The Heritage Foundation Backgrounder

No. 936 | The Heritage Foundation 214 Massachusetts Avenue N.E. Washington, D.C. 20002-4999 (202) 546-4400

April 9, 1993

THE NAFTA DEBATE, PART I: A PRIMER ON LABOR, ENVIRONMENTAL, AND LEGAL ISSUES

INTRODUCTION

George Bush signed the North American Free Trade Agreement (NAFTA) last December 17. If approved by Congress, this trade pact will link the United States, Mexico, and Canada into the world's largest free trade zone. Bill Clinton has expressed support for the agreement, but he faces considerable opposition in the Congress, primarily from his own Democratic Party. NAFTA will face an up-or-down vote in the Congress, probably this fall, but certainly no later than the end of this year.

Passage of the NAFTA will be a significant foreign policy test of the Clinton Administration. Senator Bill Bradley, the Democrat from New Jersey, noted last February that the pact will be "the most important foreign policy decision that Clinton will make in his first six months in office." There is more at stake, however, than simply enhanced trade with Mexico. The NAFTA will be an important factor in ensuring that U.S. businesses remain internationally competitive and that free trade continues to advance around the world.

Despite the agreement's acknowledged benefits to the U.S. economy, many groups oppose free trade in general, and freer trade with Mexico in particular. Among these are several labor unions, environmental organizations, and some industries which favor protectionism. Believing that their interests will be harmed by freer trade with Mexico, these groups try to portray the NAFTA as harmful to the U.S. economy as a whole. They allege that the NAFTA will increase pollution of the environment, reduce worker safety and wages in both the U.S. and Mexico, and cause the loss of U.S. jobs.

In response to these and other criticisms, Clinton has made U.S. approval of the NAFTA conditional on the negotiation of additional "parallel accords" concerning labor and the environment. Far from being low-cost remedies to these concerns, however, these agreements have the potential to undo much of the good created by NAFTA. Opponents of free trade have seized upon these parallel agreements as vehicles by which to reintroduce the trade restrictions NAFTA is intended to eliminate.

NAFTA critics also cite negative political and social consequences of the agreement as reasons for their opposition. Part II will analyze these issues, such as the effects of the NAFTA on drug-trafficking and interdiction efforts between the U.S. and Mexico, political reform and human rights in Mexico, Mexican immigration to the U.S., and the Mexican judicial system.

The strategy of anti-NAFTA groups is to make increased trade with Mexico appear to the American public as threatening. Because Americans are unlikely to be swayed by appeals for protecting such special interests as labor unions, environmental groups, and uncompetitive industries, opponents of NAFTA's free trade provisions have targeted labor and environmental issues in a campaign to broaden the appeal of their cause.

In their attempts to discredit the NAFTA, trade protectionists exaggerate the potential harm of the accord while rejecting many of its benefits. The disintegration and distortions advanced by these groups have clouded the NAFTA debate in Congress. As Congress begins its consideration of the agreement in the coming months, it will require clear and concise information on the results of approving the NAFTA. Only then can it put aside the pleas for protection by special interest groups and ideological opponents of free trade and decide whether NAFTA benefits the country as a whole.

A PRIMER ON NAFTA: QUESTIONS AND ANSWERS

Opposition to the NAFTA focuses on its alleged negative effects on jobs and the environment. Labor unions worry that freer trade with Mexico will cause the loss of jobs among their members, and lead to relaxed worker safety laws. Environmentalists maintain that commercial integration between the two countries will lower U.S. environmental standards, prompt polluting U.S. companies to move to Mexico to avoid strict standards, and lead to massive pollution in Mexico. In addition, opponents charge that the agreement was negotiated in secret, without input from labor, business, and environmental groups.

THE NAFTA, JOBS, AND THE ECONOMY

Among the most commonly expressed questions raised about the NAFTA and its impact on North America are:

Q: With Mexico so much poorer than the U.S., will expanded trade with that country reduce the standard of living of Americans?

