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Bad Signals

BY MAURO F. GUILLÉN (THE WHARTON SCHOOL) AND
EMILIO ONTIVEROS (UNIVERSIDAD AUTÓNOMA DE MADRID)

Never before has the global economy needed a stronger coordination and cooperation among its main actors with a view to supporting the incipient recovery in the high-income countries, which represent the largest markets in the world. The most important and urgent test has to do with the so-called currency war that has been going on for several years in latent form and has now broken out: the manipulation, more or less interested, of currency exchange rates with the goal of promoting one's exports and reducing the appeal of imports. The possible return of capital controls is not a welcomed development either.

This controversy is not new. China's policy of keeping the yuan's fluctuation within a very narrow band (effectively, a yuan-dollar peg) in an attempt to protect its export competitiveness has been hotly debated for years. Specifically, U.S. economic policymakers have maintained that China's currency policy is a central element of their trade policy, and is directly responsible for a large proportion of the U.S. current account deficit.

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Latin America is in Good Shape:
But Mexico to Face Hard Economic Decisions

BY SIDNEY WEINTRAUB
(CENTER FOR STRATEGIC AND INTERNATIONAL STUDIES)

I have been following Latin American developments for more decades than I care to remember. My sense of Latin America at the beginning was ambiguous—I found the region culturally fascinating, but economically and socially deficient. The main deficiencies were volatile economic growth, uncertain democracy, high inflation, and a tendency to blame others for the region's problems—such as the conviction that the terms of trade (the ratio between export and import prices) would inevitably remain unfavorable unless the region could replace its commodity exports with exports of manufactured goods. This was the central thesis of Raúl Prebisch, Latin America's best known and widely followed economic guru in the 1960s; for many years, Prebisch also directed the Economic Commission for Latin America (now ECLAC because of the addition of the Caribbean).

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The big change that has taken place over the last few weeks is that this Sino-American conflict is no longer a bilateral issue but a global one. The ballooning of the U.S. deficit after the respite caused by the crisis and the growth in Chinese international reserves (to $3.7 trillion), has added new aggravations and aggravated countries to the list. OECD governments are under pressure to reduce unemployment, and the temptation always is to look for quick fixes, such as a devaluation-induced export growth. This temptation is even more powerful when elections are near. The adverse effects of a round of competitive devaluations, however, would be felt not just in the labor market but beyond.

The big change that has taken place over the last few weeks is that this Sino-American currency conflict is no longer a bilateral issue but a global one.

Japan and the U.S. have taken the lead in terms of accusing China of currency manipulation. Meanwhile, China, Brazil and other emerging economies have charged the U.S. with implementing an excessively lax monetary policy, with two large rounds of quantitative easing. As a result, the U.S. dollar has lost ground, with the usual turmoil in global currency markets and the upswings in the prices of gold and a number of commodities. Cooperation is sorely needed at this point in order to avoid a generalization of the beggar-thy-neighbor policies that Joan Robinson so aptly described in the thirties. We don't know how many steps there are between a currency war and a trade war. What we know is that it starts with competitive devaluations and ends seriously compromising international trade relations and geopolitical stability.

It is not easy to quantify the magnitude of the appreciation of the yuan if it were to float freely in the market. It is not an exaggeration to think that it might increase in value by 10 or 15 percent. While substantial, this appreciation would not hurt Chinese export competitiveness. Let's bear in mind that since 2005 the gradual appreciation of the yuan relative to the dollar has coincided with a significant increase in the bilateral trade deficit. It is also germane to add that China's trade is becoming more specialized in product categories for which cost is not the only relevant factor. Thus, the price-elasticity of Chinese exports is on the decrease. This is a fact that U.S. multinationals know very well, given that they source from China a large proportion of their inputs, and in many cases they sell directly from China.

The second important fact to consider is that excessively accommodating monetary policies do contribute to the tension and the probability of an all-out currency war. Though the U.S. is not the only country that has engaged in monetary easing, it is by far the most aggressive. The flood of dollars after the second round of the Fed's purchases of U.S. bonds is putting downward pressure on the dollar relative to

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Important Upcoming Decisions Regarding Transfer Pricing Adjustments of Related Parties Providing Shelter Services

BY ESTEBAN G. DALEHITE, PH.D.
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Important decisions are going to be reached in the short or medium term between the United States and Mexico concerning the transfer pricing adjustments made by related parties providing shelter services in Mexico. Bilateral procedures between both countries have been initiated by several groups which together comprise an important segment of the shelter industry. Although only the parties involved are privy to these procedures, the decisions reached by both countries could have an important impact on the current and future multinational groups providing shelter services. The purpose of this article is to discuss generally some of the main issues.

What Are Shelter Services?

Shelter services are best understood by first referring to the standard *maquila* arrangement. In the typical *maquila* structure, a manufacturer (typically U.S. or Canadian) wishes to take advantage of cheaper labor costs in Mexico and to that end it establishes a subsidiary in Mexico. This subsidiary in turn imports capital and intermediate goods provided by its parent company, hires the necessary labor in Mexico, manufactures an intermediate or final good, and exports this good back to its parent company in the U.S. or Canada.

Many U.S. and Canadian manufacturers have utilized this structure and benefitted from cheaper labor costs and other advantages of Mexico-based production. However, there are manufacturers who simply do not have the capital to offshore operations by setting up a subsidiary in Mexico, going through the learning curve of doing business in Mexico and establishing a structure to provide the necessary support services for their core manufacturing processes in a foreign land. This is where shelter services come in.

Clients of shelter services providers typically do not want to outsource their core manufacturing systems and processes, but wish to take advantage of Mexico-based production. They want to retain control of their production and their own unique corporate culture; expand without overtaxing their existing management team, and they want to do so securely without taking on unnecessary risk and over-committing resources.

Shelter services allow a manufacturer to offshore its core manufacturing systems and processes into Mexico and to focus solely on these core processes without having a legal presence in the country. To make this happen, it is the shelter service provider that establishes an entity in Mexico through which all necessary support services are rendered.

A shelter service provider once told me that if he were to liken shelter services to better known industries, he would pick employee leasing first, and contract manufacturing second.

Although business structures may vary, the typical support services provided include the following: recruiting, staffing, and labor relations; employee medical services and benefits administration; payroll administration; importing, exporting and transporting of machinery, equipment, and intermediate and final goods; purchasing of indirect goods and services in Mexico; financial and accounting services; information technology support; facilities and security; and governmental relations. Given that these services are provided to multiple clients, the latter can benefit from economies of scale. The Mexican entity obtains a *maquiladora* permit from the Mexican government to operate as a shelter. Therefore, shelter service providers are typically categorized together with straight *maquilas*.

