

The NAFTA Negotiations: A Mexican Perspective

By

Luz María de la Mora
Director, LMMConsulting and Visiting Professor, International Studies
Division, CIDE, Mexico City

Woodrow Wilson International Center for Scholars (WWICS)
Washington, DC
August 17, 2017

I want to thank the Woodrow Wilson Center for International Scholars and the Mexico Institute for the opportunity to participate in this NAFTA conference. I would like to thank Duncan Wood for his kind invitation to be here with you today.

I believe that a NAFTA discussion is always welcome and timely given what it represents for the 3 countries in terms of trade, investment, economic integration, joint production and innovation. More so when tomorrow we will see the beginning of a negotiation process that I hope will allow us to move towards deeper integration and better understanding of what North America means for our 3 countries.

Having been part of the Mexican government group that took part in the NAFTA negotiations between 1990 and 1992, and having worked on its implementation for many years I have to say that when President Trump announced his decision to RENEGOTIATE NAFTA as a way to address the US DEFICIT and a way to recover lost manufacturing Jobs I could not believe it. I would never have expected that the US could have been the source of distrust and questioning of NAFTA's value. It still puzzles me how to address both questions -the deficit and jobs -through a trade negotiation.

No question it will be a daunting task for Mexico and Canada to sit down with the US, when it seems that President Trump views this opportunity as payback time and has outlined an agenda clearly tainted with a protectionist and nationalist perspective.

NAFTA today

After more than 23 years in place, NAFTA has delivered economic results beyond the most optimistic expectations. NAFTA created a US\$19 trillion regional market with more than 470 million consumers. Every day the region trades more than 2.5 billion dollars. At the time when NAFTA was negotiated Mexico aspired to export US\$10 billion per month. Today Mexico exports more than US\$1.3 billion every day. In the past 23 years, trade between the three partners went from roughly \$290 billion in 1993 to more than \$1.2 trillion in 2016. US-Mexico trade increased almost 6 times, going from US\$88 bn in 1993 to US\$482 bn in 23 years and Mexico's exports to North America increased by more than 7. In terms of FDI, US and Canadian FDI into Mexico has reached close to US\$215 billion, namely, 52 percent of the cumulative FDI stock received by Mexico up to March 2017, which accounts for roughly 20% of our GDP. In addition Mexico has also become a source of FDI in the US; in 2015 FDI stock reached \$16.6 billion in manufacturing, wholesale trade, and depository institutions.

So where is Mexico in this new negotiation? I would like to center my remarks on 5 points.

1. THE FIRST ONE IS THAT IN THIS RENEGOTIATION PROCESS MEXICO IS NOT READY TO BE CONSIDERED ANYTHING ELSE BUT A US AND CANADIAN TRADING PARTNER

At the table and in the NAFTA we are equal partners with equal rights and obligations. Why? Because after 23 years of NAFTA's implementation Mexico is the US' second largest trading partner and **second largest export market**, only after Canada

For every dollar the US sells abroad **16 cents** are bought by Mexican consumers compared to 7.7 cents by Chinese consumers. Today the United States trades more in goods and services with Mexico and Canada than it does with Japan, South Korea, Brazil, Russia, India, and China combined.

In 2017 Mexico is also the US' second source of imports only after China and Mexican products account for **14%** of total US imports from the world.

In addition, production of automobiles, electronics, machinery, and appliances, have greatly benefitted from production sharing across the 3 countries as NAFTA has enabled firms to reduce costs and become more globally competitive. Economists estimate that 40 percent of the content of U.S. imports from Mexico and 25 percent of the content of U.S. imports from Canada are of U.S. origin while U.S. imports from China only integrate **4 percent** U.S. content; talk about regional integration. About half of this trade takes place between related companies, and its resulting specialization has boosted productivity levels in the three economies.

2. MY SECOND POINT IS THAT MEXICO SHOULD LOOK FOR MORE AND NOT LESS NAFTA

In the early 1990s NAFTA triggered a structural reform in Mexico. Since its inception, NAFTA has been a force for change and deep transformation of Mexico's key economic structures and institutions. NAFTA transformed the face of the Mexican economy and opened the door to a young democracy after 70 years of a one-party rule.

NAFTA has also been one of Mexico's most important engines of economic growth given the relevance that international trade and foreign direct investment flows have acquired under the Agreement. Today international trade represents 2/3 of Mexico's GDP.

NAFTA IS EMBEDDED IN MEXICO'S EVERYDAY LIFE. Mexico is not ready to reverse the progress made in the last 23 years. NAFTA created a wide consensus in Mexico that an open economy is the way to go, that we need more not less competition and that we want to be global players.

