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Has the North American Free Trade Agreement fulfilled its promise? An assessment after 15 Years

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Abstract. Five years have passed since the North American Free Trade Agreement (NAFTA) celebrated its 10th anniversary. In that time, trade expansion among the United States, Mexico, and Canada continues to be strong, albeit in a more modest fashion than in the initial ten years of the agreement. This continued growth has not been without complications in the last five years, especially between the United States and Mexico. The corn and sugar trade have both sparked controversy, while trucking regulation remains an unresolved issue. Trade between the United States and Canada has largely been free of complications save for recent protectionist actions at the sub-national level. These actions are due to misunderstandings concerning the 2009 economic stimulus bill passed in the United States. Many new players have emerged in the free trade landscape since NAFTA's 10th anniversary. Foreign direct investment, imports, and exports have all grown exponentially between the United States and China. Despite rising trade friction due to the global recession of 2008–2009, the North American Free Trade Agreement continues to generate net positive economic benefits for all three signatories.

JEL classification: F10, F13, R11

Key words: Free, Trade, Mexico, China, United States

1 Introduction

In 2004, the North American Free Trade Agreement (NAFTA) celebrated its 10th anniversary. At that time, the agreement's effectiveness was analysed and results were presented and published as part of the proceedings of the Canada-United States Business Conference (Rugman 2004). Data pointed to NAFTA being a beneficial agreement among the three countries in question with foreign direct investment and trade growing substantially during the 10 year period. Each country also recorded employment growth, real income increases, and lower rates of inflation during the same period, though this growth was not without complications. Disputes among Canada, Mexico and the United States concerning such issues as timber, food products, and immigration were present during the first 10 years of NAFTA (Weinstein 2004).

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A current analysis of NAFTA's impact must be weighed with the knowledge that the playing field has changed radically within the span of the five years since its 10th anniversary. International trade patterns have been altered significantly with new free-trade deals, enlargement of the World Trade Organization (WTO), more foreign countries opening up to direct foreign investment (DFI), financial deregulation, and the explosion of China's economy (Engardio et al. 2008). To frame an analysis of NAFTA by considering only the cause and effect among the three countries would be myopic. The oft quoted 'giant sucking sound' has been moot for the last five years, replaced by a global breeze redistributing jobs, products, and migration across nations as the integrated economy warrants.

2 Continued growth

If one does focus solely on NAFTA's three member countries, evidence of continued economic growth is readily apparent. During the first 10 years of NAFTA, trade among the three countries grew exponentially; five years out, and that growth has continued, albeit in a more modest fashion. The United States continues its healthy export relationship with Canada as exports climbed from $189 billion in 2004 to $224 billion year-to-date October, 2008. Similarly, exports to Mexico rose from $110 billion to $129 billion in the same time span (Figure 1). A strong North American economy prompted imports to the United States to rise as well between 2004 and year-to-date October, 2008. Canada's exports to the United States increased at a steady pace from $255 billion to $293 billion; and, while still in the economic shadow of Canada, Mexico's exports rose from $155 billion to $186 billion (Figure 2). Table 1 highlights the most commonly traded products within NAFTA.

The overall balance of trade continues to be skewed heavily in favour of both Canada and Mexico. Upon closer examination, it should be noted that while the U.S. trade deficit with Mexico has increased sharply from $45 billion in 2004 to $74.6 billion in 2007, the U.S. deficit with Canada has fluctuated in the same time period, hitting a high of $78.4 billion in 2005 while sliding back to $68.1 billion in 2007 (Figure 3).

The acceleration of direct investment that was prevalent during the initial years of NAFTA has cooled somewhat (Figure 4). U.S. investment in Mexico has recovered from the economic turbulence wrought by the terrorist attacks of 11 September, 2001 but still hovers just under