How Did The Current Transfer Pricing Problems Arise?

Mexican statutes contain a transfer pricing regime that has been satisfactory in general for the standard *maquila* arrangement. Partly, as a result

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of negotiations between the U.S. and Mexico, the latter wrote Article 216-bis into the Mexico Income Tax Act (MITA) which provides that the Mexican *maquila* is deemed to comply with transfer pricing provisions and to not constitute a permanent establishment for its foreign client or related party (typically the U.S. or Canadian parent) as long as it applies any of the following procedures to determine taxes:

Clients of shelter services providers typically do not want to outsource their core manufacturing systems and processes, but wish to take advantage of Mexico-based production.

1. Income and deductions are determined by adding arm's length prices obtained through an acceptable transfer pricing method (ignoring assets not belonging to the Mexican related party) plus 1% on foreign-owned machinery and equipment provided to the Mexican related party under non-arms length terms and conditions. This is known as the cost-plus method.
2. Taxable income is equal to the greater of 6.9% on all assets used in the *maquila* operation regardless of ownership, or 6.5% on operating cost and expenses incurred by the Mexican related party and also those incurred by the foreign related party with some exceptions. This is known as the safe harbor. A Presidential decree cuts these percentages in half.
3. Income and deductions are determined using a transactional net profit method considering the return on machinery and equipment used in the *maquila* operation belonging to the foreign related party.

Although these options have been satisfactory for the standard *maquila*, they appear to have not worked out for shelter services providers. The reason is that *maquila* and shelter services are quite different. While a standard *maquiladora* subsidiary manufactures goods for its parent company—i.e. it actually provides *maquila* services to its parent—the Mexican shelter entity does not manufacture any goods for anybody; it simply facilitates the manufacturing of goods by its unrelated clients. Formally, the Mexican entity providing shelter services is a *maquila*; substantively, it is not.

The reader will have noticed that all options contained in Article 216-Bis are based on return on assets or return on operating cost. Such methods make sense for an entity that is manufacturing goods—for which gross income is typically the market value of the goods produced—and hence a mechanism to determine income, deductions, or taxable income based on some fraction of the assets or operating costs used to produce the goods is *prima facie* reasonable.

However, this is not the case for shelter service providers where gross income is tied to the support services provided to clients. Fees for shelter services differ across providers. At least in some cases the shelter fee is fundamentally a function of the labor cost of clients. This is not surprising given that one of the most important roles played by shelter service providers is identical to the role played by employee leasing companies. Gross income essentially increases with every additional employee hired on behalf of clients.

If gross income and profits are a function of client labor costs, one can see the problem with determining taxes as a function of the value of client machinery and equipment or client total operating cost. The methods can produce tax burdens that are out of proportion with or bear no relationship with actual profits. Furthermore, if the ratio of labor costs to the value of machinery and equipment, or to total operating cost shifts from year to year according to changes in the clientele or the technology used by clients, then the tax burden could also shift with no proportion or relation to changes in actual profits.

The above methods can produce tax burdens that are high, low or reasonable, even if the methods are unrelated to the profits of shelter service providers. That would depend on the data and specifics of the methodology in each case. Shelter service providers, as *maquilas*, have the right to apply the methods contained in Article 216-Bis.

However, it is the potential of the methods in Article 216-Bis to produce disproportionate tax burdens that drove some multinational groups providing shelter services to devise alternative transfer pricing methodologies. These multinational groups sought confirmation from the Mexican Tax Administration Service (SAT) for these alternative methodologies through advanced pricing agreements. Unfortunately, it appears that the SAT took a rather aggressive approach in unilateral rulings.

These events put the involved shelter service providers in a quandary. If they complied with the SAT's unilateral advanced pricing rulings then they could eventually end up with double taxation, should the U.S. find the corresponding adjustments in disagreement with arm's length standards, which was likely. As a consequence, these multinational groups are now seeking a bilateral solution to their transfer pricing problems pursuant to Article 26 of the U.S.-Mexico Tax Treaty.

Important Issues

Adequately solving the transfer pricing regime of shelter services providers should be a priority for both the U.S. and Mexico for several reasons. First, not reaching an agreement would almost surely imply double taxation for shelter services providers. Second, a bilateral agreement imposing additional taxes owed in Mexico could signify an important financial burden on the shelter industry. Bilateral solutions are sometimes categorized as zero sum games—i.e. whatever tax is paid to one country is not paid to the other—with no additional burden to the taxpayer. However, this can be misleading given that differences in tax structures between both countries can imply strong burdens to taxpayers.

For instance, Mexican statutes establish an inflation adjustment for back taxes which does not exist in the US. Thus, a solution implying additional tax payments in Mexico would entail not only inflation adjustment but also penalties on inflation adjusted amounts. This is why it is important that the bilateral agreements are based on arm's length principles and that they gives proper consideration to the fact that at least part of the time delay in reaching the agreements may be attributable to tax authorities. It has been customary in previous bilateral agreements to waive penalties.

Lastly, a transfer pricing solution that not only solves current problems but that also provides a reasonable regime for the industry in general should be on the agenda for both governments. It goes without saying that the present and future viability of this industry requires an adequate, durable, and generalized solution. Given that only the parties to the bilateral procedures are privy to the agreements reached, both governments should give consideration to publicizing the agreed-upon transfer pricing methods in some general format so that all participants in the industry can opt to utilize them.

An important issue that authorities and parties involved will have to wrestle with is the adequate methodology to apply in these cases. As mentioned above, shelter services are essentially manufacturing facilitator services. Hence, ideally they should be taxed as manufacturing facilitators. However, this concept of facilitator is relatively new, not well understood, and parties will have trouble finding external data to validate their methodologies. If external pricing benchmarks cannot be found for manufacturing facilitators, the natural inclination will be to liken shelter services to already existing industries.

Another important issue or challenge for the parties to the bilateral proceedings is to make sure that the cases get the proper attention from the US-IRS, despite the relatively small tax revenue that is at stake for the US.

A shelter service provider once told me that if he were to liken shelter services to better known industries, he would pick employee leasing first, and contract manufacturing second. This opinion provides a general guideline of where methodologies could go. Indeed, at least some shelter services calculate their fees as a function of client labor cost, similarly to employee leasing companies. This is one general direction in which methodologies could go, and where the existence of reliable external data is likely.