The reduction of trade barriers around the world since the end of World War II has brought about enormous increases in trade and economic activity among the participating countries. In constructing this international trading system at the 1948 Bretton Woods Conference, Democrats and Republicans understood that free trade would benefit most working Americans.

Despite the clear connection between free trade and general economic prosperity, there will always be groups who believe their individual interests to be threatened by competition from abroad. The traditional free trade opponents were those industries such as shipping and textiles that profited from government subsidies and tariffs that protected them against foreign competition. In addition to these protected, uncompetitive industries, the opponents of free trade now include labor unions and organizations whose self-interest makes them hostile to free trade and market economics in general and whose message is that, contrary to all evidence, free trade will lead to a reduction in living standards.

These critics are wrong. The NAFTA will benefit the whole U.S. economy. It will lower costs for consumers on such basic products as food, clothing, electronics, appliances, and automobiles. Since these products require a high labor content in their production, lowering labor costs will lower the retail price of these goods. Reducing the costs of consumer goods not only dampens inflation but also improves the standard of living of all Americans and makes businesses more competitive.

The NAFTA also will expand U.S. exports to Mexico, which will greatly benefit the American economy. Mexico already is America's third largest trading partner, after Japan and Canada, and is growing rapidly. U.S. exports to Mexico are heavily weighted toward the high-value, high-technology products that are the foundation of future U.S. growth. Growth in exports has been one of the major factors in U.S. economic growth over the past decade and a source of much of the past and future job creation. The U.S. Department of Commerce estimates 19,100 U.S. jobs are created for every $1.0 billion increase in U.S. merchandise exports. The NAFTA will lower Mexico's trade barriers even further, ensuring that U.S. exports to that country will continue to increase.

Q: Since the Mexican economy is so small, how can it become a sizeable market for U.S. products?

Although the Mexican economy is small compared to that of the U.S., total U.S.-Mexico trade in 1992 was $73 billion (compared to U.S.-German trade with $50 billion and U.S.-China trade with $33 billion), with $40.6 billion in U.S. exports producing a surplus of $6.8 billion.[1] By comparison, the U.S. had a trade deficit with China of $17.1 billion.

U.S. merchandise exports to Mexico support 611,000 American jobs. The Institute for International Economics, a non-partisan research group that studies the effects of trade on the U.S. economy, projects that by 1995, over 1 million U.S. jobs will be dependent on U.S. exports to Mexico. The NAFTA is expected to spur growth in the Mexican economy from between 3.5 percent and 6 percent annually during the next ten years.

Because Mexico will continue to buy most of its imports from the U.S., opportunities for U.S. business will grow as Mexico's economy grows. Currently, 73 percent of Mexico's imports come from the United States. In contrast, Hong Kong buys only 8.1 percent of its imports from the U.S., Japan 22.9 percent, and Germany only 7.5 percent. Each Mexican purchases $300 worth of products every year from the U.S., compared to $30 of European imports. The NAFTA will only add to the advantages enjoyed by U.S. businesses in Mexico. Because the NAFTA will reduce tariffs and restrictions on U.S. and Canadian imports into Mexico, while retaining them on imports from countries outside the free trade zone, U.S. businesses will see their competitive advantage enhanced by the agreement.

Q: How can an economy as underdeveloped as Mexico's help U.S. businesses become more globally competitive, especially against East Asia? Will a free trade pact with Mexico slow down the U.S. economy?

Far from being a threat to U.S. prosperity, the disparity in wage rates with Mexico (Mexican unskilled and semi-skilled wages are seven times lower than in the U.S.) affords an important opportunity for U.S. businesses to become more competitive internationally by emulating some of the successful practices of their East Asian competitors. Given the relatively high U.S. wages, U.S. industries cannot adequately compete with foreign companies which use cheap unskilled labor. Unlike the U.S., such advanced industrial countries in Asia as Japan, South Korea, and Taiwan have adjusted to competition from labor-intensive, unskilled manu-

1 Gary Clyde Hufbauer and Jeffrey J. Schott, *NAFTA: An Assessment* (Washington, D.C.: Institute for International Economics, 1993), p. 14.

facturers in developing countries like Mexico and Malaysia through a scheme known as "co-production."