What Mexico should look for in this negotiation is ways to improve the Agreement. There is plenty of room for improvement. Just a quick glance at the history of European integration shows how much a regional integration project can move on as long as there is leadership and consensus on a common view.

In Mexico there is no political party that has suggested that it would be a good policy option to walkout of NAFTA or that Mexico should respond to Trump's aggressions by closing our border or by building a fortress. In fact a recent survey conducted by Consulta Mitofsky showed that close to 50% of Mexicans have a positive opinion of NAFTA and of the trade relationship with the US while only 16% have a negative one.¹ Moreover, in a GEA survey, from March of this year, 73% of Mexicans surveyed oppose to getting rid of NAFTA.² This does not mean that NAFTA has not yielded winners and losers in Mexico; however, it does mean that overall the country has undergone a silent but deep transformation that has opened new opportunities in a variety of areas that we had not experienced before.

Mexico is in a very strong position to push in this negotiation for the establishment of 21st century trade rules; 20th Century rules are not enough and are not the way to go. Mexico is ideally positioned to boost NAFTA's integration and competitiveness as a result of the reform agenda that President Peña Nieto put forward in 2012 with the *Pacto por México*. The structural reforms touched upon key sectors -education, telecommunications, finance and most importantly energy- and placed Mexico in a better position to contribute to a stronger and more competitive North America.

This set of reforms, in addition to its participation in TPP, allow Mexico to negotiate new issue areas such as energy, services, e-commerce, telecommunications, or financial services.

¹ <http://www.consulta.mx/index.php/estudios-e-investigaciones/mexico-opina/item/951-tlcan-2017>

² <http://www.elfinanciero.com.mx/opinion/nueva-encuesta-empeoran-los-resultados.html>

3. MY THIRD POINT IS THAT NAFTA 2.0 COULD BECOME THE LATEST STRUCTURAL REFORM IN MEXICO

Why do I say this? In Mexico NAFTA has made it even more evident the huge disparities and inequalities that have characterized Mexican development.

For Mexico this is an ideal opportunity to democratize trade. A NAFTA 2.0 will have to lead to a more inclusive economy where more sectors, regions and firms take part in globalization. Today more than half of Mexican exports are done by the six states at the northern border; 60% of total exports are concentrated in only 2 sectors -the automotive and electronics- and according to Secretary Guajardo in Mexico only 45 firms out of a universe of 5 million account for 50% of our exports.³

A NAFTA 2.0 inclusive rules will lead Mexico to create a better business environment where more people benefit from the opportunities the Agreement can offer. NAFTA 2.0 should be the opportunity for Mexico to reduce red-tape for international trade, and business in general.

North American competitiveness should not only rely on the free flow of goods, services and investment. A strong North America and a 21st century NAFTA requires to find ways to opening orderly venues for labor market integration. It is urgent that the 3 countries acknowledge that Mexican labor is a key factor in the region's competitiveness. Mexican workers are filling jobs ranging from low- to high-skilled positions in the US economy and are contributing to maintaining US high growth economic rates in a market with the lowest unemployment rates. Ordering the North American labor markets will not only reduce illegal flows and criminal activities, it will create a more inclusive NAFTA.

4. MY FOURTH POINT IS THAT NAFTA HAS TO STOP BEING A NEGATIVE TERM. NAFTA NEEDS TO BE RETHOUGHT, RESTATED AND REVALUED

³ <http://www.eluniversal.com.mx/articulo/cartera/economia/2017/01/18/trasnacionales-concentran-un-tercio-de-exportaciones>

The late Robert Pastor conceived of the North American idea and of North America as a region that could lead the world economy. Maybe one of the reasons we are renegotiating the NAFTA today in such a contrasting context from the early 1990s is that we never took the time or the effort to socialize NAFTA or to explain the value of North America and how it benefits each one of us.

Today one of our biggest challenges is how to restore the North American idea as a truly regional integration scheme where the 3 countries are better off with it rather than without it.

However, we need to rethink how to reposition NAFTA not as a result of a defensive agenda where each one counts its losses. NAFTA and North America urgently need a common vision from the 3 countries that shows that together we not only add but multiply gains in a highly globalized and competitive economy.

5. MY FIFTH POINT RELATES TO WHAT HAVE WE LEARNED IN MORE THAN TWO DECADES OF NAFTA

NAFTA has offered the region a clear set of rules and disciplines that have created a transparent and predictable business environment. NAFTA's dispute settlement mechanisms for state-to-state disputes in chapter 20, the investor-state mechanism in chapter 11 and trade remedy laws in Chapter 19 have been one of the pillars of NAFTA's effective implementation.