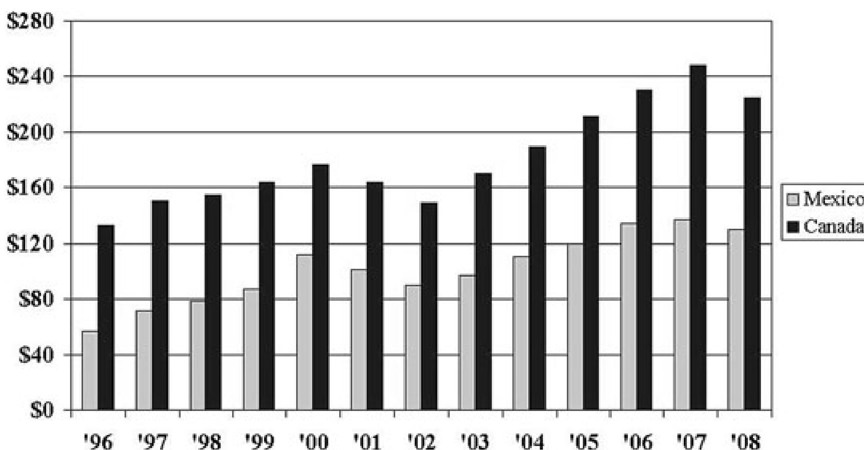

Fig. 1. U.S. exports to Canada and Mexico, 1996–2008 (in billions of U.S. dollars)
Source: U.S. Census Bureau (2008). 2008 data to October

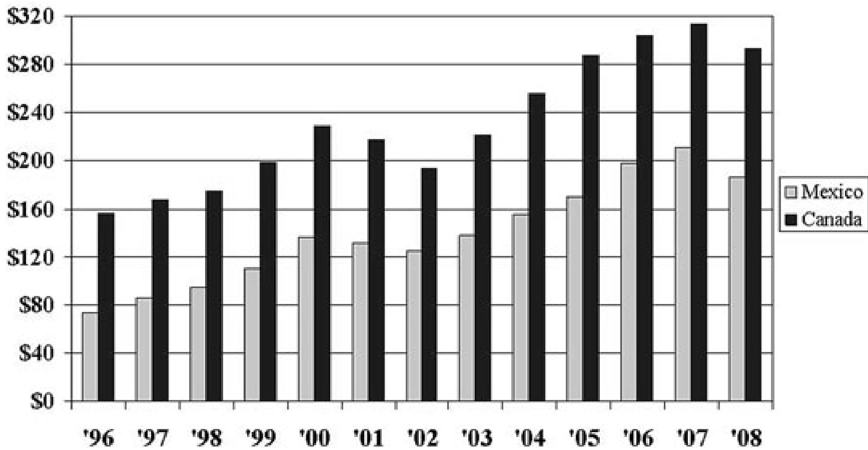

Fig. 2. U.S. imports to Canada and Mexico, 1996–2008 (in millions of U.S. dollars)
Source: U.S. Census Bureau (2008). 2008 data to October

Table 1. U.S. Trade with Mexico, 2007 (in millions of U.S. dollars)

Top U.S. Exports to Mexico		Top U.S. Imports from Mexico	
Total	132,033,941	Total	210,799,021
Computer and Electronic Products	22,951,638	Transportation Equipment	46,968,757
Transportation Equipment	17,322,558	Computer and Electronic Products	45,635,297
Chemicals	15,898,880	Oil And Gas	30,927,079
Machinery, Except Electrical	12,080,681	Electrical Equipment	17,347,470
Electrical Equipment	8,507,338	Machinery, Except Electrical	9,719,244
Food and Kindred Products	6,962,086	Primary Metal Manufacturing	6,492,320
Primary Metal Manufacturing	6,603,783	Misc. Manufactured Commodities	5,590,552
Plastics and Rubber Products	6,156,466	Fabricated Metal Products	5,532,261
Fabricated Metal Products	5,880,504	Agricultural Products	4,944,461
Petroleum and Coal Products	5,681,464	Apparel and Accessories	4,689,076
Agricultural Products	5,325,385	Chemicals	3,651,908
Special Classification Provisions	4,950,810	Petroleum and Coal Products	3,154,563
Misc. Manufactured Commodities	4,081,254	Food and Kindred Products	2,841,449
Paper	3,704,746	Special Classification Provisions	2,811,620
Textiles and Fabrics	2,654,050	Beverages and Tobacco Products	2,558,221
Waste and Scrap	1,225,219	Plastics and Rubber Products	2,410,484
Oil And Gas	1,026,043	Nonmetallic Mineral Products	2,389,407
Nonmetallic Mineral Products	1,021,036	Leather and Allied Products	1,701,273

Source: U.S. Census Bureau

$9 billion from 2004 through 2007. Direct investment in Canada by the U.S. has been uneven at best with 2004 and 2007 witnessing levels of over $20 billion, and 2005 and 2006 registering only $13.5 and $8.1 billion respectively. Direct investment in the U.S. by Canada and Mexico tells a similar story (Figure 5). Mexico's investment levels are nascent at best while Canada invested record levels in 2004 and 2007, and then recorded precipitous drops in the years, 2005 and 2006.

