

The Economic Impact Of Violence in Mexico

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The new upswing in insecurity and criminal violence in Mexico has many causes, but two are decisive and structural. The first is mass unemployment and the absence of economic and educational expectations for millions of young people; the second is the breakdown of the institutions involved in the administration of justice and crime prevention. The insecurity-violence binomial is an increasingly complex phenomenon rapidly weakening the fabric of society and inhibiting productive activities in general, particularly business activities, in broad regions of the country. It is already considered a risk factor for the economy as a whole by some financial institutions like the Bank of Mexico, the country's central bank.

The liberal economic model, based on deregulation of markets and the withdrawal of the state from promoting the

economy, has brought about a cycle of low growth—even stagnation—that has accentuated poverty and social disparities. The country's economic move backwards coincides with the lack of efficacy and credibility of government institutions in charge of guaranteeing the security of persons and their property, a basic function of the national state.

The economy's sluggish performance and the weakening of government institutions have sparked a chain of negative incentives such as impunity and the structural corruption of police forces, among other phenomena, that favor an expanding informal economy and organized crime activities linked mainly, but not exclusively, to the traffic in narcotics. Rigorously speaking, the millions of dollars in business done by these organizations, converted *de facto* into powerful corporations, are an extreme expression of the informal economy.

The patterns of functioning and the structures of the criminal organizations come very close to the modern definition of a corporate firm: a hierarchical organization with internal and external rules, based on certain values and objectives

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of profitability and social recognition. From this point of view, the narco-corporations are something more complex than the common image of simple bands of criminals with no rules, no strategy, and no organizational logic, completely dependent on a nucleus of bosses and groups of armed men.

The proliferation of the criminal corporations and the territorial influence they exercise in different regions has generated a “national map of insecurity” and systemic criminal violence. This is how a scenario of social instability emerges, experienced and perceived in different ways by different sectors of society. So, I will make a preliminary exploration of some of the many complex economic effects of insecurity and the violence associated with criminal corporations nationwide.

ECONOMIC FAILINGS, INCENTIVES FOR THE INFORMAL ECONOMY

The expansion of criminal activities should be situated in the economic and social context molded over the last 25 years by the economic model that concentrated income and wealth, creating social exclusion. This model prompted a first stage of stagnation and is currently going through a phase of slow growth.

In accordance with the dictates of orthodox liberal economics, the strategic withdrawal of the state from the promotion of growth and development created a situation in which the growth dynamic gravitated around national and foreign private investment and international trade, mainly with the United States. The decrease in social rights (employment, health, education, and culture) has regressively altered the *distribution of social risks*. The liberal state’s refusal to uphold these rights re-launched the family, in any of its forms, as the main refuge of security for individuals.¹

In Mexico, almost 50 percent of the population lives at some level of poverty, and more than half the work force participates in the informal economy, which makes up 30 percent of the gross domestic product (GDP), more than in Chile and Costa Rica, and less than Bolivia or Peru’s 60 percent. Things

are not going very well in the Mexican economy’s formal sector either if we take into account that the purchasing power of real wages dropped one-fourth from 1980 to 2010.²

Economic inequality in Mexican society is caused by the advancing concentration of wealth and social privileges. According to International Labor Organization (ILO) estimates, the urban unemployment rate in 2012 will be 6.1 percent of the work force, and the informal economy will absorb 54.25 percent of jobs.³ Every year, 900 000 more people join or rejoin the work force.

In 2012, 500 000 will join the formal sector and 400 000, the informal sector. The economy will grow at a relative rate of 3.6 percent, which can be considered a very poor performance compared with the demand for jobs. In these conditions, it is understandable that the economy’s mediocre performance created a structure of incentives that stimulates the informal sector.

INCENTIVES FOR CRIMINAL ORGANIZATIONS

The informal economy spans a diversity of mechanisms for obtaining a job and an income, an economic space that is reaffirmed as the “last-resort option” for millions of people. It is characterized by a broad range of alternatives, from precarious jobs to illicit itinerate sales, which offer attractive profits but are high risk, like moving around drugs or adulterated alcohol and even trafficking in persons.

By definition, in Mexico, this sector does not comply with the basic institutional norms of a market economy: paying taxes, making social security payments, obtaining sanitation certificates, respecting copyright laws, paying royalties, etc. An extreme form of this are the criminal organizations based mainly, but not exclusively, on the production and distribution of illegal drugs inside and outside Mexico.

The economic variables of the crisis are only one dimension that partially explains the origin of the criminal organizations. It is therefore necessary to integrate the institutional dimension into the analysis. This is identified as the unspoken “rules of the game” that make criminal activities possible, such as active or passive collusion between segments of the municipal, state, and federal government bureaucracy and the criminal organizations.