The manufacturing process is split between highly skilled workers in the advanced countries and low-skilled workers in developing countries, such as the People's Republic of China, the Philippines, and Singapore. This arrangement has allowed the advanced East Asian countries to dominate global markets and rapidly expand their own economies by lowering labor costs in the production of goods. Much of these countries' often-alleged "unfair advantage" comes from their intelligent use of these resources to adapt to the highly competitive environment of the international market.

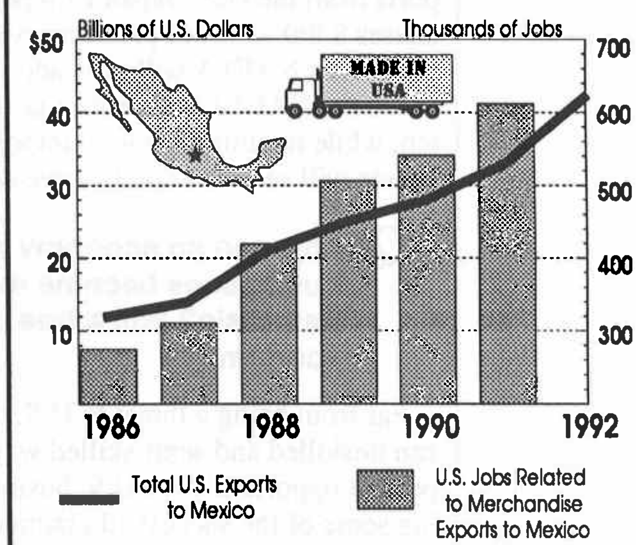
The U.S. has been less successful than Japan and Taiwan at co-production, mainly because there have been few developing countries close to home whose economies complemented that of the U.S. and which were sufficiently open to allow easy operations. The NAFTA will help U.S. companies co-produce more efficiently by combining operations in the U.S. and Mexico. This will occur because of the more stable business environment the NAFTA will create for U.S. business operating in Mexico.

Those who oppose expanding such operations in Mexico, saying they "export jobs," ignore a simple fact: U.S. operations will move somewhere else if Mexico is closed to them, principally to East Asia, with far less positive results for the U.S. economy.

When American companies transfer part of their operations to Mexico, most of their work force stays in the U.S., particularly in administration, sales, warehousing, and components manufacturing. For instance, Ford Motor Company operates an assembly plant in Hermosillo, Mexico, which produces small cars and engines for the U.S. and Mexican markets. Over 75 percent of the components used at that plant are produced in the U.S.[2] Without this plant, Ford would be forced to produce these cars in Asia or Europe, with practically no materials or services used in their production coming from the U.S.

Investment by U.S. companies in Mexico also increases U.S. exports. For example, U.S.-Mexican joint ventures on average buy 51 percent of their materials and services from the U.S. By contrast, when U.S. industries locate their operations in Pacific Rim countries or in Europe, U.S. firms supply only an average of 13 percent of the materials and services to those companies.

U.S. Trade With Mexico: Exports and Export-Related Jobs Are Up



Source: U.S. Trade Representative's Office; U.S. Department of Commerce.

Heritage DataChart

2 Paul A. London and Jonathan Whittle, "Investment, Trade, and U.S. Gains in the NAFTA" (Washington, D.C.: U.S. Council of the Mexico-U.S. Business Committee, 1992), p. 24.

By making Mexico a more attractive investment opportunity than East Asia, the NAFTA will encourage U.S. companies that have already moved assembly plants to faraway countries like Malaysia to relocate to Mexico. Once in Mexico, most of these assembly plants will benefit the U.S. economy by buying their components from U.S. companies instead of from East Asian suppliers, thereby providing more jobs for U.S. parts manufacturers, research and development, transportation and shipping firms, and marketing companies.