The data indicate that between the years of 2004 and 2008 NAFTA still exerted a positive influence on the economies of the United States, Canada and Mexico. The explosive growth that came during the initial ten years of the treaty has slowed, but remains steady. Granted, this

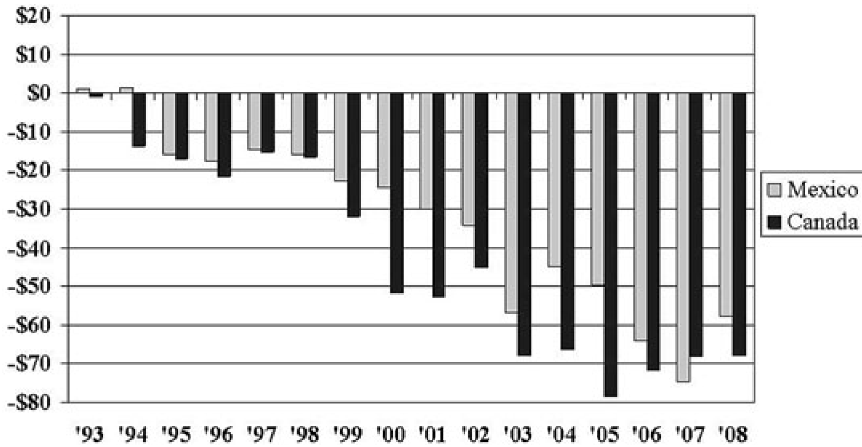

Fig. 3. U.S. trade balances, 1996–2008 (in millions of U.S. dollars)
Source: U.S. Census Bureau (2008). 2008 data to October

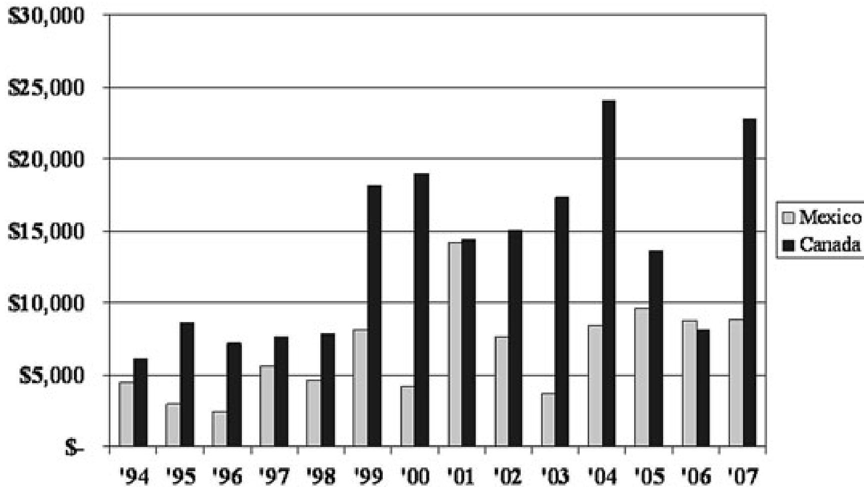

Fig. 4. Foreign direct investment by U.S. – capital outflows (in billions of U.S. dollars)
Source: U.S. Bureau of Economic Analysis (2008)

steady growth may soon see a drop similar in nature to the one witnessed after the terrorist attacks of 11 September, 2001. Although the authors only have access to year-to-date October 2008 data, the current global recession and financial meltdown may have an extended impact on the United States, Canada and Mexico, resulting in significantly weakened economic activity in regards to NAFTA throughout 2009 and into 2010.

3 Complications since 2004

During NAFTA's first 10 years, critics consistently levelled the charge against the treaty that Mexico would lure thousands of production jobs away from the United States. Indeed, a high number of jobs were relocated south of the Border, but not to the degree that many predicted, nor to the overwhelming destruction of the U.S. economy (Weinstein 2004; Engardio et al. 2008;