The institutions’ progressive deterioration contributes to the increased climate of violence, of intolerance in society, and

non-compliance with the law. In 2009, of almost 70 000 investigations initiated into violent crimes, fewer than 10 percent ended in charges being brought. In these conditions, the drop in the number of people who even make complaints about crimes against them can be attributed to the fact that Mexicans consider it a waste of time to make a complaint or file charges; this is an expression of the citizenry's mistrust of the institutions.⁴

THE MAP OF INSECURITY AND VIOLENCE IN MEXICO

Contrasting with the government's discourse presented in costly media campaigns to convince people of the achievements of the police-military strategy, critical points of view also exist questioning the orientation, advances, and social costs of President Calderón's policy. One notable exception is the article by Joaquín Villalobos, former commander of the Salvadoran guerrilla movement and currently an essayist and consultant on international conflicts. Villalobos disregards the idea that the criminal violence in Mexico is the consequence of a *failed government strategy*. He thinks it is the result of the cumulative effect of policies by different governments in recent years characterized by "an aversion to risk" that only sought to "manage the conflict."⁵ However, studies and reports on this topic put forward a different vision.

According to the Global Peace Index, Mexico has become one of the most insecure countries in Latin America, occupying 107th place out of a total of 149 countries in 2010, while in 2007, it was in 79th place. In 2010, 15 000 murders were committed, and more than 30 000 at the end of President Felipe Calderón's fifth year in office.⁶

With regard to how the population views the climate of insecurity, the "Index of Perception about Public Security" indicates that 60.7 percent of those polled in early 2011 thought criminal activity had gotten "worse" than the previous year, while 10.7 percent thought it was "much worse."⁷

The United Kingdom Foreign and Commonwealth Office distributed a diagnostic analysis underlining the increasing gravity of insecurity and the risks in Mexican territory. The alert classified half the country, spanning 15 states, as risky for travelers. Concerned about the safety of their citizens visiting the country, the governments of Australia, the United States, France, Italy, Spain, and Germany have also drawn up lists of insecure areas in Mexico.⁸

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In short, it can be said that the results of the government strategy in its fight against the criminal organizations are the object of controversy, and we cannot say there is consensus around it. Both inside the country and abroad, critics question the rigidity of the President Calderón's policy, its advances, and the social costs.

THE INSECURITY-VIOLENCE BINOMIAL, RISK FACTOR FOR THE ECONOMY

The cycle of violence and insecurity sharpens two characteristic traits of market economies regarding uncertainty and the risks with a negative impact on economic performance. Global financial corporation J. P. Morgan has fielded the idea that the greatest problem generated by the climate of insecurity and violence is missed business and investment opportunities. Their studies estimate a macro-economic cost of Mex\$195.72 billion (US\$15 billion), which represents between 1.0 and 1.5 percent of GDP.⁹

Fitch financial rating agency analyst Shelly Shetty has also warned that drug trafficking-related violence puts economic growth and investment flow at risk. And, in an unprecedented report titled "Mexico: Who Let the Dogs Out?" Credit Suisse bank affirmed that insecurity was becoming a threat for national economic recovery expressed in a drop in investments and a rise in the cost of doing business.¹⁰

MICRO-ECONOMIC IMPACTS

At the micro-economic level, evidence exists suggesting that conditions for doing business in Mexico are deteriorating. Seven out of every ten businesses operating in the North have been affected by insecurity (66 percent of the firms consulted). At the same time, in the South, the impact is less than in the North: half the firms surveyed said their operations had not been hurt. Actually, the impact is diverse and varies from

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one region to another. Theft of merchandise is higher in the central part of the country, including Mexico City; in the North, telephone extortion by criminal gangs is more common, upping the cost of corporate security (see Table 1).¹¹

The climate of violence stimulates the emergence of a *new behavior pattern* by firms, aimed at protecting their business, property, and markets by negotiating new, costly insurance policies that allow them to protect and provide continuity in their transactions in local and foreign markets.

For businessmen, *adapting to the new environment* of insecurity and violence has meant increasing security personnel, acquiring electronic control units for protecting factories and distribution equipment (see Table 2). In extreme situations, companies and authorities on different levels of government will seek to preserve their commercial or bureaucratic interests with informal arrangements—voluntary or not—including extortion payments, ransoms, and protection payments to criminal organizations. In short, for companies, the insecurity-violence binomial has translated into a *negative externality* that demands extraordinary spending, different from traditional production costs.¹²

IMPACT ON THE CONSTRUCTION SECTOR

Certain experiences indicate that the business class in Mexico lacks a unified, coherent vision and an appropriate strategy to implement it. For Eduardo Correa Abreu, president of the Mexican Chamber of the Construction Industry, insecurity affects the businessmen's investment decisions in this strategic sector, such as what is happening in the *conflict zones* in north of the country.

Correa Abreu states that firms emigrate to the states offering greater security to company operations and workers. In cities considered poles of development like Monterrey, an important number of construction companies have stopped working. In 2009, 2010, and 2011, the list of construction companies in the state of Nuevo León dropped from 680 to 480. Ciudad Juárez, Chihuahua, is an extreme case, where the number of construction firms plummeted from 220 to 18.