The region has a lot to lose if the US walks out of NAFTA. When the NAFTA became effective, North America accounted for more than 20% of world trade. Today our share has declined to less than 18%. NAFTA needs to regain competitiveness. The Agreement needs to offer the kind of rules required by a 21st Century economy where global production sharing is the name of the game.

Mexico also has a lot to lose from the US leaving the Agreement, the US is Mexico's largest export market with 80% of its total exports which account for US\$300 bn, 30% of Mexico's GDP and 46% of FDI (more than US\$200 bn). Jobs, industrial production, agriculture, services, energy, tourism, entertainment, etc. in Mexico and the region have a lot to lose if we tamper with NAFTA.

A vast majority of business groups in the US realize how important NAFTA is for them and have made specific proposals from where to modernize and improve NAFTA. For many, in the US the lowest POSSIBLE expectation for NAFTA's renegotiation is that whatever results, it will DO NO HARM. If the US decides to walk out of the NAFTA, it will certainly affect regional value chains, production, trade, investment, jobs and economic growth. However, the Agreement will still remain in place for trade between Canada and Mexico.

If we show that we can overcome this very delicate moment the 3 countries will still have to develop a regional strategy to safeguard NAFTA and North American integration.

In 2014, Former USTR Bob Zoellick and General David Paetres issued a report that makes the case for North America. They argued that the US needs to switch its stance vis a vis the NAFTA from "an afterthought" to "a central priority for US policy".⁴

The question is how do we revitalize NAFTA in order to strengthen the competitive position of the region and integrate those that have been left behind into the benefits of globalization. NAFTA countries need to develop a new regional strategy. Such strategy needs to consider a few key elements.

1. The integration of a North American market is the way to boost the region's competitiveness, job creation, business opportunities, and innovation.

⁴ North America. Time for a New Focus. Council of Foreign Relations. October 2014. https://www.cfr.org/sites/default/files/report_pdf/TFR71_North_America.pdf

2. We need to reconcile integration and security. Since 9/11 NAFTA has been torn between its driving force to deepen integration and the break imposed by the US need to build a fortress to guarantee safe and secure borders.
3. Border infrastructure needs to be modernized and more resources need to be allocated to make integration smoother.
4. Land transportation services should be fully liberalized and a seamless door-to-door operation should be facilitated.
5. Mexico has a demographic bonus in the region, we have a young population; our average age is 26 years—old. North America increasingly requires qualified human resources in new disciplines to meet the production needs of the region. A competitive workforce is key to maintaining a dynamic region, so we need to think about the training and development of human resources to meet the new demand for qualified personnel in areas that did not exist 20 years ago such as biogenetics or nanotechnology.
6. North America's integration will be incomplete until we find a way to sort and integrate labor markets; this is something that could take generations given the huge income gap existing between Mexico and its two partners to the North. However, there are some steps that can be taken in this regard. The late Robert Pastor in 2013 suggested to improve the provisions on professional services contained in NAFTA to facilitate and expedite obtaining NAFTA visas for professionals; offer them for longer periods of time and create an expanded Mexican worker program.

I would like to conclude my remarks by referring to how, in the absence of TPP, the new rules that will result from a NAFTA 2.0 may become the new golden standard of trade rules. In the early 1990s the disciplines that we negotiated in the NAFTA became the state-of-the-art trade rules in new areas such agriculture, trade in services, investment, and IP to name a few. NAFTA was the lab where new rules were developed and later set on the negotiation agenda of the Uruguay Round and the WTO. The negotiations that will start tomorrow will be closely followed by the

whole world. The rules and disciplines that we give ourselves in North America will offer a very clear idea of the direction that global trade may take in the future. WE have a responsibility beyond NAFTA.

Mexico needs NAFTA and Mexico needs a strong NAFTA. Mexico will face Presidential elections on June 2, 2018. We have been able to finally pass a series of structural reforms that will yield results in the medium to long term. However, corruption and transparency, the rule of law, crime and a weak judiciary are serious challenges that are also acting against Mexico's competitiveness. If Mexico is to contribute to a stronger region, we need to find sustainable and long-term solutions. In 1994, NAFTA may have triggered Mexico's transition to democracy in 2000. Today, more NAFTA may be the required force to address security and rule of law questions in Mexico.

Boosting North American integration requires political leadership and a shared vision. Returning credibility and legitimacy to the process may prove to be the biggest challenge. We need to be up to it.

* * * * *