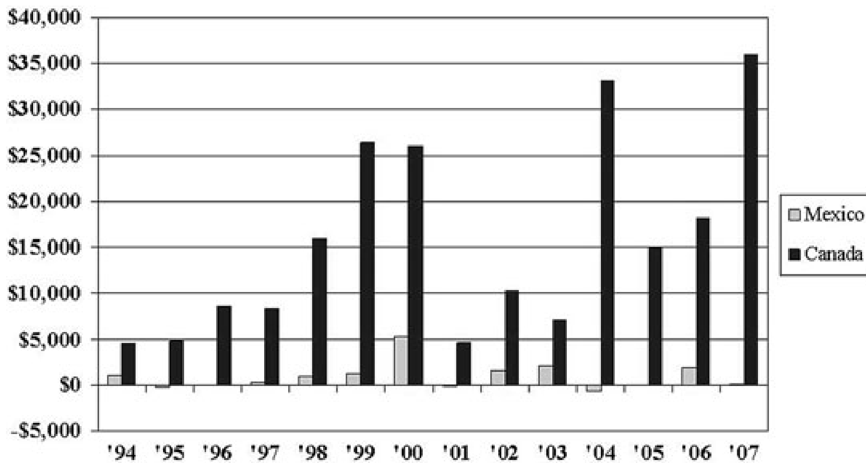

Fig. 5. Foreign direct investment by U.S. – capital inflows (in billions of U.S. dollars)
Source: U.S. Bureau of Economic Analysis (2008)

Legrain 2008). The years following NAFTA's first decade presented a different scenario with American corporations becoming globalized in a way that shifted some jobs to Mexico but also allowed for international growth benefiting both U.S. based companies and their employees. The case of General Electric is emblematic of this NAFTA-fuelled dichotomous growth:

> Since 2006, GE has struck deals to sell Mexican companies $350 million worth of turbines built in Houston, 100 locomotives made in Erie, Pa., and scores of aircraft engines. GE Capital has amassed $10 billion in real estate, corporate loans, mortgages, and other assets south of the border. This is what a free-trade deal is intended to achieve. Mexico specializes in industries where its cheap labor gives it an edge, and it imports U.S. goods requiring advanced technology and major capital investment. Some U.S. workers lose jobs, but new ones are created in services and heavy manufacturing (Engardio et al. 2008).

Most complications in the years following NAFTA's 10 anniversary revolve around the agricultural trade, though their roots have been previously noted (Weinstein 2004). On 1 January, 2008, all remaining cross-border tariffs applied to agricultural goods were lifted. This final mandated step in NAFTA resulted in massive public demonstrations and threats of civil unrest due to the perceived inequalities in agricultural subsidies among the three participating NAFTA nations. In particular, the remaining tariffs on corn, beans, milk, and sugar theoretically helped bolster Mexican farmers who receive fewer subsidies per acre than their American and Canadian counterparts (Global Subsidies Initiative 2008). However, the initial design of NAFTA included assumptions that the free trade nature of the treaty would 'rationally' balance trade inequities over time. For instance, Mexican farmers would eventually react to significantly cheaper corn entering the market from the United States by diversifying their corn crops into other fruits and vegetables, in some cases using foreign investment to do so. This did not happen. However, while some 'campesinos' in Mexico may have been directly affected by the cheaper corn imported from the United States, a closer look at the corn trade is needed to further define the problem.

The first item to consider when examining the corn trade is that the 1 January, 2008 date was 'largely symbolic' as barriers regarding corn trade between the United States and Mexico had been almost entirely lifted before that date (Schwartz 2007). Second, the corn imported from the United States is largely yellow corn used for feed, not the white corn that is primarily used for food items such as tortillas. The abundance of cheap corn used for feed in Mexico is actually a

boon to the country's livestock farmers. The third item of interest is that, across the board, Mexican corn production is significantly higher since the initiation of NAFTA (Porter 2008). Further evidence of the impacts of cheaper corn imports from the United States were demonstrated when they were drastically reduced during 2007 as ethanol production accelerated in the United States. With the help of Mexican wholesalers who seized the opportunity to hoard corn supplies, the price of corn flour increased 400% in a few months resulting in nationwide civil unrest (Taylor 2007).

The underlying problem is not one of trade inequality but of rural poverty and the inequity in subsidy allocation. If the Mexican government's Ministry of Agriculture had taken steps to help transition 80% of its farmers – who are, at best, subsistence farmers – from steadfastly relying on maize as their sole crop, these farmers would have diversified into other crops, as the spirit of NAFTA intended. It is estimated that only 6% of Mexican farms are 'highly efficient and profitable,' and a majority of the $1.4 billion set aside by the Mexican government for its subsidy programme, 'Procampo,' routinely goes to large-scale farmers (*The Economist* 2008). Some argue that due to the massive inequalities in agricultural subsidy distribution within Mexico, as well as the lack of diversification by the multitude of small-scale farmers, many financially unstable campesinos simply stopped farming and migrated to the United States in search of work (Uchitelle 2007).

