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Boston University The Frederick S. Pardee Center
for the Study of the Longer-Range Future

**The Future of
North American
Trade Policy:**
Lessons from NAFTA

PARDEE CENTER TASK FORCE REPORT

Pardee House Seminar: The Future of NAFTA

*Launch of the Pardee Center Task Force Report
on the Future of North American Trade Policy*



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Wednesday, February 10, 2010

Pardee House
67 Bay State Road
Boston University

12.00 PM to 1.30 pm
Lunch available 11.30 am
RSVP: pardee@bu.edu

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Rethinking Trade Policy for Development: Lessons From Mexico Under NAFTA

Eduardo Zepeda, Timothy A. Wise, and Kevin P. Gallagher

Summary

- The North American Free Trade Agreement (NAFTA) is a good place to begin a comprehensive review of U.S. trade agreements, as called for by President Obama. Any U.S. review of NAFTA should, however, go beyond its impact on the United States to assess its effects on Mexico.
- The evidence points overwhelmingly to the conclusion that Mexico's reforms, backed by NAFTA, have largely been a disappointment for the country. Despite dramatic increases in trade and foreign investment, economic growth has been slow and job creation has been weak. Now, with its economy so closely tied to that of its northern neighbor, Mexico is suffering the most severe economic crisis in the region.
- Reforms to the template for U.S. trade agreements must go deeper than the incorporation of improved labor, environmental, and intellectual property provisions, as seen in more recent U.S. trade agreements. Such measures are laudable, but they would have had little impact on the negative trends we have seen in Mexico under NAFTA.
- U.S. trade agreements with developing countries should avoid NAFTA's restrictions on government policies proven to promote dynamic development. They should leave countries such as Mexico the flexibility to deploy effective policies for industrialization, rural development, poverty alleviation, and environmental protection.
- Mexico's experience under NAFTA shows that U.S. trade agreements must include robust funding for development to create a more level playing field among trading partners.

Rethinking Trade Policy for Development

"I voted against CAFTA, never supported NAFTA, and will not support NAFTA-style trade agreements in the future."

-Candidate Barack Obama

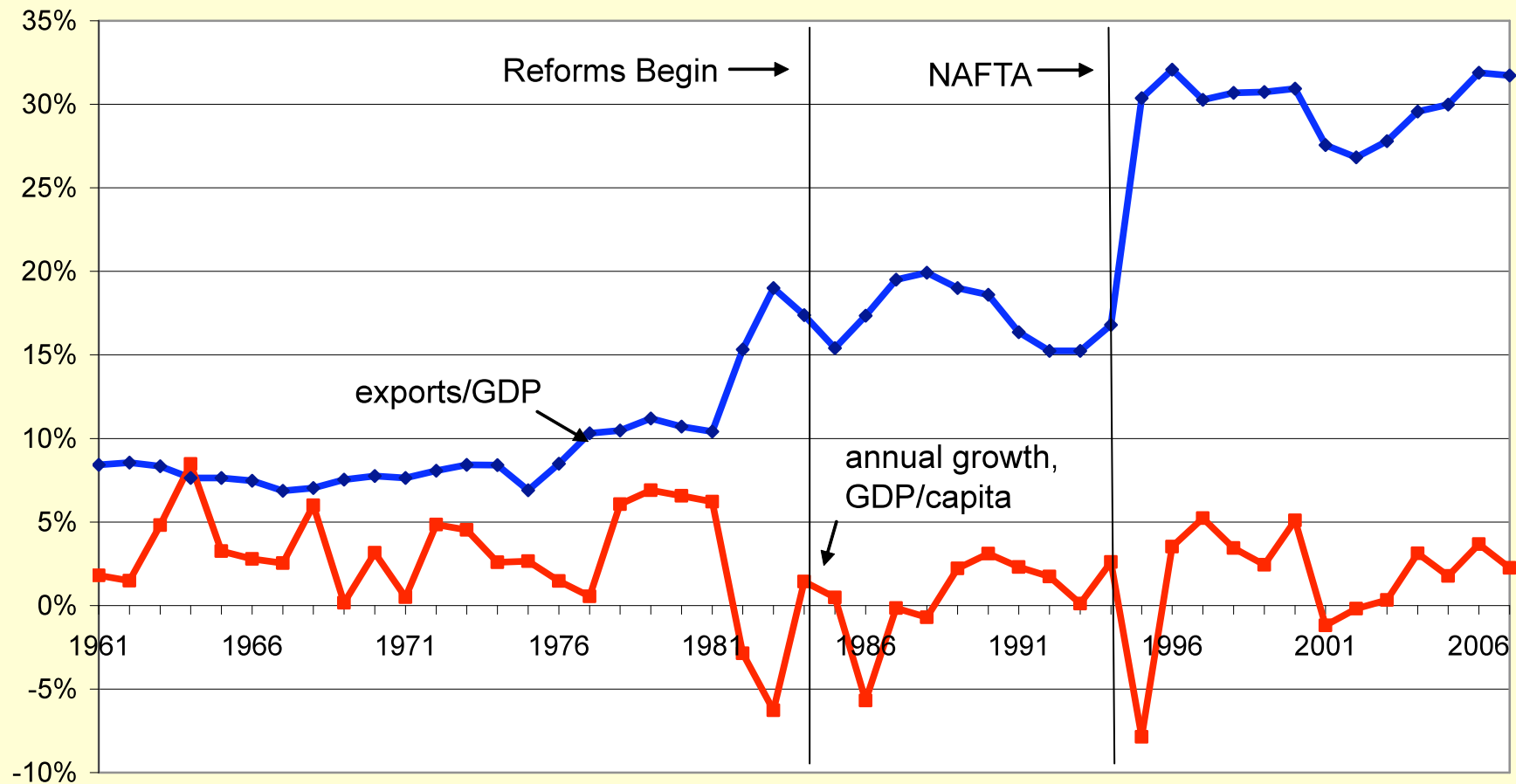
- NAFTA is a good place to begin the review of U.S. trade agreements.
- Such a review should also assess its effects on Mexico.
- NAFTA model has been a disappointment.