Q: Should not the U.S. government be protecting workers from losing their jobs as a result of the NAFTA?

Like other industrialized nations, the U.S. is confronted with ever-increasing global economic competition. Since World War II, the wages of U.S. workers have increased dramatically compared to those of workers in the developing world. Given this wage disparity for unskilled labor, the U.S. is faced with two choices: It can encourage American companies to focus on higher technology production where the U.S. has a comparative advantage, or it can provide government protection in the form of higher tariffs and import quotas for industries that employ large numbers of unskilled workers. If the U.S. government chooses the second alternative, it will:

1) raise costs to U.S. consumers;

2) encourage retaliation by other countries against U.S. exports;

3) increase costs for U.S. companies that use imports in their manufacturing processes and render them less globally competitive; and

4) ensure that the protected industries become ever more uncompetitive.

The temptation to use the government to protect inefficient industries from competition should be resisted because for every uncompetitive sector that is protected, the economy as a whole suffers. Government protection of threatened industries may help small groups of people temporarily, but the costs, ultimately born by the American consumer and the unprotected workers, are quite large.

During the 1980s, for example, the steel industry received government protection from foreign competition in the form of tariffs and import quotas, ostensibly to protect an estimated 18,000 jobs threatened by less expensive imported steel. This protectionism raised the cost of domestic and imported steel. Many U.S. manufacturers that used steel in their production could not buy cheap raw steel from abroad, raising the final cost of their products. These U.S. manufacturers lost sales, costing 52,400 jobs in U.S. steel-related industries during the 1980s.[3] The U.S. International Trade Commission estimates quotas and tariffs on textiles and steel cost consumers an additional $168,700 in 1988 dollars for every U.S. job saved by the protectionist measures.[4] According to the U.S. General Accounting Office, the system of "voluntary" quotas the U.S. imposes on the Japanese automobiles costs American consumers over $190,000 for every U.S. job saved. Clearly, the costs of protectionism to the economy as a whole far outweigh any benefits to individuals.

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3 Arthur T. Denzau, "Can Trade Protectionism Save Jobs," Center for the Study of American Business, April 1987, p. 5.

4 International Trade Commission, "Economic Effects on U.S. Imports Restraints: Phase 1: Manufacturing," Pub. 2222, October 1989, p. 8.

In contrast, the NAFTA, by facilitating co-production, will help U.S. companies to remain competitive in what they do best: producing high-technology goods and services for export and domestic use. With a more stable business environment in Mexico, U.S. companies can have many of their products assembled in Mexico for export abroad. Those who would erect artificial barriers in an attempt to protect uncompetitive industries in the U.S. would succeed only in reducing the prospects for economic growth for everyone.

Q: Will there be a massive loss of jobs as U.S. companies move south in search of cheaper labor?

During the presidential campaign, Ross Perot referred to a "great sucking sound" being made as companies were pulled into Mexico, attracted by cheaper labor.[5] Nevertheless, in spite of dire warnings by Perot and other opponents of the NAFTA, virtually all economists agree the NAFTA will produce a net increase of U.S. jobs over the next decade.[6] By increasing opportunities for exports to Mexico, the NAFTA will generate jobs throughout the entire economy. And, as more U.S. companies engage in co-production, more U.S. jobs will be created as the American companies become more competitive in the international market.

To be sure, some U.S. companies will move a portion of labor-intensive operations like the assembly of components to Mexico to take advantage of the unskilled and semi-skilled labor. The labor needed to manufacture textiles, shoes, some glassware, and other labor-intensive industries is too expensive in the U.S. for them to remain competitive. But for most U.S. industries, especially those upon which the future growth and competitiveness of the U.S. economy rest, and which require highly skilled and trained workers, Mexican labor will hold few attractions.

Q: Will Mexico's lower labor costs depress wages in the United States?