The situation is reversed for the sugar trade. The removal of remaining agricultural trade barriers in January 2008 prompted the United States sugar industry to seek ways in which to either circumvent NAFTA or alter its language. Negotiations with the Mexican sugar industry that resulted in a separate trade agreement outside of NAFTA were ultimately shelved (Porter 2008). Likewise, the U.S. sugar industry's attempts at swaying government representatives to insert NAFTA circumventing language in the 2008 farm bill were denied (Lipman 2008; Ryan 2008).

Opponents of the U.S. sugar industry's actions are many and include those who would benefit from lower sugar prices, such as food processors, and those who believe that preferential treatment from the federal government would threaten the entire foundation of NAFTA (Ryan 2008). Still, despite these complications, the overall agriculture trade between the United States and Mexico remains healthy. Both imports and exports continued their steady rise from 2004–2007 (Figure 6).

Other complications have arisen recently that are more directly tied to the political landscape of the United States. NAFTA's language provided that by 2000, trucks carrying goods between countries were not to be impeded by national borders. This provision was not heeded in the case of Mexican truck traffic to the United States; and, in 2001, an arbitration panel ruled that the

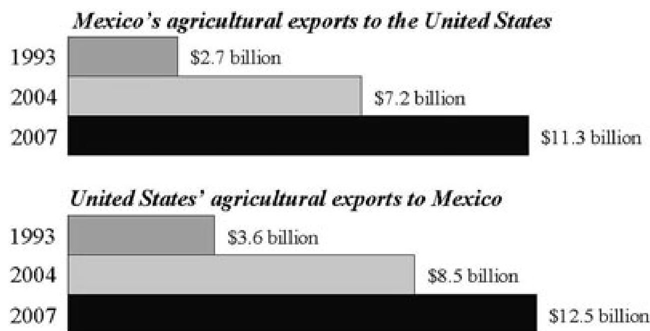

Fig. 6. Agricultural trade between Mexico and the U.S.
Source: U.S. Census Bureau (2008)

United States was in breach of its obligations under the agreement (*The New York Times* 2009). Despite this ruling, Congress indirectly refused to grant Mexican carriers unfettered access to United States roads by approving a measure that set 22 new safety standards for Mexican trucks. This measure created an effective impasse on the issue. Congress was lobbied largely on the issue by the Teamsters Union who held that Mexican trucks were unsafe and heavy polluters. Although Mexico had the right to enact punitive tariffs in response, they chose not to do so in an effort to reach an accord (*The Economist* 2009).

In 2007, the Bush administration was able to initiate a pilot programme granting a sample of Mexican trucking carriers direct access to the United States (Mele 2009). The programme was short-lived, however as Congress – once again lobbied by the Teamsters Union – inserted a provision into the 2009 Omnibus Appropriations Bill calling for elimination of the programme. The Bill was signed into law and the programme was shuttered. This action came even as Mexican trucks and their drivers involved in the pilot programme were documented by the United States Department of Transportation as being considerably safer than their American counterparts (*The Economist* 2009; *The New York Times* 2009). In this case, Mexico chose not to be passive in response to Congress's actions and immediately enacted $2.4 billion in tariffs on nearly 100 items imported from the United States (Williamson & Luhnow 2009).

What this means in terms of daily transportation at the United States/Mexico border is that instead of the NAFTA-provided process of driving a truck directly from Point A in Mexico to Point B in the United States, a Mexican truck must unload its goods at the border. Once unloaded, the goods are then placed on a truck that carries them over the border. Shortly after crossing the border, the goods are unloaded again and then reloaded onto a truck that will carry them to their final destination in the United States. This process is estimated to add $400 million yearly to the cost of goods imported from Mexico, and it also erodes air quality at the border crossings (*The Economist* 2009; *Williams & Luhnow* 2009).

