: parts

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[17)] There are two types of HTS 9802. Subheading 9802.00.60 sets forth tariff treatment for certain metal U.S. origin processed in a foreign locations and returned to the United States for further processing. Duty is applied on the value added by the foreign processing. Subheading 9802.00.80 provides tariff treatment for eligible imported goods that contain U.S.-made components. Duty is applied on the value of the imported product minus the value of the U.S.-made componetd. United States International Trade Commission (1991), 1-1, 1-2.

and component made in U.S. to Mexico and finalized production through labor intensive processes, and imported final goods-so called intra-firm international division of labor between U.S.A. and Mexico. Accomplishing promoting exports and jobs creation and not realizing wage and technical level increases were the other side of coin.

Therefore, the next subject to consider is progress of the intra-firm international division of labor between U.S.A. and Mexico of the U.S. Multinational Company accompanying the conversion of the Mexico development strategy from Import Substitute Industrialization to Export-Oriented Industrialization.

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