NAFTA model: a disappointment

- Despite successes in:
 - Increasing exports.
 - Increasing foreign direct investment.
 - Controlling inflation.
 - Reducing public deficits.
- There are significant and fundamental shortcomings:
 - Slow growth.
 - Low levels of total investment.
 - Persistent macroeconomic vulnerability.
 - Weak job creation and widening US-Mexico wage gap.
 - Little or marginal progress in reducing poverty and inequality.
 - Weak environment protection.

Slow growth in spite of rising exports

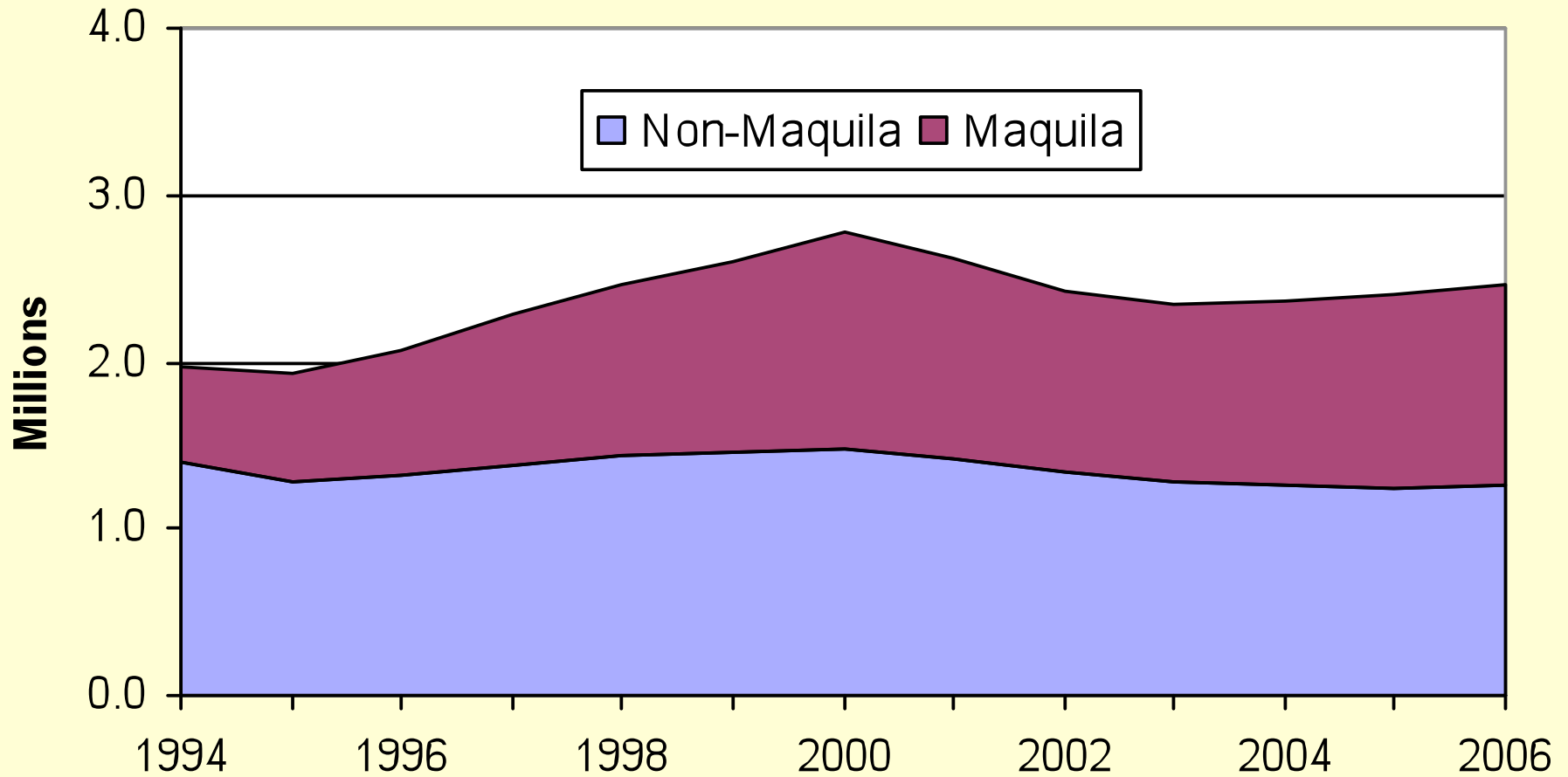
**Fig. 1. Trade and Income Divergence in Mexico
1961-2007**



Source: World Bank, *World Development Indicators*, 2008.