The other general direction is to liken shelter services to contract manufacturing. Here too reliable external data is available. Applying the options contained in Article 216-Bis of the MITA essentially implies likening shelter services to contract manufacturing. The SAT might be inclined to search for a general solution in this area given that it might want to try to tax the underlying manufacturing process taking place in Mexico, rather than the facilitating services actually being provided in Mexico by the taxpayer. The problem of this general direction, as explained above, is that it has to be based essentially on the client's data (who is the manufacturer with no legal presence in Mexico) and not on the shelter services provider data. The possibility of obtaining tax burdens that are either unrelated or out of proportion with profits is likely. Excessive tax burdens, whether absorbed by the shelter service provider or passed on to the client, can diminish or wipe out whatever competitive advantages is

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held by this industry. Therefore, if this general direction is sought, appropriate adjustments and safeguards should be included.

Another important issue or challenge for the parties to the bilateral proceedings is to make sure that the cases get the proper attention from the US-IRS, despite the relatively small tax revenue that is at stake for the US. If these multinational groups are now seeking a bilateral solution to their transfer pricing problems, it is obvious that they are expecting the US-IRS to weigh in on their side and straighten matters out. In principle, the US-IRS should have an interest in correcting these problems because U.S. tax revenues are at stake.

However, the historical evidence seems to point in a different direction. Although the relationship between the U.S. and Mexico concerning the taxation of *maquila* income has been a good one, it has also been one in which Mexico typically asserts rather aggressive claims and the US, placing relatively little importance on the *maquila* tax base, has been willing to make concessions to Mexican authorities. This precedent does not bode well for the shelter industry.

Finally, there may be a tendency to perceive the shelter industry as structurally homogenous and to produce a single (one-size-fits-all) transfer pricing rule or method for the shelter services industry. However, this could be a mistake. Evidence suggests at least one major difference in the industry that calls for a diversified policy, if not more. Some multinational shelter service providers are fundamentally Mexico-based, with most important functions being carried out by the Mexican related party. In such cases, it seems that most of the group's profits should be reported in Mexico.

In contrast, there are multinational groups that are essentially US-based. In these cases, while it may be that the Mexican related party is the one that provides most support services to clients, it is the U.S. related party that carries out the fundamental functions of financing, loss absorption, marketing, client management and contract negotiation, amongst others. In these cases, it seems that an important part of the profits should be reported in the US.

Much hangs in the balance in the bilateral procedures under way as the agreements reached can potentially have a significant impact on the shelter service industry. Enterprises taking advantage of Mexico-based production will do well to put these eventual bilateral agreements on their radar screen. ❑

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Using the First Sale Rule to Lower Duties on Imports Into the U.S.

BY LAURA SIEGEL RABINOWITZ
(SANDLER, TRAVIS & ROSENBERG, P.A.)

Each year, most U.S. importers pay more customs duties than are legally required. Importers deal with a wide range of individuals and companies to get their goods from the foreign factory door to the domestic retail floor, and each of these interactions can add to the ultimate cost of the imported product. Perhaps none have a bigger effect, however, than the importer's purchase from a vendor or middleman who buys the item from the original manufacturer. This price usually represents a substantial markup and is used to calculate duties when the goods are imported into the U.S.

Fortunately, these types of transactions also open up the possibility of substantial duty savings. A unique aspect of U.S. customs law, the First Sale Rule, allows companies that import into the U.S. to lawfully reduce their duties by entering goods at a lower value than the price actually paid to the foreign vendor. Most U.S. importers are eligible to take advantage of this benefit because, whether they realize it or not, they usually purchase foreign goods through multiple parties, not directly from the manufacturer. First Sale can even be used if the vendor is related to the importer and/or the factory or there are multiple levels of vendors. While it has sometimes been difficult to obtain the needed information from business partners to take advantage of First Sale, experience shows that this problem can be overcome, and especially in times of economic struggles and factory closings vendors are more likely to cooperate with their customers.

This article reviews the structure and legal requirements of a First Sale transaction, briefly discusses the legislative and regulatory status of First Sale and lists some best practices for taking advantage of this duty savings opportunity.

First Sale Transactions

The dutiable value of a First Sale transaction is based on the purchase price between the vendor and the factory rather than the price between the vendor and the importer. As a result, no duty is ultimately paid on the vendor's mark-up or any additional charges on the subsequent sale. This differential presents a duty savings of 10-20%, but government statistics indicate that most importers are not taking advantage of this cost saving methodology.

The validity of First Sale is well-established in both law and practice. It is supported by over 20 years of case law, including several Court of International Trade decisions that set forth the requirements an importer must meet in order for duty to be assessed based on the first sale within a multi-tier transaction. Specifically, there must be two bona fide sales, the goods must be destined for export to the U.S. at the time of the first sale, and the foreign manufacturer/seller and middleman/buyer must either be unrelated or conduct their transactions at arm's length. The courts have established that when these criteria are met U.S. Customs must base the dutiable value of the goods on the manufacturer's price to the vendor.

Importers who are thinking of implementing First Sale should focus on vendors with whom they plan to stay for the foreseeable future. A good working relationship is a bonus because the vendor will be sharing confidential information with the importer's customs compliance team.

Bona Fide Sales. When there are two bona fide sales, the same party serves as the buyer in the first sale (usually from a foreign manufacturer) and the seller in the second (usually to a U.S. importer or consignee). On the contrary, when that intermediary is functioning as an agent, the actual sale is between the foreign seller and the importer, with the agent acting as a facilitator. In that case, the pertinent issue is whether the commissions the agent receives for its services are part of the transaction.

U.S. Customs defines "sale" as the transfer of property from one party to another for consideration; i.e., payment. Evidence of consideration

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includes payment by check, bank transfer or other commercially accepted means. In determining whether property or ownership has been transferred, Customs considers whether the potential buyer assumes the risk of loss (i.e., is liable for goods when lost or damaged during shipment) and acquires title to (i.e., legally possesses or owns) the goods. In addition, Customs will examine whether the potential buyer pays for the goods (i.e., consideration passes between the parties).

It is critical that First Sale transactions be carefully developed. While the concept has been in place for some time most importers are unsure of how to construct a compliant document trail.

Even if the second party does not actually possess the goods, there are other means to satisfy Customs with respect to the risk of loss. For instance, a foreign middleman could serve as consignee in care of its customs broker so that title and risk of loss would pass to the middleman for at least some time during transit of the goods between the manufacturer and the U.S. importer. Transaction documents, the shipping terms and insurance contracts would need to indicate this to be the case.