If the NAFTA is approved, Mexico's economic modernization will accelerate. Since approximately 80 percent of all the capital equipment Mexico buys is made in the U.S., U.S. export industries are likely to expand production and hire more U.S. workers. These companies will not be tempted to relocate to Mexico because that country's work force and infrastructure are not capable of supporting high-technology production. As Mexico grows, the demand for skilled manufacturing in the U.S. will grow, placing upward pressure on U.S. wages.

Mexico is one of the fastest growing markets for U.S. goods. The NAFTA will increase that market by forcing Mexico to lower trade barriers that are on average 2.5 times higher than those in the U.S. The reduction in barriers by Mexico over the last several years has resulted in a $6.8 billion trade surplus for the U.S. in 1992. That surplus is projected to continue for the next fifteen to twenty years as Mexico requires capital equipment to modernize, which will create U.S. jobs in export industries.

President Clinton promised repeatedly in his campaign to expand high-wage jobs for U.S. workers. Without a NAFTA, those high-wage jobs will be more difficult to create because U.S. businesses will not be able to export to Mexico as easily as before. Neither will they be

5 *The Wall Street Journal*, January 15, 1993, p. A16.

6 For the most recent study on job growth under the NAFTA, see Hufbauer and Schott, *op. cit.*

able to increase their efficiency through co-production schemes in Mexico. Japan's business sector not only has maintained its generous wage levels but actually increased them through its high-technology exports and its relocation of low-technology, low-paying manufacturing jobs to developing countries like Malaysia and Singapore. This strategy has allowed Japanese companies to stay competitive and reinvest in research and development and high-technology production at home.

Trade between the U.S. and Mexico, up 200 percent since 1987, will increase even more under the NAFTA, providing more U.S. jobs in such businesses as shipping, trucking, warehousing, and retailing that will service the growing commercial base. Increased sales to Mexico, in turn, will cause U.S. wages to rise.

For instance, the advanced countries of the European Economic Community did not experience lower wages when the far less developed economies of Greece, Portugal, and Spain joined the Community.[7] Japan's co-production with Malaysia and Singapore has not slowed the rapidly increasing prosperity of Japanese workers.

Opponents of free trade view international commerce as a fixed economic pie: job growth in manufacturing industries in country A must mean job losses in manufacturing industries in country B. Opponents also believe that less expensive labor in one country will depress wages in a country with more expensive labor, if they are allowed to trade freely.

These views are mistaken. Market economies are far more sophisticated and dynamic than free trade opponents seem to realize. Jobs are created when economic activity increases and are lost when it shrinks; wages respond to the demand for labor. No modern economy is static; only by adapting to changing conditions and making use of opportunities can economies avoid stagnation. Therefore, the NAFTA will not only stimulate business activity across the U.S. economy, but also offer new business opportunities that will create jobs. Economic growth in Mexico will create jobs in export industries in the U.S.

Q: Will the abundant, unskilled labor in Mexico hurt unskilled, poorer workers in the U.S.?

In some cases, industries such as apparel and shoe manufacturing that use high-cost, unskilled or semi-skilled labor will relocate their assembly operations to Mexico. However, most unskilled U.S. workers are located in the services sector; it employs 80 million Americans, compared to 19 million in manufacturing. The poorest American workers are concentrated in service industries like restaurants and retail stores. These industries will not be threatened by lower Mexican wages. In fact, since low-wage Mexican workers will tend to produce cheaper agricultural and consumer goods, the services industries in the U.S. that sell these goods will benefit.

In addition, the NAFTA will help reduce competition for unskilled jobs by illegal immigrants. Economic growth in Mexico will remove much of the economic incentive for Mexicans to migrate to the U.S. in search of employment. An estimated 2.5 million to 4 million illegal immigrants from Mexico now work in the U.S.,[8] almost exclusively in the service sector in areas such as construction, food services, and agriculture.