Weak employment creation

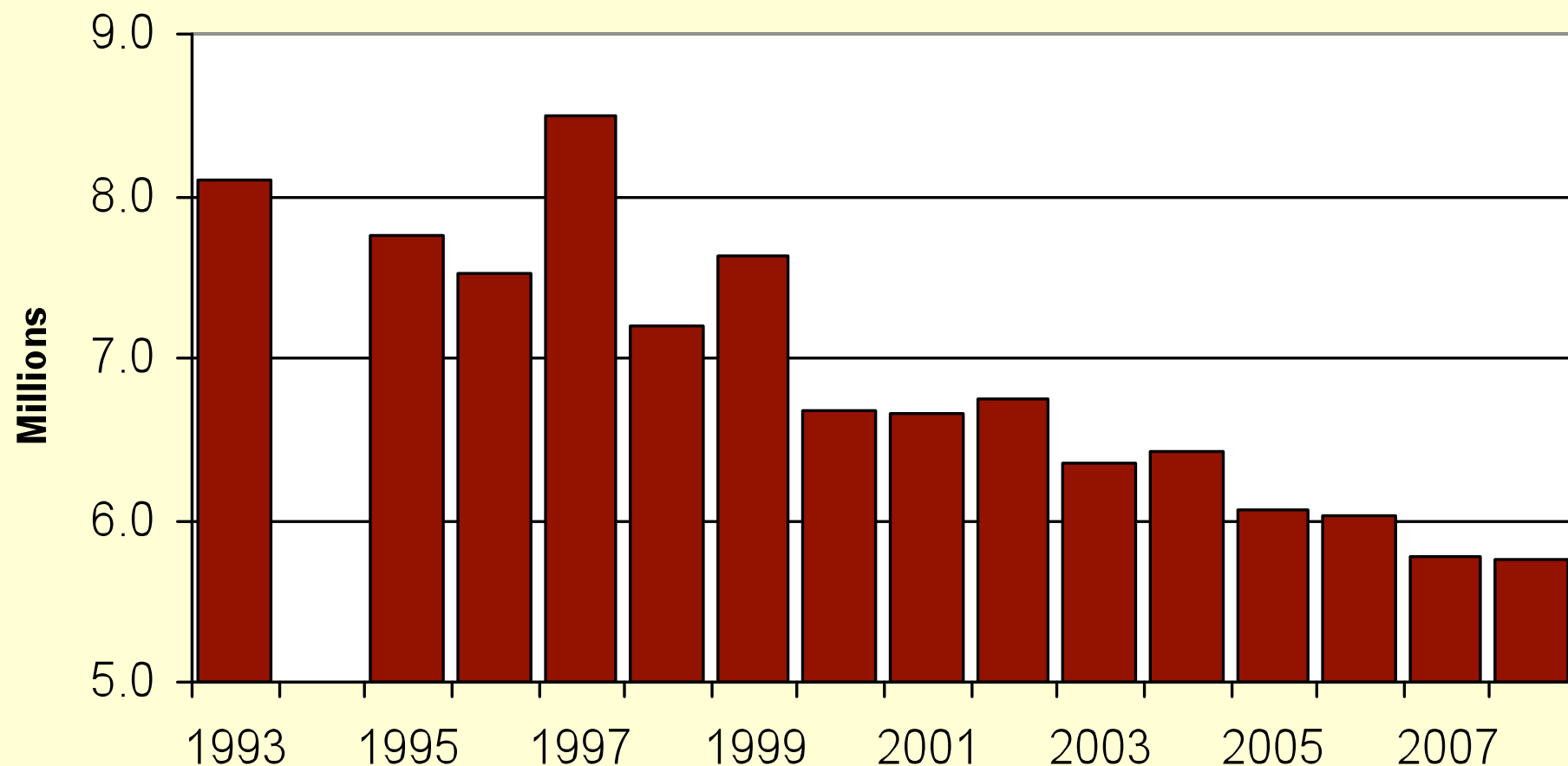
Fig. 4. Manufacturing Employment, 1994-2006



Sources: INEGI, Encuesta Industrial Mensual, Estadística de la Industria Maquiladora de Exportación.

The collapse of employment in agriculture

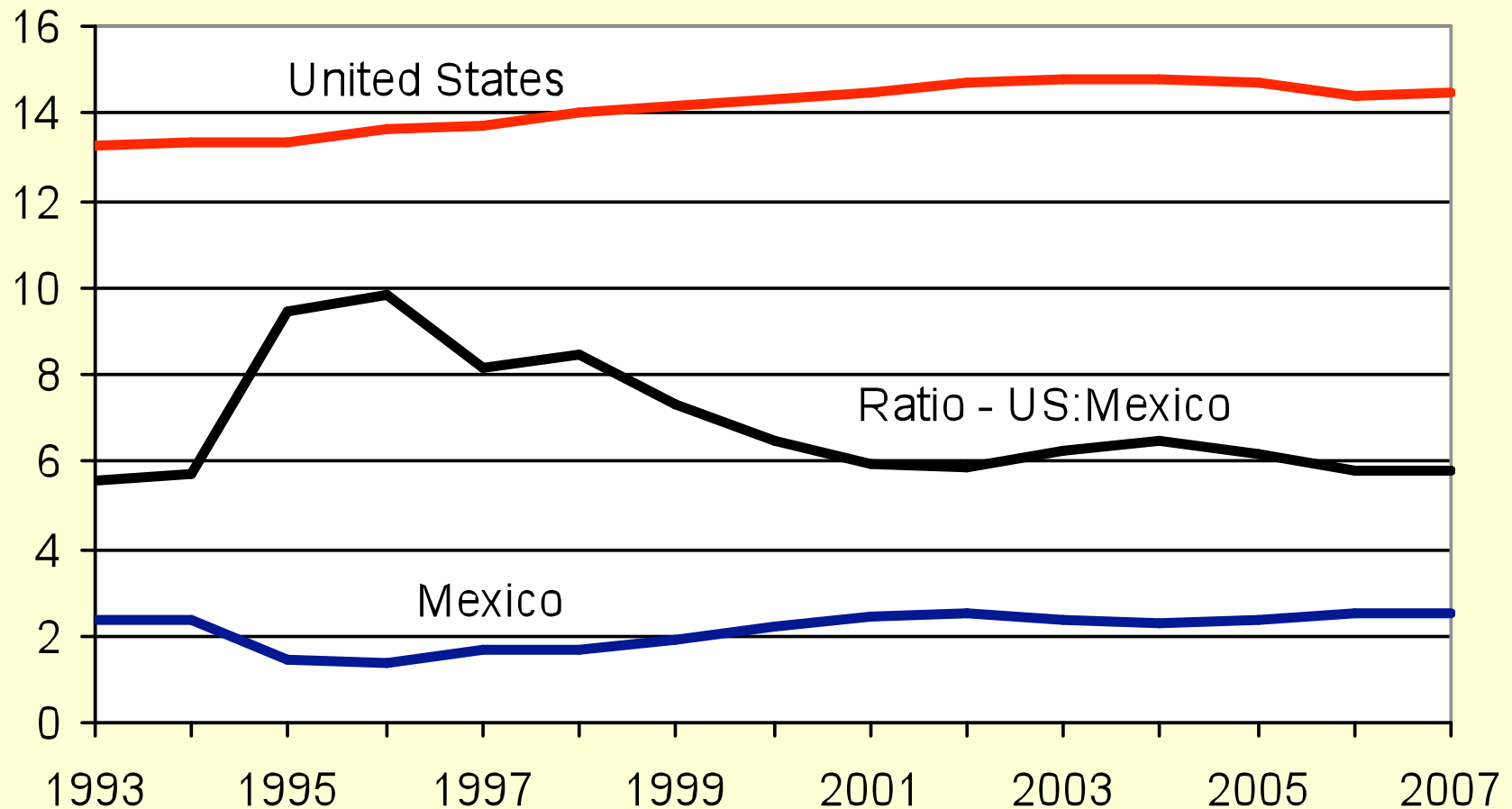
Fig. 5. Agricultural Employment, 1993-2008