Executives and shareholders of large national and foreign corporations have remained optimistic, minimizing the repercussions of the climate of insecurity and violence. Luis Zárate, executive vice-president of the Mexican multinational Ingenieros Civiles Asociados (ICA), asserts that the companies in his corporate group have not suffered insecurity to any degree that would be of concern. From that perspective, and from the position of strength made possible by a fortune estimated at US\$68 billion, Mexican magnate Carlos Slim thinks the problem of drug trafficking in Mexico should not be an impediment for businesspeople to continue to invest in the country.¹³

TABLE 1
IMPACT OF INSECURITY AND VIOLENCE ON FIRMS BY REGION (2011)
(% OF FIRMS AFFECTED)

Problem	North	Central North	Central Mexico	South
Theft of goods and inputs	22	32	42	29
Losses of future business or investments	27	24	15	35
Drop in sales	12	12	8	4
Insecurity of personnel	5	11	11	11
Rising security expenditures	7	8	5	3
Other crimes (includes extortion by telephone)	27	13	19	18

Source: Banco de México, "Reporte sobre las economías regionales. Enero-marzo de 2011," <http://www.banxico.org.mx/publicaciones-y-discursos/publicaciones/informes-periodicos/reportes-sobre-las-economias-regionales/>.

TABLE 2
ACTIONS TAKEN BY FIRMS FOR PREVENTION AND PROTECTION (2010)
(% OF FIRMS BY REGION)

Measure	North	Center North	Central Mexico	South
Hiring security personnel	20	21	39	24
Security cameras/alarms	18	22	18	17
Other preventive measures (changing delivery routes, satellite tracking, etc.)	11	13	11	15
Heightened security measures/more guards	10	12	10	14
Taking out a bond or insurance policy	9	13	7	4
Others ^a	33	19	14	26

^a "Others" includes changing working hours and days, restricting access to facilities, limiting the use of cash, making complaints to the police or bringing legal suit, and taking measures to support personnel.

Source: Banco de México, "Encuesta mensual de actividad económica en los sectores manufactureros y no manufactureros," December 2010, <http://www.banxico.org.mx/publicaciones-y-discursos/publicaciones/informes-periodicos/reportes-sobre-las-economias-regionales/>.

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for organizing the economy and the citizenry to contribute to overcoming the "state failure" manifest in the government's inability to ensure a climate of social stability favorable to production and development. ■■■

NOTES

Just to show the great disagreement prevailing in the business community, it should be mentioned that Gerardo Gutiérrez Candiani, recently elected as head of the Business Coordinating Council (CCE), made the surprising statement that what exists in Mexico is "a political system and institutions that are not democratic because they are the home of partisan and group interests." He went on to say that the political parties do not facilitate agreements and fail in their responsibility of achieving justice and ensuring respect for the law.¹⁴

He goes even further, stating that Mexico is facing a grave crisis in public security and its inability to achieve the economic growth that is both needed and that it has the potential for. He says that the country has moved toward a modern market economy, but continues to be one of the nations with the greatest social inequality and a chronic culture of illegality and impunity.¹⁵

We have seen, then, that the continuity in the flow of goods and services is strategic for the world of business and the economy as a whole. This is why recognizing insecurity as a risk factor poses the urgency of fostering new mechanisms

¹ David Ibarra, "El ahogo de la inseguridad," *El Universal* (Mexico City), July 16, 2011, p. 16.

² Organización Internacional del Trabajo, *Panorama laboral 2011 de América Latina y el Caribe* (Mexico City: OIT Lima, Oficina Regional para América Latina y el Caribe, 2012).

³ Ibid.

⁴ Alejandro Madrazo, *Un balance de la política de drogas en México* (Mexico City: CIDE, 2012).

⁵ Joaquín Villalobos, "Nuevos mitos de la guerra contra el narco," *Nexos* no. 409, January 2012.

⁶ Instituto para la Economía y la Paz, "Índice global de paz," <http://www.universitam.com/?p=154>.

⁷ "Barómetro de empresas," *Excelsior* (Mexico City), January 18, 2011, p. 8-D.

⁸ Silvia Otero, "Países alertan sobre peligros en México," *El Universal* (Mexico City), November 6, 2011, p. A-6.

⁹ J. P. Morgan, "Inseguridad cuesta 1.5% del PIB," *El Universal* (Mexico City), June 10, 2011, p. B1.

¹⁰ Fernando Franco, "Prevén invertir con cautela por inseguridad," *Excelsior* (Mexico City), January 18, 2011, p. 8.

¹¹ Banco de México, "Reporte sobre las economías regionales enero-marzo de 2011" (Mexico City: Banco de México, 2012).

¹² José Ayala, *Instituciones y economía. Una introducción al neoinstitucionalismo económico* (Mexico City: FCE, 1999).

¹³ "Violencia afecta inversión en construcción, dice CMIC," *El Universal* (Mexico City), August 27, 2011, p. A-12.

¹⁴ "Con cartera bajo el brazo," *Excelsior* (Mexico City), February 7, 2011, p. 3.

¹⁵ "Gobiernos, incapaces ante crimen, asegura Consejo Coordinador Empresarial," *El Universal* (Mexico City), March 2, 2012, p. A-12.