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7 Michael Porter, *The Competitive Advantage of Nations* (New York: The Free Press, 1990), p. 50.
8 Telephone interview with Bureau of Labor Statistics, March 9, 1993.

Q: Why do labor unions oppose the NAFTA so adamantly?

United Auto Workers Union President Owen Beiber expressed the general sentiment of other labor unions about the NAFTA when he said it was time to "stop tinkering with the damn thing and just say no." The Executive Council of the AFL-CIO issued a statement on February 17 calling for rejection of the NAFTA, saying it "would be a disaster for millions of working people in the United States."[9]

Although most labor unions resoundingly oppose the NAFTA, most union workers stand to benefit from the agreement. For example, while the International Trade Commission estimates a 5 percent decrease in automobile manufacturing in the next ten to fifteen years under the NAFTA, the same study estimates a growth of 6 percent to 15 percent in automotive parts exports during that period.[10]

Certain apparel industries may move south, but the textile industry is projected to increase exports by 13 percent under NAFTA. Unions in the service sector, such as the Teamsters, will benefit from the agreement because of increases in cross-border trucking and warehousing. Even in the areas that will experience job loss, the loss is minor, such as 6 percent to 15 percent loss in flat glass and major household appliance manufacturing, and less than 5 percent over the long term in the U.S. automotive industry.[11]

Most surprising is labor union opposition to an agreement that will spur growth in export industries where most high-wage jobs are located. The International Trade Commission estimates that workers in export manufacturing industries earn wages 17 percent higher than workers in non-export related manufacturing. Estimates are the U.S. will have a $7 billion to $9 billion trade surplus with Mexico by 1995. That means an estimated 200,000 to 350,000 additional jobs in U.S. export industries.[12]

Of larger concern to the unions should be U.S. economic competitiveness. Union jobs in uncompetitive industries cannot long survive without government assistance, which eventually dooms an industry to hopeless inefficiency. Job security, as well as standards of living, rest directly upon finding ways of enhancing the competitiveness of U.S. business. Without a NAFTA, however, U.S. industries will have difficulty co-producing like the Japanese and Europeans. This could lead to much larger losses of jobs in the medium to long term, as foreign businesses gain a larger share of the U.S. market at the expense of inefficient U.S. producers. Industries will also have a harder time exporting to countries like Mexico if those countries maintain high trade barriers.

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9 Statement by the AFL-CIO Executive Council on The North American Free Trade Agreement, Bal Harbour, Florida, February 17, 1993.

10 International Trade Commission, "Potential Impact on the U.S. Economy and Selected Industries of the North American Free Trade Agreement," Report to the Committee on Ways and Means of the United States House of Representative and the Committee on Finance of the United States Senate, U.S.I.T.C Publication 2596, January 1993, p. 2-8.

11 *Ibid.*

12 "Guide to the North American Free Trade Agreement: What It Means for U.S. Business," U.S. Chamber of Commerce, International Division, 1992, p. 25.

Q: Will NAFTA expand *maquiladora* industries, causing greater loss of U.S. jobs?

U.S. companies have been operating assembly co-production or *maquiladora*—plants along the U.S.-Mexico border since 1965. Under the *maquiladora* program, components made in the U.S. are sent to Mexico for assembly, utilizing Mexico's less expensive labor. The finished products are then sent back to the U.S. or exported abroad. Despite frequent charges that the *maquiladora* program has hurt the U.S. economy, it has not caused a net loss of U.S. jobs. To the contrary, by reducing labor costs, this program has allowed manufacturers to remain globally competitive and keep their U.S. plants operating.

During the early 1970s, U.S. corporations faced stiff competition from foreign companies exporting cheaper goods to the U.S. With the U.S. paying relatively high wages for unskilled labor, U.S. companies that used high percentages of unskilled labor in their production processes found it hard to compete against these foreign providers. To stay in business U.S. companies were forced to move the labor-intensive part of their production to countries where labor was less expensive. Most of this co-production in Mexico takes place in the *maquiladora* program.