Other evidence of bona fide sales includes whether the buyer and seller are independent of each other. Specifically, Customs considers whether the potential buyer provided (or could provide) instructions to the seller, was free to sell the items at any price it desired, selected (or could select) its own customers without consulting the seller, and could order the imported merchandise and have it delivered for its own inventory.

Documentary evidence to support bona fide sales includes contracts, distribution and similar agreements, invoices, purchase orders, bills of lading, proof of payment, correspondence between the parties, and company reports or brochures.

Destined for Export. The second requirement is that the goods must be clearly destined for export to the U.S. at the time of the first sale. To make such a determination Customs considers evidence such as production orders and / or manufacturing instructions and other unique specifications of the merchandise to conform to the buyer's standards; examples of labels, logos, stock numbers, bar codes and other unique merchandise or carton marks; and examples of country of origin marking on finished goods, hang tags, etc., any warranty cards provided, or other types of certification required for entry and / or sale of the goods in the U.S.

Relationship Between Factory and Middleman. The third requirement is that the middleman buyer and the factory seller either be unrelated or negotiate at arm's length. A sale will be considered at arm's length if the relationship between the buyer and seller did not influence the price of the merchandise or the transaction value closely approximates a test value.

Always a clear indicator of an arm's length sale is when the factory makes a profit. In addition, the circumstances of sale test will be met if the price is settled or negotiated in a manner consistent with normal pricing practices in that industry or with the way the seller settles prices with unrelated buyers. Another way to satisfy this test is to show that the price is adequate to ensure the recovery of all costs plus a profit that is equivalent to the firm's overall profit in sales of such merchandise. Alternatively, the transaction value will be deemed to closely approximate a test value if Customs has previously accepted a comparable transaction value, deductive value or computed value for identical or similar merchandise for goods already exported to the U.S. at or about the same time as the imported merchandise.

Legislative and Regulatory Status

In January 2008 Customs issued an unexpected proposal to eliminate the First Sale Rule. The resulting outcry among the importing community led to an unusually quick response from Congress, which inserted a provision in the 2008 Farm Bill that prohibited Customs from attempting to revoke First Sale until Jan. 1, 2011, and established strict standards on any such attempt Customs might make after that date. Customs recently issued a formal withdrawal of its 2008 proposal and is not known to be actively considering the issue.

Congress also directed the U.S. International Trade Commission to undertake a review of the use of First Sale. The ITC found that in fiscal year 2008 this methodology was utilized for only 2.4% of total U.S. imports and by a mere 8.5% of importers. The use of First Sale is generally more widespread in sectors with the highest average tariffs, which is not at all surprising given that this methodology is employed to legally reduce duties.

The relatively small share of U.S. imports that are valued using First Sale could be used to support or oppose the continued use of this methodology. On the one hand, Customs could conceivably be more inclined to make another attempt to revoke First Sale and Congress may not be as sympathetic to industry opposition because of the limited use of First Sale by U.S. importers. On the other hand, the concentration of First Sale use in some sectors (e.g., textiles, apparel and footwear) suggests that its elimination would have a negative impact on consumers and businesses, something the federal government is likely to avoid given the continued struggles of the U.S. economy. It is therefore anticipated that First Sale will remain available to U.S. importers for some time to come.

Best Practices

Finally, we present here some best practices that can help importers get the most out of their utilization of the First Sale Rule.

- Importers who are thinking of implementing First Sale should focus on vendors with whom they plan to stay for the foreseeable future. A good working relationship is a bonus because the vendor will be sharing confidential information with the importer's customs compliance team.
- The use of First Sale can be augmented by shifting certain administrative, service or other costs from the production facilities to a related middleman. These costs include overhead or service-related costs such as payments for managers, costs for sourcing or obtaining materials, payroll, accounting and legal expenses, and charges for non-production-related equipment. Once these costs are shifted from the books of the manufacturer to those of the related vendor, a further reduction in the dutiable First Sale price can be realized without affecting the purchase price between the U.S. buyer and the vendor.
- Since importers are obligated to exercise reasonable care when declaring entry data, they should work with their vendors to ensure that First Sale invoices are properly prepared.
- It is critical that First Sale transactions be carefully developed. While the concept has been in place for some time most importers are unsure of how to construct a compliant document trail. However, with careful planning and coordination with suppliers overseas it is a goal that can be achieved and will be well worth the effort. ❑

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Snapshots

BY REUTERS

Canada

Canada Regulators Propose OTC Derivatives Rules

Canadian regulators are recommending mandatory electronic trading and central clearing of some over-the-counter derivatives as part of a global push to strengthen financial markets.

In a consultation paper, the Canadian Securities Administrators said its recommendations are in line with a G20 commitment to bolster transparency in markets.

Canadian regulators are recommending mandatory electronic trading and central clearing of some over-the-counter derivatives as part of a global push to strengthen financial markets.

As with the U.S. Dodd-Frank Wall Street reform bill, which aims to force most OTC derivatives through clearinghouses and transparent trading venues, Canadian regulators also are proposing mandatory reporting of all derivatives trades by Canadian counterparties to a trade repository. They also seek to impose capital and collateral requirements to effectively manage risks, according to the paper. Regulators recommend exemptions for some specialized users, and say surveillance of OTC derivatives markets should be stepped up.

China

China Introduces CDS-like Products on Trial Basis

China unveiled rules governing credit derivatives akin to credit default swaps (CDS), to lay the groundwork for a trial and prepare its fledgling bond market for the trade of riskier products.

Companies wishing to trade in the derivatives, called "credit risk mitigation tools" (CRM), must have registered or net capital of at least 800 million yuan ($120 million), said the National Association of Financial Market Institutional Investors (NAFMII). Core traders, who will be able to create CRM products, must have capital of 4 billion yuan, it said.

The rules go into immediate effect, said NAFMII, an industry body under the People's Bank of China.

Top Chinese leaders, after a four-day meeting this month that settled the nation's next five-year development plan starting in 2011, pledged major reform to let small companies issue high-yielding products -- a move that creates the need for derivatives to hedge risk.

Colombia

Colombia Takes Measures Against Strong Peso

Colombia announced measures to help counter the rise of its peso currency that included keeping money abroad, buying dollars in forwards markets and helping industry by cutting import tariffs.

The government said it would reduce its general average import tariff rate to 8.2 percent from 12.2 percent to help industry competitiveness. The government also said that it had eliminated a tax exemption on interest from foreign loans, as a way to discourage external debt.