Sources: INEGI, Encuesta Nacional de Empleo, sector primario (1995-2008); Audley, et al., NAFTA's Promise and Reality, 2004, for 1993 estimate. (1994 data not available.)

No Convergence in Wages

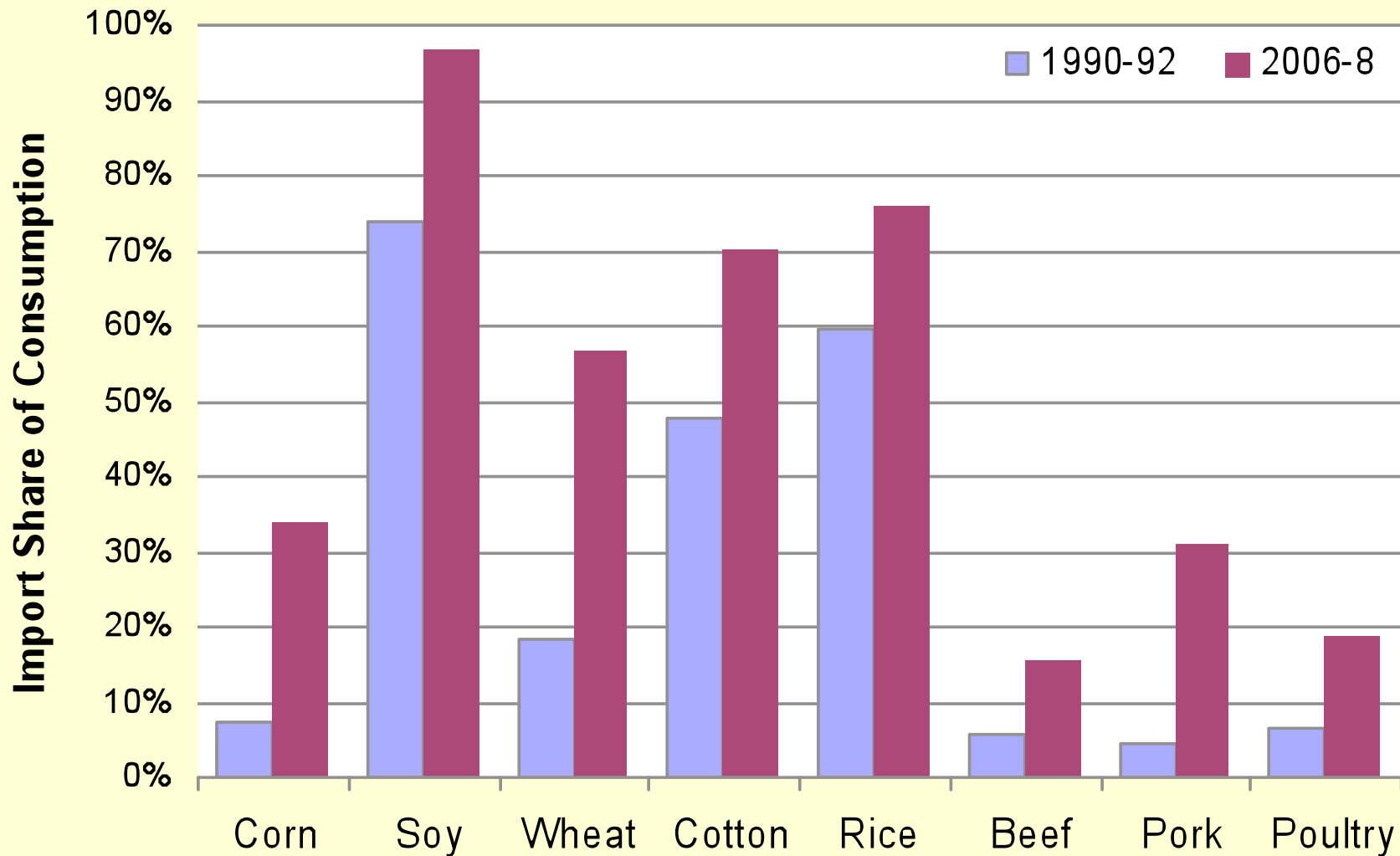
Fig. 7. U.S.-Mexico Wage Gap 1993-2007



Sources: INEGI, Encuesta Industrial Mensual (EIM); IMF, International Financial Statistics. Real wages in manufacturing (2000 US\$/hr), excluding *maquiladora* sector in Mexico.