Co-production with Mexico has helped many U.S. companies face international competition and increase exports. For instance, the Mexico-based Trasgo Group is working with U.S.-based Tyson Foods Company in the growing and packaging of poultry products, 50 percent of which is being sold in Japan. General Motors' Packard Electric Division assembles sophisticated components that are produced in its Ohio and Mississippi plants and assembled in plants throughout Mexico. The Company has remained internationally competitive only by lowering labor costs on the unskilled portion of its manufacturing. AT&T has several facilities in Mexico for manufacturing and phone equipment repair. AT&T plans to shift its Asian supply base to Mexico, providing components manufacturing jobs in the U.S. Moving facilities to Mexico will help AT&T produce for the U.S./Mexico market and beyond.[13]

The NAFTA will eliminate *maquiladora* rules that prevent U.S. companies from selling in Mexico the products they assemble there. Formerly, *maquiladoras* could sell only 20 percent of their products in Mexico.[14] Under the NAFTA, U.S. companies with *maquiladoras* can sell 100 percent of their products in the Mexican market.

Q: Will NAFTA make it easier for Mexico to flood the U.S. with goods?

NAFTA opponents paint a grim picture of truckloads of cheap Mexican products heading north, flooding U.S. markets and putting U.S. producers of similar goods out of work. Freer trade with Mexico in the past four years, however, has demonstrated the reverse to be true. As barriers to trade have been removed, the U.S. has exported more to Mexico than it imported. Under the NAFTA, these barriers will fall even farther and U.S. exports will continue to grow. Because Mexican tariffs to U.S. goods are 2.5 times greater than U.S. tariffs on Mexican goods, U.S. exporters will benefit from trade more than their Mexican counterparts. The majority of U.S. exports to Mexico are in automotive parts, telecommunications equipment, electronic components, processed foods, and basic grains, which currently are subjected to

13 London and Whittle, *op. cit.*, p. 24.

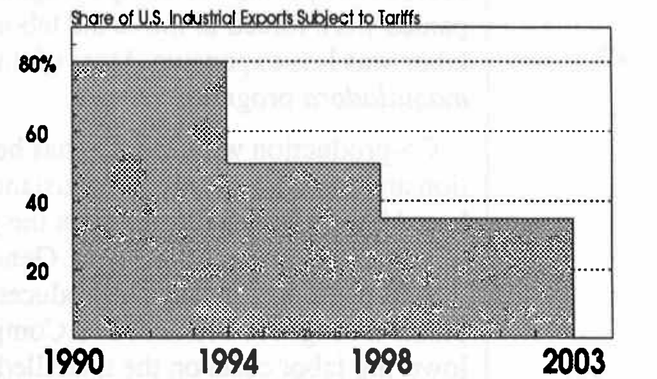
14 U.S. Department of Labor, "Economic Discussion Paper #29," August 1988, p. 17.

Mexican import quotas and tariffs that raise the costs of these goods from 10 percent to 20 percent.

Currently, only 17.9 percent of U.S. goods enter Mexico without tariffs. Once NAFTA becomes law, half of U.S. exports will enter Mexico duty-free. After five years, under the NAFTA, 67 percent of U.S. exports will be duty-free. That percentage rises to 80 after ten years.[15] The apocalyptic scenarios by opponents seem especially exaggerated because the U.S. has had trade surpluses with Mexico for the past three years. Those surpluses are widely projected to continue as Mexico imports U.S. capital equipment needed to modernize its economy. Although Mexico has in the past attempted to restrict such imports, it will be forbidden to do so under the NAFTA.

The NAFTA also removes non-tariff barriers to U.S. exports. For instance, today U.S. auto makers need import licenses to sell U.S.-produced cars in Mexico. U.S. auto makers with auto assembly plants in Mexico have also been under restrictions, known as export quotas, that require U.S. automobile companies with plants in Mexico to export $2 of automotive products for every $1 of U.S. automotive products imported into Mexico.[16] These restrictions are also eliminated under the NAFTA, giving U.S. auto makers greater flexibility to export to Mexico from U.S. plants.