Separately, the central bank board decided to continue its dollar-buying program until at least March 2011.

Germany

Germany Backs Tougher Bank Law on Securitization

Germany's lower house of parliament approved new guidelines that will force its banks to retain a bigger share of risks in securitized products.

The approval of the bill by the Bundestag lower house means banks will have to keep on their books at least five percent of risks from assets like loans and mortgages bundled together and resold as so-called asset-backed securities (ABS).

The new German bill was the result of a mediation committee between both houses of parliament, meaning that its passage through the Bundesrat upper house should be a formality.

To further cut risks, the bill also caps the size of claims one bank can make on another to 25 percent of the lender's equity capital and sets out to ensure that cooperation between national supervisory authorities in the EU is improved.

Global

Emerging Market Policymakers Vow to Combat New Fed Easing

The U.S. Federal Reserve committed to buy $600 billion more in government bonds by the middle of next year in an attempt to breathe new life into a struggling U.S. economy, in a move that quickly spurred policy makers from the world's new economic powerhouses in Latin America and Asia to seek fresh measures to curb capital inflows.

The U.S. central bank, seeking to lower borrowing costs for consumers, said it would buy about $75 billion in longer-term Treasury bonds per month.

Emerging economies expressed displeasure, making any substantive deal on global imbalances and currencies at next week's Group of 20 meeting that Seoul is hosting even less likely.

South Korea's Ministry of Finance and Strategy said it would "aggressively" consider controls on capital flows. Brazilian Finance Minister Guido Mantega said the country will use the upcoming G20 meeting as a forum to complain about the Fed's decision, and the foreign trade secretary warned of possible "retaliatory measures."

Thailand raised the possibility of concerted action to combat the flood of investment dollars that are expected to wash into into emerging markets, and said the region's central bankers were ready to impose measures to curb speculative inflows.

India will keep all options on the table to handle a surge of capital inflows, but is not in favor of direct controls, said Kaushik Basu, the Finance Ministry's chief economic adviser said.

Xia Bin, an adviser to the Chinese central bank, bluntly warned in the Chinese language Financial News that Beijing would pursue its own interests, saying: "We must think 'what is good for us'."

Russia

Russia Aims to Ease Companies' IPOs Abroad

Russia aims to lift restrictions on Russian companies' initial public offerings on international bourses once a long-awaited law on insider trading comes into force, the head of the financial market watchdog told Reuters. Vladimir Milovidov, head of the FSFR regulator, described the IPO restrictions, imposed in 2010, as a "temporary, forced measure," but said they would not be lifted in the "very short term."

He said the lack of a law on insider trading was one the biggest obstacles preventing FSFR from easing the curbs, which cap at 25 percent the stake that a Russian firm can offer on an international bourse. He also cited the lack of a clearing law and uncertainty over a central securities depository as the other hurdles.

United Kingdom

Companies Brace for UK Bribery Act Wake-up Call

British and overseas companies with businesses in the UK are in a race to tighten ethical procedures as the country poises to impose one of the most draconian anti-corruption laws in the world.

> **Multinational firms with businesses in the UK have demanded clarification of the Bribery Act's new rules, which are expected to hit those industries especially relying on myriad overseas partners, such as oil and gas, pharmaceuticals, insurance and private equity.**

The Bribery Act, due to come into effect next April, has unsettled those eyeing a new offence of failure to prevent bribery, which makes businesses with any UK interest criminally liable if staff, subsidiaries, intermediaries or "associated persons" offer bribes on their behalf across the world.

The planned act is more draconian than the relatively fierce U.S. Foreign Corrupt Practices Act (FCPA), for it also bans the bribery of people other than public officials as well as "facilitation payments" -- to speed up services such as visa applications or approval for aircraft take-off slots.

Multinational firms with businesses in the UK have demanded clarification of the new rules, which are expected to hit those industries especially relying on myriad overseas partners, such as oil and gas, pharmaceuticals, insurance and private equity.

United States

Republicans Ability to Reshape Dodd-Frank Limited

Republican lawmakers vowed to vigorously oversee the new financial reform law but stopped

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Snapshots, from page 11

short of promising major changes to legislation they have described as "job killing."

Following their capture of the House of Representatives in Tuesday's elections, Republicans took a cautious approach to the overhaul of financial regulation passed last summer, reflecting the likelihood that any major legislative changes would likely fall flat in the face of Democrats' control of the Senate and White House veto power.

House Republican leader John Boehner, who is expected to become House Speaker in January, predicted the regulatory overhaul would be subject to significant oversight by Congress.

The U.S. Treasury Department is seeking comment on whether exempting foreign-exchange swaps and forwards from new derivatives rules being developed by the Commodity Futures Trading Commission might create a systemic risk for the economy.

Spencer Bachus, in line to become chairman of the House Financial Services Committee but facing competition from Republican colleague Ed Royce, said he would conduct "vigorous oversight" of financial regulators writing hundreds of new rules to carry out the reform law. Such tactics can pressure regulators to soften their rules.

Lawmakers said some changes to the law would likely be attempted in the areas of derivatives regulation, credit rating agency liability and the setup of the Consumer Financial Protection Bureau, which will be funded by the Federal Reserve and not through congressional appropriations.

Bachus also wants to tweak new rules for the $615 trillion over-the-counter derivatives market.

Senator Jack Reed, a senior Democrat on the Senate Banking Committee, said Democrats would not let Republicans "gut important measures" designed avert another financial crisis.

Analysts said banks and other financial services companies are unlikely to see any further legislative crackdowns and can now focus on implementation of existing law.

No U.S. Decision on World Accounting Before 2011

U.S. securities regulators are grappling with how to transition companies to international accounting rules and will not make the decision to do so before 2011, the Securities and Exchange Commission said. In its first report on the U.S. plan to converge domestic accounting rules with international rules, the SEC said work was continuing and was not expected to be done until next year.

That means the SEC will not be able to decide before 2011 whether to forgo U.S. Generally Accepted Accounting Principles (GAAP), which U.S. publicly traded companies now use, for the International Financial Reporting Standards, which are used in more than 100 countries.

The SEC is under pressure to allow U.S. companies to make the switch, but it has concerns, including whether the international accounting rule maker is truly independent and whether IFRS is high quality.

Sir David Tweedie, chairman of the International Accounting Standards Board, said efforts to create a single global accounting system will be set back a generation if they do not succeed within 12 to 15 months. If the SEC decides against joining, or delays its decision, political pressure on the IASB would mount, Tweedie said. There is already "silent pressure" to remove U.S. members from the IASB because the country still uses GAAP.