Excessive Dependence on US

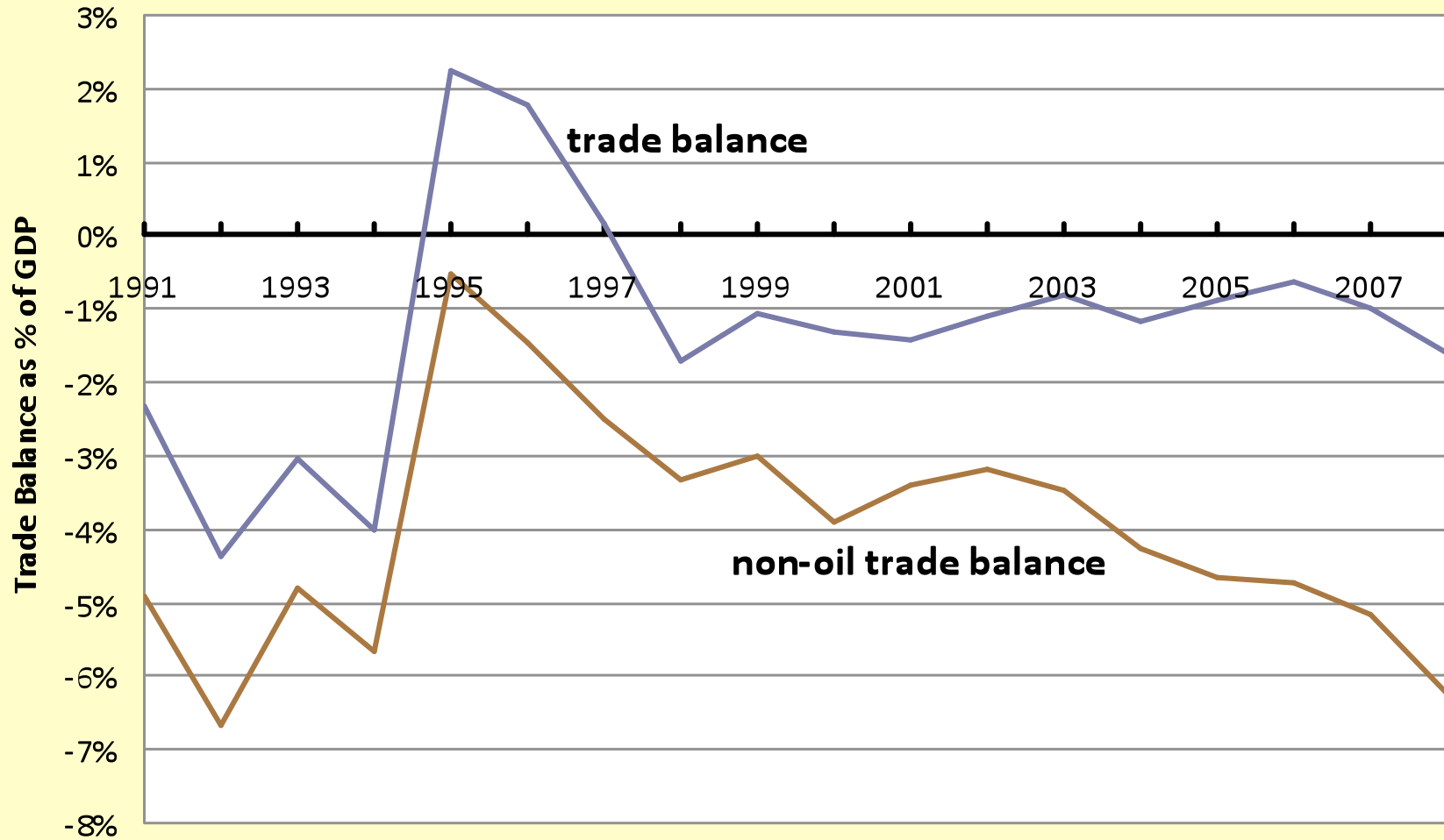
Mexico: Rising Import Dependency



Source: USDA FAS Production, Supply and Distribution Online, 2009.

Persistent macroeconomic vulnerabilities

Fig. 3. Mexico's Trade Balance, 1991-2008



Source: INEGI-BANXICO-SAT (Servicio de Administración Tributaria) y la Secretaría de Economía

US review of trade policy

- The United States should review its trade policies to make them consistent with development needs in partner countries:
 - Better meet the needs of the population
 - Promote job creation
 - Protect the environment
 - Respect the right to development

Reforms must go beyond labor and environment.

NOVEMBER 2009

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Starting Point: Bi-Partisan Trade Compact of 2007