Trade with Canada is not exempt from the occasional quagmire of American politics. The 'Buy American' provision within the 2009 $787 billion economic stimulus bill has led to widespread misunderstanding and actions of protectionism between the countries (Reuters 2009). In its final form, however, the 'Buy American' provision was drafted to exempt 38 countries, including Canada and Mexico (Austen 2009). The problem with the funding is that many projects are being handled at the state and local level – entities that are not bound to the NAFTA agreement. This difference in hierarchy has allowed for regional political maneuvring as well as general misunderstanding of how the funds may be spent. The result has been low-impact protectionist actions at the sub-national level in both Canada and the United States (Austen 2009; Reuters 2009).

4 The new international trade landscape

Though NAFTA is by far the largest trade agreement to which the United States is a party, a number of other countries have entered into, or are in the process of negotiating, free trade deals with the U.S. These include Colombia, Panama, Republic of Korea, Israel, Jordan, Chile, Singapore, Australia, Morocco, Bahrain, Oman, Peru, Malaysia, and Thailand. NAFTA commerce is now just one of many free trade concerns for the United States.

Perhaps the most stunning shift in the trade landscape since 2004 has been the emergence of China. Trade between China and the United States accelerated once China became a member of the World Trade Organization in 2000. Much like the initial explosion of trade among the United States, Canada, and Mexico in the first 10 years of NAFTA, the acceleration of imports from China to the United States between 2000 and 2008 is impressive and dwarfs that of Mexico, tripling from $100 billion to $312 billion (Figure 7). The situation is reversed when considering

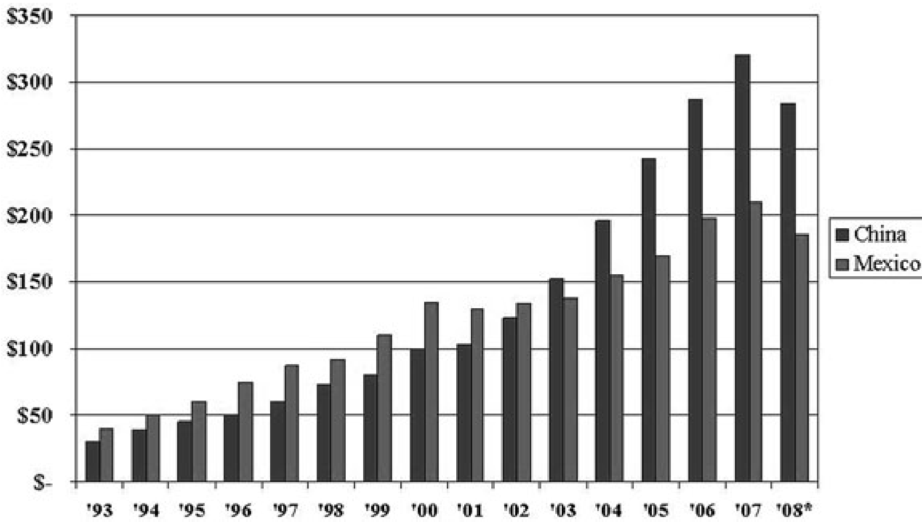

Fig. 7. U.S. imports from China and Mexico (in billions of U.S. dollars)
Source: U.S. Census Bureau (2008); 2008 data to October

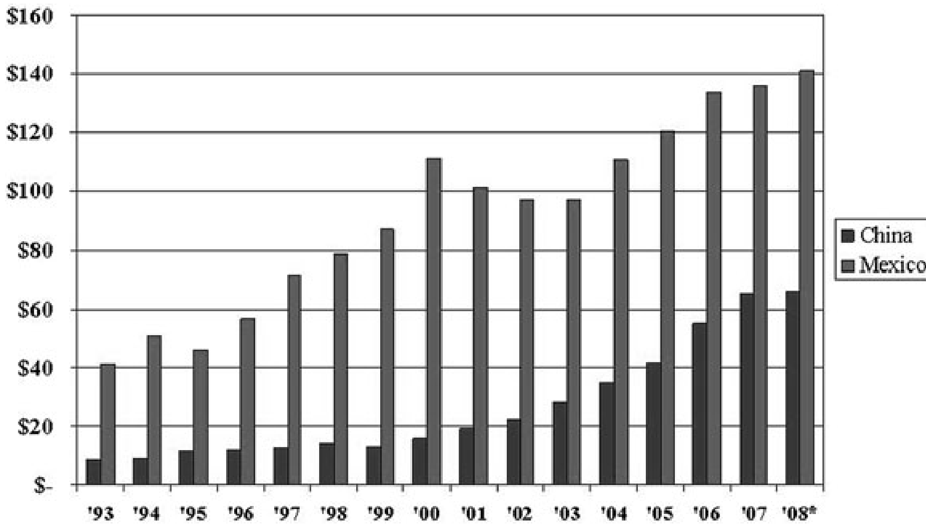

Fig. 8. U.S. exports to China and Mexico (in billions of U.S. dollars)
Source: U.S. Census Bureau (2008). 2008 data to October