U.S. Treasury Seeks Comment on Forex Swaps

The U.S. Treasury Department is seeking comment on whether exempting foreign-exchange swaps and forwards from new derivatives rules being developed by the Commodity Futures Trading Commission might create a systemic risk for the economy.

Treasury Secretary Timothy Geithner is authorized by the Dodd-Frank regulatory overhaul to decide whether foreign exchange swaps or forwards, or both, merit an exemption from the CFTC rules. Interested parties have until Nov. 29 to offer an opinion. The department said in a Federal Register notice that it had made no determination of whether an exemption is warranted.

Among questions it raised are whether "required trading and clearing of foreign exchange swaps and foreign exchange forwards would create systemic risk, lower transparency, or threaten the financial stability" of the country. ❏

Pacific Exchange Rate Services Exchange Rates for the Dollar as of November 9, 2010

The table below gives the rates of exchange for the U.S. dollar against various currencies as of November 9, 2010. All currencies are quoted in foreign currency units per U.S. dollar except in certain specified areas. All rates quoted are indicative. They are not intended to be used as a basis for particular transactions. Pacific Exchange Rate Services (http://pacific.commerce.ubc.ca) does not assume responsibility for errors.

	Currency	Value of U.S. Dollar	Country	Currency	Value of U.S. Dollar	Country	Currency	Value of U.S. Dollar
Afghanistan	Afghani	45.2	Georgia	Lari	1.765	Norfolk Islands	Aus. Dollar	0.9846
Albania	Lek	99.505	Germany	Euro*	1.3921	Norway	Krone	5.802
Algeria	Dinar	73.575	Ghana	Cedi	1.436	Oman Sultanate	Rial	0.3851
Andorra	Euro*	1.3921	Gibraltar	Br. Pound*	1.6155	Pakistan	Rupee	85.31
Angola	Kwanza	90.25	Greece	Euro*	1.3921	Panama	Balboa	1.00
Antigua	E.Car. $	2.7	Greenland	Dan. Krone	5.3547	Papua N.G.	Kina	2.6385
Argentina	Peso	3.9621	Grenada	E.Car. $	2.7	Paraguay	Guarani	4900.00
Armenia	Dram	364.75	Guadeloupe	Euro*	1.3921	Peru	Nuevo Sol	2.7957
Aruba	Guilder	1.79	Guam	US$	1.00	Philippines	Peso	43.4
Australia	Dollar	0.9846	Guatemala	Quetzal	8.005	Pitcairn Island	NZ Dollar	1.2659
Austria	Euro*	1.3921	Guinea Republic	Franc	7002.50	Poland	Zloty	2.8141
Azerbaijan	Manat	4606.50	Guinea Bissau	CFA Franc	472.02	Portugal	Euro*	1.3921
Azores	Euro*	1.3921	Guyana	Dollar	204.95	Puerto Rico	US$	1.00
Bahamas	Dollar	1.00	Haiti	Gourde	39.71	Qatar	Riyal	3.6411
Bahrain	Dinar	0.377	Heard/McDonald Is.	Aus. Dollar	0.9846	Rep. Yemen	Rial	208.55
Bangladesh	Taka	70.325	Honduras	Lempira	18.895	le de la Reunion	Euro*	1.3921
Barbados	Dollar	2.00	Hong Kong	Dollar	7.7513	Romania	Leu	3.6411
Belarus	Ruble	3025.00	Hungary	Forint	196.78	Russia	Ruble	30.652
Belgium	Euro*	1.3921	Iceland	Krona	110.59	Rwanda	Franc	591.80
Belize	Dollar	1.95	India	Rupee	44.325	Samoa (American)	US$	1.00
Benin	CFA Franc	472.02	Indonesia	Rupiah	8907.50	San Marino	Euro*	1.3921
Bermuda	Dollar	1.00	Iran	Rial	10368.00	Sao Tome/Principe	Dobra	17632.00
Bhutan	Nguitrum	44.325	Iraq	Dinar	1169.00	Saudi Arabia	Riyal	3.7502
Bolivia	Boliviano	7.020	Ireland	Euro*	1.3921	Senegal	CFA Franc	472.02
Bosnia Herzegovina	Konv. Marka	1.340	Israel	New Shekel	3.629	Serbia/Montenegro	Yug. N. Dinar	N/A
Botswana	Pula	6.4725	Italy	Euro*	1.3921	Seychelles	Rupee	12.236
Bouvet Island	Krone	N/A	Jamaica	Dollar	85.025	Sierra Leone	Leone	4156.60
Brazil	Real	1.6942	Japan	Yen	80.627	Singapore	Dollar	1.2839
Brunei	Dollar	1.2837	Johnston Island	US$	1.00	Slovakia	Koruna	21.641
Bulgaria	Lev	1.405	Jordan	Dinar	0.7077	Slovenia	Tolar	N/A
Burkina Faso	CFA Franc	472.02	Kazakhstan	Tenge	147.58	Solomon Is.	Solomon$	7.485
Burundi	Franc	1231.30	Kenya	Shilling	80.45	Somali Rep.	Shilling	1584.00
Cameroun	CFA Franc	472.02	Kiribati	Aus. Dollar	0.9846	South Africa	Rand	6.8164
Canada	Dollar	0.999	Korea, North	Won	1.18	Spain	Euro*	1.3921
Cape Verde Islands	Escudo	78.532	Korea, South	Won	1113.30	Sir Lanka	Rupee	111.61
Cayman Islands	Dollar	0.82	Kuwait	Dinar	0.2804	St. Helena	Br. Pound*	1.6155
Cent. Af. Republic	CFA Franc	472.02	Kyrgyzstan	Som	47.741	St. Kitts	E. Car. $	2.7
Chad	CFA Franc	472.02	Laos	Kip	8029.50	St. Lucia	E. Car. $	2.7
Channel Islands	Br. Pound*	1.6155	Latvia	Lat	0.5095	St. Pierre/Miq'lon	Euro*	1.3921
Chile	Peso	476.65	Lebanon	Pound	1500.50	St. Vincent	E. Car. $	2.7
China	Renminbi	6.6434	Lesotho	Maloti	6.8164	Sate of Cambodia	Riel	4074.00
Christmas Islands	Aus. Dollar	0.9846	Liberia	Dollar	70.50	Sudan	Dinar	N/A
Cocos Islands	Aus. Dollar	0.9846	Libya	Dinar	1.2266	Suriname	Dollar	2.745
Columbia	Peso	1833.80	Liechtenstein	Sw. Franc	0.9631	Swaziland	Lilangeni	6.8164
Comoros Rep.	Franc	352.60	Lithuania	Litas	2.4802	Sweden	Krone	6.6866
Congo Republic	CFA Franc	472.02	Luxembourg	Euro*	1.3921	Switzerland	Franc	0.9631
Congo Dem Rep.	Franc	N/A	Macau	Pataca	7.981	Syria	Pound	46.38
Costa Rica	Colon	519.39	Macedonia	Dinar	40.97	Taiwan	Dollar	30.144
Cote d'Ivoire	CFA Franc	472.02	Madagascar	Franc	8547.00	Tajikistan	Somoni	N/A
Croatia	Kuna	5.2838	Madeira	Euro*	1.3921	Tanzania	Shilling	1487.50
Cuba	Peso	1.00	Malawi	Kwacha	151.52	Thailand	Baht	29.505
Cyprus	Pound	0.4236	Malaysia	Ringgit	3.0968	Togo Rep.	CFA Franc	472.02
Czech Repub.	Koruna	17.66	Maldive Is.	Rufiyan	12.800	Tokelau	NZ $	1.2659
Denmark	Krone	5.3547	Mali Republic	CFA Franc	472.02	Tonga Island	Pa'anga	1.81
Djibouti	Franc	177.72	Malta	Lira	0.3084	Trinidad/Tobago	Dollar	6.29
Dominica	E.Car. $	2.7	Martinique	Euro*	1.3921	Tunisia	Dinar	1.3951
Domi. Rep.	Peso	37.25	Mauretania	Ouguiya	282.00	Turkey	Lira	1.4062
Dronning Maud.	Nor. Krone	5.802	Mauritius	Rupee	29.696	Turkmenistan	Manat	14250.00
East Timor	US$	1.00	Mexico	New Peso	12.181	Turks & Caicos	US$	1.00
Ecuador	US$	1.00	Moldova	Lei	11.53	Tuvalu	Aus. Dollar	0.9846
Egypt	Pound	5.7467	Monaco	Euro*	1.3921	Uganda	Shilling	2285.00
El Salvador	Colon	8.7475	Mongolia	Tugrik	1283.50	Ukraine	Hryvnia	7.9226
Eq'tl Guinea	CFA Franc	472.02	Montserrat	E.Car. $	2.7	United Kingdom	Br. Pound*	1.6155
Eritrea	Nafka	13.64	Morocco	Dirham	8.0958	Uruguay	Peso	19.95
Estonia	Kroon	11.238	Mozambique	Metical	36000.00	U.A.E.	Dirhan	3.6727
Ethiopia	Birr	16.5	Myanmar	Kyat	6.42	Uzbekhistan	Som	1629.30
European EMU	Euro*	1.3921	Namibia	Dollar	6.53	Vanuatu	Vatu	92.695
Faeroe Islands	Dan. Krone	5.3547	Nauru Is.	Aus. Dollar	0.9846	Vatican City	Euro*	1.3921
Falkland Islands	Br. Pound*	1.6155	Nepal	Rupee	70.88	Venezuela	Bolivar	4.29
Fiji	Dollar	1.8018	Neth. Antilles	Guilder	1.79	Vietnam	Dong	19498.00
Finland	Euro*	1.3921	Netherlands	Euro*	1.3921	Virgin Islands BR	US$	1.00
Fr. Pacific Islands	Franc	85.469	New Zealand	Dollar	1.2659	Virgin Islands US	US$	1.00
France	Euro*	1.3921	Nicaragua	Cordoba	21.728	West Samoa	Tala	2.13
French Guiana	Euro*	1.3921	Nieue	NZ Dollar	1.2659	Zambia	Kwacha	4640.00
Gabon	CFA Franc	472.02	Niger Rep.	CFA Franc	472.02	Zimbabwe	Dollar	N/A
Gambia	Dalasi	28.480	Nigeria	Naira	150.30			