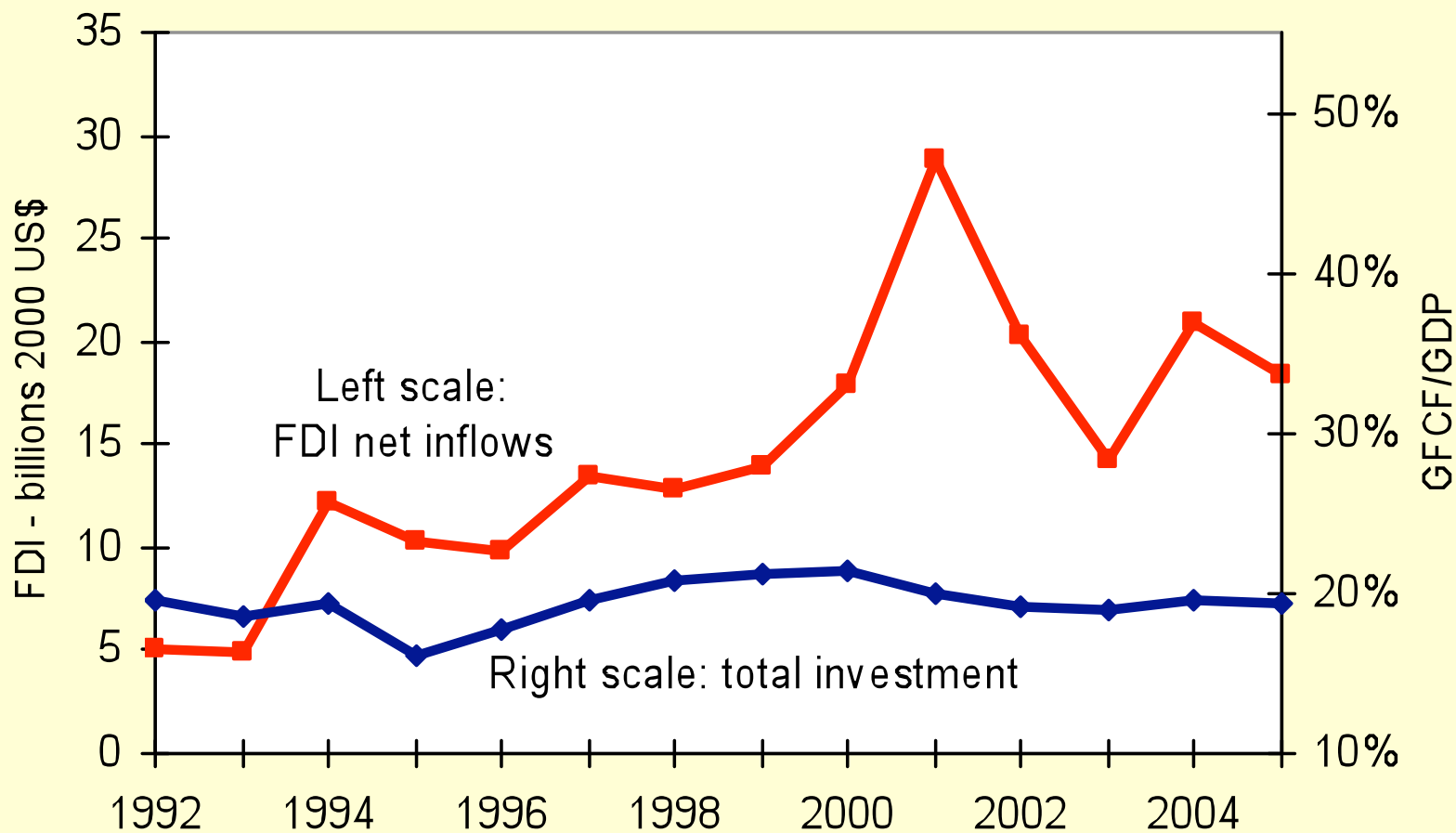
May 10, 2007

- **Labor**
 - Enshrines ILO core principles
 - Dispute mechanism part of main treaty
- **Environment**
 - Enforcement of MEAs
 - Dispute mechanism part of main treaty
- **Intellectual property**
 - Data exclusivity, patent extensions, patent linkage, side letter on public health



Perils of Liberalization: rising FDI, low total investment

Fig. 2. FDI vs. Investment Growth, 1992-2005



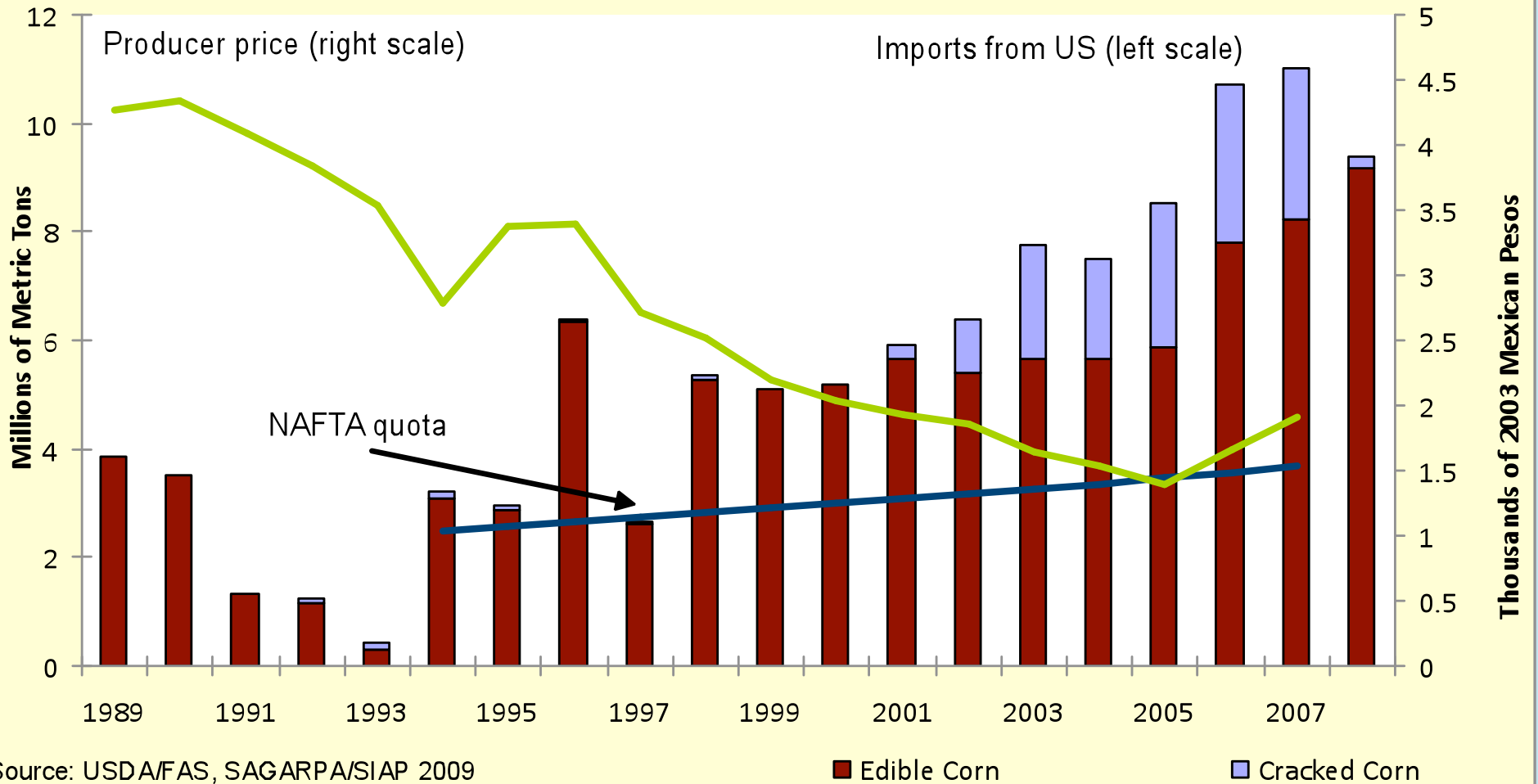
Source: World Bank, *World Development Indicators 2008*. GFCF - gross fixed capital formation.