exports. Still, China's emerging marketplace was responsible for a 310% jump in exports, from $16.1 billion in 2000 to $66.2 billion in 2008 (Figure 8). Direct investment in China by the United States also increased substantially after 2000, more than tripling from $1.8 billion in 2000 to $5.7 billion in 2007 (Figure 9).

5 Conclusion

At least through the middle of 2008, the North American Free Trade Agreement must be judged a qualified success. Though detractors of the original agreement argued it would depress the

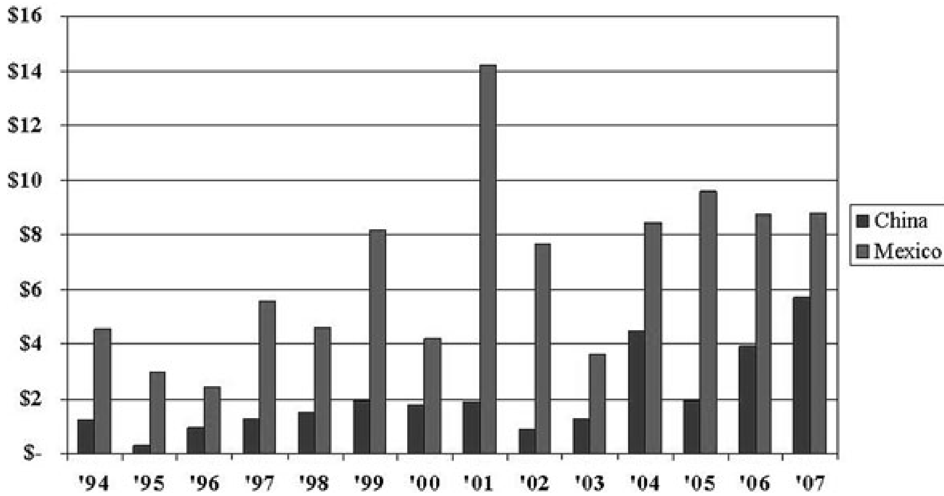

Fig. 9. Foreign direct investment by U.S. in China and Mexico (in billions of U.S. dollars)
Source: U.S. Bureau of Economic Analysis (2008)

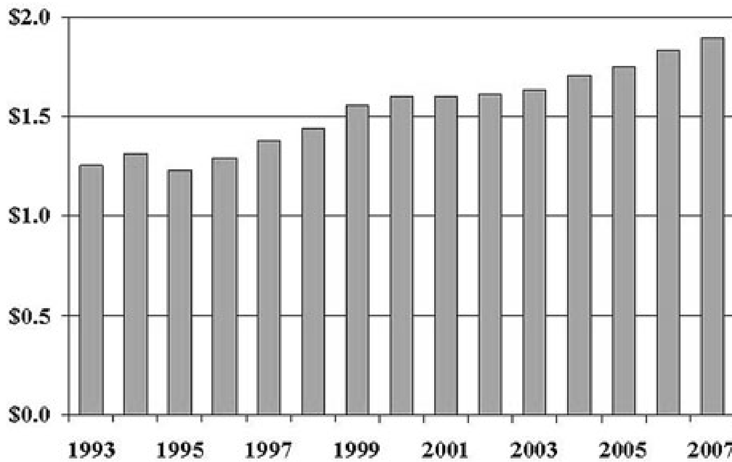

Fig. 10. Steady growth in Mexican GDP (in trillions of U.S. dollars)
Source: National Institute of Statistics and Geography (2008)

economies of both the United States and Mexico, the reality has proved otherwise (see Figure 10). What's more, at least through the first half of 2008, net employment growth in the U.S. has averaged more than two million per year since the NAFTA was enacted.

The next few years will be prove challenging – not only for NAFTA but for the entire global economy. For the first time since the 1930s, all the world's major economies are contracting in tandem and millions of jobs are disappearing in every large country. Protectionist sentiment is on the rise, not only in the United States but across the world. The Doha round of trade negotiations appears dead, and new free trade deals are unlikely to emerge in the foreseeable future.

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