(N/A) Not Available * U.S. Dollar per national currency unit

Global Economy

***Bad Signals*, from page 2**

We don't know how many steps there are between a currency war and a trade war. What we know is that it starts with competitive devaluations and ends seriously compromising international trade relations and geopolitical stability.

other currencies. The interventions by central banks in Japan, Switzerland, and a number of emerging economies (these in terms of capital controls) are worrisome. The renewed quantitative easing not only disturbs the implementation of monetary policies worldwide, but also makes it more difficult in some economies to absorb foreign capital flows, as a result of excessive appreciation of some currencies. That expectation of appreciation encourages capital outflows from economies with lower interest rates. The situation poses a trilemma for emerging economies: an inability to simultaneously adopt an autonomous monetary policy coupled with free movement of capital and exchange rate stability. We could be witnessing a spiral of protectionism starting with currency actions that could escalate into financial and even trade protectionism. The global trade and investment system needs stability, especially during these tough times of crisis and slow recovery.

These unresolved tensions will continue to monopolize the agenda for the G20 summit. We would like to point out, however, that the solution cannot be reduced to making the yuan exchange regime more flexible. It is also necessary to revisit essential aspects of the global financial architecture, including exchange rate regimes, which was the main task assigned to the IMF at the Bretton Woods conference in 1944. The IMF has recently taken decisive steps in this direction, not only changing the arithmetic of country representation and decision-making procedures but also acknowledging the various lessons about macroeconomic policy that have emerged from the crisis. It is healthy to engage in this "macroeconomic revisionism," especially if it comes together with consensus building and power sharing in the global economy.

Tim Geithner's proposal to place upper limits on deficits is worth considering. John Maynard Keynes made a similar proposal at Bretton Woods, and it was rejected by the U.S. While these type of proposals undermine national economic and trade sovereignty, global integration per se—well before placing limits on deficits have been under discussion—is the prime limitation on national policymaking. The persistence of large global imbalances continues to threaten financial stability. We must resist the temptation to protect and bet instead on cooperative solutions, unless we want to set the clock back to the 1930s. As Mark Twain famously argued, "history does not repeat itself, but it rhymes." ❑

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M&A

***Latin America Is In Good Shape*, from page 1**

After a decline of 1.9 percent in 2009, estimated GDP growth this year for Latin America is once again projected to be more than 5 percent. Brazil's GDP growth this year is estimated to be 7.6 percent, the highest in Latin America.