Beyond May 10: Investment

- Reform “investor-state” dispute process
- Policy space for industrial development
- Codify US position in Glamis Gold case
 - Customary and International Law
 - “fair and equitable treatment”
- Broaden prudential exceptions to prevent and mitigate financial crises
- Close loopholes in **services chapters** that can allow private companies to challenge regulations, e.g. Canadian tar sands

The Perils of Liberalization: Agriculture

Mexican Corn: Imports and Real Producer Prices, 1989-2008

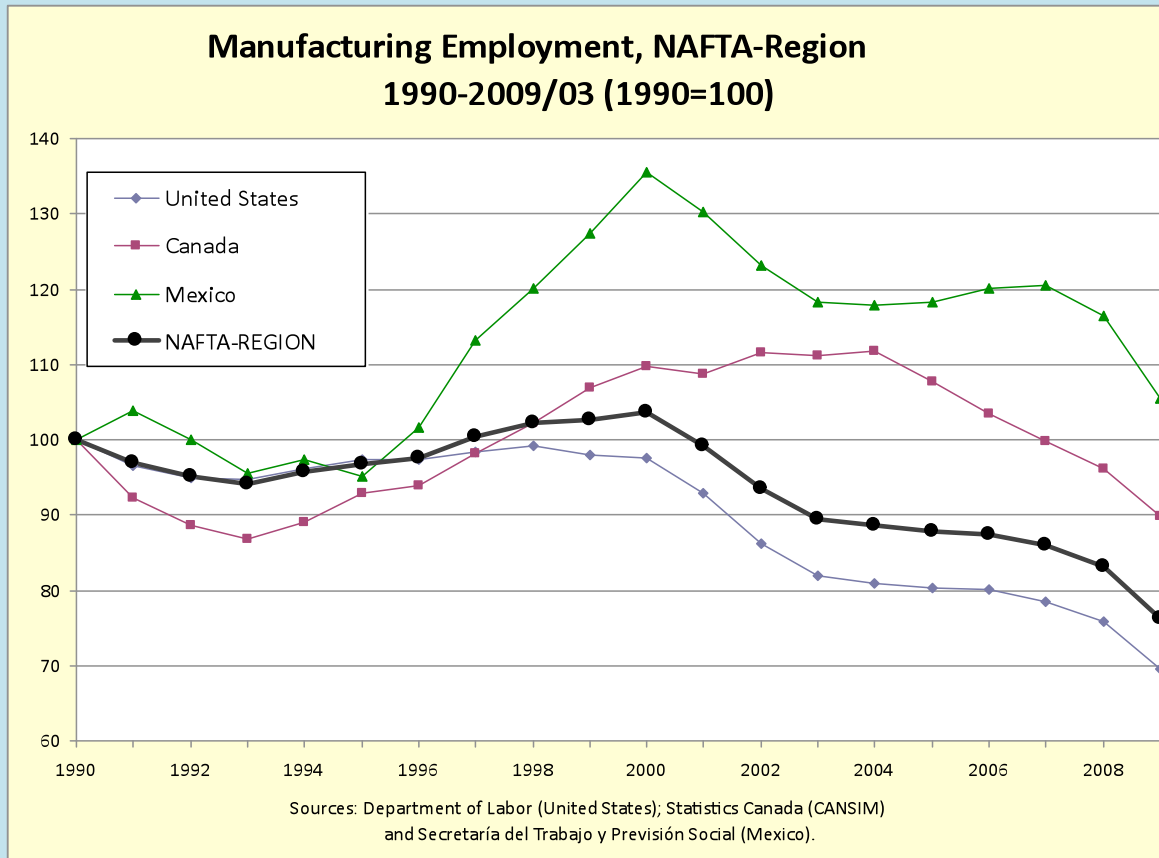


Beyond May 10: Agriculture

- **Borrow from the WTO:**
 - special and differentiated treatment for less developed trading partner
 - "special products" that warrant extended protection,
 - SSM to protect against import surges
- **Strong financing for development** (reform NADBANK)
 - credit
 - infrastructure (irrigation, roads)
 - productivity of smallholder sector
- **Critical to migration issue**
- **NAFTA locks in bad policies**



Beyond May 10: Labor



- Focus on job creation and closing wage gap
- Enshrine ILO core labor standards
- Expand NACLC
- Ensure protections for migrant workers

Beyond May 10: Environment

- Expand NACEC and NADBANK
- Amend other chapters
 - Investment
 - Services
 - intellectual property



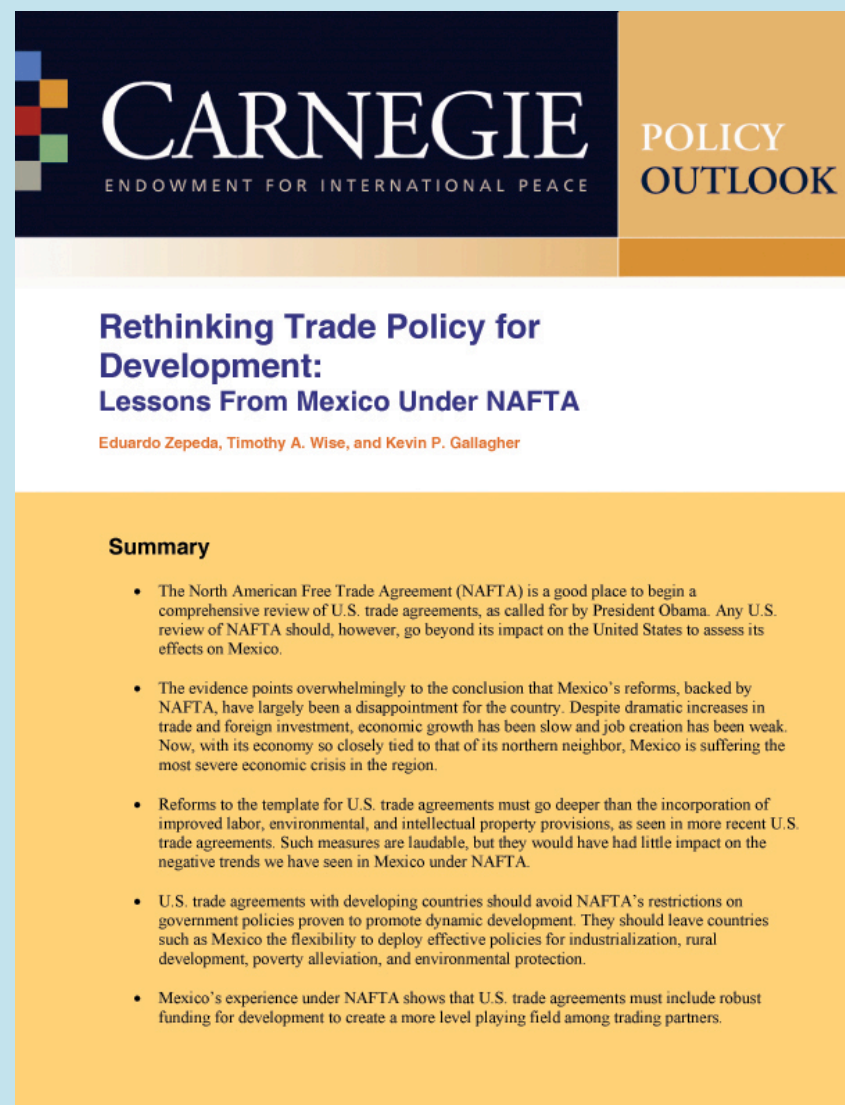
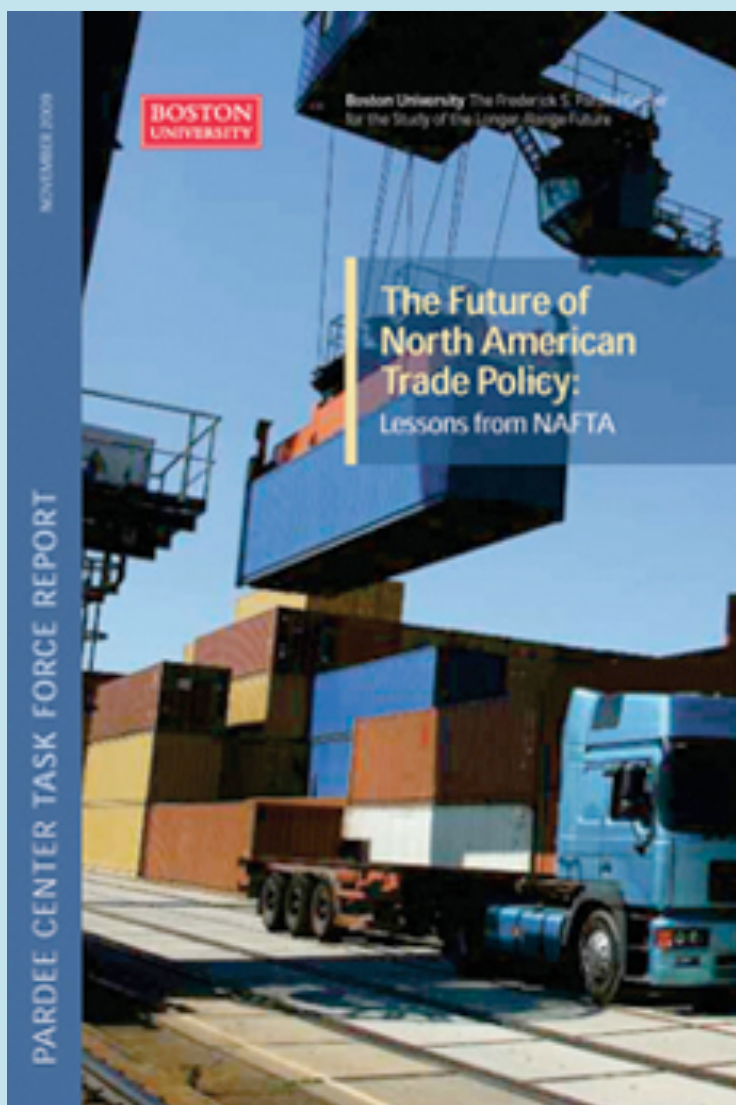
Beyond May 10: Intellectual Property

- Ensure access to medicines
 - Allow for parallel imports and reform pipeline system
- Re-affirm right to exclude plants and animals from patentability
- IP and the environment
 - Require patent applicants to disclose the source and country of origin of genetic and biological resources
 - Require patent applicants to show prior informed consent and benefit sharing for genetic and biological resources
 - Ensure that clean technology transfer is not hindered

Three conclusions

1. NAFTA and the NAFTA template need deep reform
2. Trade agreements need to address the asymmetries among trading partners
3. Trade agreements are no substitute for coherent national development policy

Lessons from NAFTA for Development



<http://www.bu.edu/pardee/>

www.gdae.org

<http://www.carnegieendowment.org/>