Last year (2009), the worst economic performer in Latin America was Mexico, which suffered a 6.5 percent fall in its gross domestic product (GDP). The reason for this decline was that more than 80 percent of Mexico's exports were manufactured goods sent mostly to the United States. Mexican exports are doing better this year because of the modest economic recovery in the United States. In 2009, when the economies of most Latin American countries declined, Argentina had positive GDP growth (0.9 percent) and Brazil had only a small GDP decline (0.2 percent) because China's strong demand for the soybeans of both countries compensated for weakness in their exports to other countries. The pattern of economic growth in China has contradicted what Prebisch fervently believed—that commodity prices would inevitably decline while prices for manufactured goods would increase over time. Prebisch did not live long enough to experience the emergence of China. Commodity prices have long been volatile, and at some point in the future, commodity prices will likely decline as China's economic needs change.

Latin America's average annual GDP growth was more than 5 percent a year from 2004 through 2008. After a decline of 1.9 percent in 2009, estimated GDP growth this year for Latin America is once again projected to be more than 5 percent. Brazil's GDP growth this year is estimated to be 7.6 percent, the highest in Latin America. Other than Haiti, which has suffered from natural disasters, Venezuela is the only country in Latin America in which GDP is expected to decline this year.

Foreign direct investment (FDI) into Latin America and the Caribbean grew in this century from an annual average of $66 billion a year from 2000 through 2005 to a high of $132 billion in 2008. FDI dropped sharply by $55 billion in 2009, but is expected to climb to more than $100 billion this year. According to ECLAC, most FDI in manufacturing is concentrated in low and medium-low technology intensive activities—a situation that does not augur well for the future of the region.

The other feature for which Latin America was noted in the past was its high inflation. If one used the word "inflation," an immediate association 15 or more years ago was "Latin America." This was because fiscal deficits were common, which made currency devaluations necessary, and the devaluations frequently came at or near the end of administrations. Most Mexicans understood this, and before each sexenio (six-year term of office) ended, there were large-scale withdrawals of pesos from bank accounts to put these assets into some other currency or activity that held its value. When I lived in Chile in the latter 1960s, one expected annual inflation to be about 30 to 50 percent and it made little sense to retain a large bank balance, especially as one administration was giving way to the next. Chile's annual inflation in 2009 was 1.5 percent. The average for Latin American inflation in 2009 was 5.8 percent. The one country in the region where inflation remains high is Venezuela; last year, it was more than 28 percent.

Latin American countries tended to be pessimistic about export prospects for much of the 20th century. The argument given was that if particular exports thrived in the U.S. market, the United States would institute protectionist measures. In fact, this was common. Tomatoes and avocados from Mexico faced severe protectionism for many years. So did inexpensive imports from developing countries worldwide—in particular for textile products. Pascal Lamy, head of the World Trade Organization, noted that the United States collected $30 million in tariffs on $3 billion of French goods imported in January 1996 and also collected $30 million in tariffs on $200 million of goods imported that month from Cambodia. Ed Gresser, of the Progressive Policy Institute, has noted that in 2003, U.S. tariffs on $2 billion of imports from Bangladesh (hats, clothing, shrimp, and jute) were $300 million, while U.S. tariffs on $42 billion of imports from the United Kingdom were only $435 million.

The main advantage that Mexico has in the U.S. market is proximity; this is especially valuable for heavy goods that are costly to ship over long distances, but not sufficient for the generality of Mexico's exports to be competitive in the U.S. market.

U.S. protectionism has diminished considerably from what it was some 15 years ago, but is not completely absent. The United States has signed three free trade agreements (FTAs)—with Korea, Colombia, and Panama—that it has not ratified, primarily because of opposition from U.S. labor

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***Latin America Is In Good Shape*, from page 15**

unions. The Colombia case has led to some interesting anomalies. Most imports from Colombia enter the United States free of import duties, thanks to the U.S. system of preferences for developing countries. However, the lack of a formal agreement results in discrimination against U.S. exports to Colombia. Canada and the European Union have negotiated FTAs with Colombia that remove the import duties that must be paid on their goods when shipped to Colombia—import duties that U.S. exporters must still pay when their goods enter Colombia.

Mexico, between 1995 and 2005, exported more goods than all other Latin American and Caribbean (LAC) countries combined. However, Mexico's share of LAC exports began to decline in 2001 while those from the rest of the LAC region started to increase at about the same time. ECLAC estimates that Mexico's share of LAC exports will be 32 percent in 2010 compared with 39 percent for the rest of LAC. Brazil's export share was projected to be 23 percent of the LAC total this year. Mexico faces sharp competition from China in the export of manufactured goods because Chinese wages are lower than those in Mexico.

These realities indicate that Mexico has some hard economic decisions to make. Mexico cannot rely on low wages to be competitive in the U.S. and LAC markets because China's wages are lower. Mexico's industrial productivity (output per unit of input) is not particularly high—and it will take higher productivity to make many Mexican manufactured goods competitive with those from China. The main advantage that Mexico has in the U.S. market is proximity; and this is especially valuable for heavy goods that are costly to ship over long distances, but not sufficient for the generality of Mexico's exports to be competitive in the U.S. market.

Mexico, therefore, has to build further on the advantages of proximity to be competitive with China in the United States. Proximity makes it possible for joint production of products in the two countries to exploit U.S. capital intensity with Mexico's lower wages—to be able to ship intermediate products back and forth between the two countries without high shipment costs. This was the merit of the maquiladoras, under which partially completed goods were sent from the United States to Mexico, where production was completed, exploiting the relatively lower labor costs in Mexico. The proximity also allows for just-in-time (jit) inventory accumulation to reduce inventory costs. As Mexico looks ahead to its competitive challenge from China, it must be highly flexible in its manufacturing processes and must build on every conceivable advantage—lower transport costs, smaller inventories, jointly producing with U.S. companies, and the capacity to ship intermediate goods back and forth as many times as needed as long as this lowers production costs. This will work only when there are no tariffs or other impediments in the trade between Mexico and the United States.

Except in locations near its northern border from which fresh fruits and vegetables can be shipped cheaply into the United States, Mexico will have to rely largely on its manufacturing competitiveness for its well-being. Indeed, Mexico has been gathering experience in accomplishing this. When China entered world markets for manufactured goods, few countries were as vulnerable as Mexico in maintaining its largest market. Mexico cannot extricate itself from this reality. The future economic progress of Mexico depends a great deal on Mexican producers and shippers learning how to best cope with this immense problem of competing with China in the U.S. market. ❏

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