In 10 Years, NAFTA Will Tear Down All Mexican Tariff Walls Against U.S. Industrial Exports



Source: U.S. Trade Representative's Office; U.S. Department of Commerce.

Heritage DataChart

Q: Will freer trade with Mexico benefit only the Southeastern states while hurting the industrial states of the Northeast and Midwest?

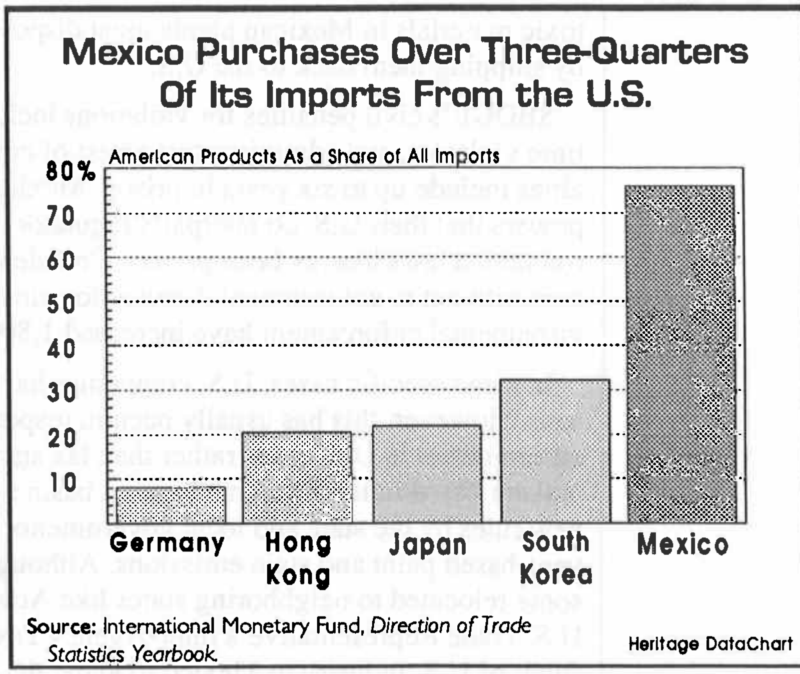
Almost all fifty states have substantially increased their exports to Mexico in the last five years as Mexican barriers to trade have dropped. In Arkansas, exports to Mexico grew 154 percent from 1987 to 1991. In Michigan 31,000 jobs depend on exports to Mexico; from 1987 to 1991 exports to Mexico rose 51 percent.[17] Surprisingly, many Members of Congress who oppose the NAFTA, such as Congressman Donald Pease of Ohio, and Senate Majority Leader George Mitchell of Maine, come from states which have experienced net gains in employment because of growing U.S. exports to Mexico. For example, Ohio Senator Howard Metzenbaum is opposed to the NAFTA; but between 1987 and 1991 his state's exports to Mexico increased 137 percent to $582 million. Over the same period, New York's exports to Mexico increased 73 percent, providing new jobs for thousands of workers. Mexico repre-

15 International Trade Commission, "Potential Impact," p. 104.

16 Hufbauer and Schott, *op. cit.*, p. 39.

17 *U.S. Exports to Mexico: A State-by-State Overview 1987-1991* (U.S. Department of Commerce, International Trade Administration, July 1992), p. 32.

sents the third largest export market for Illinois, Michigan, New York, and Pennsylvania, and the second largest market for Maine, New Hampshire, and Ohio. Mexico is the largest export market for California and Texas. Pennsylvania Senator Harris Wofford's election platform included an anti-NAFTA stance; yet Pennsylvania's exports to Mexico have climbed 283 percent since 1987 to $694 million in 1991, creating approximately 9,000 additional jobs for Pennsylvania workers.[18]



PROTECTING THE ENVIRONMENT UNDER THE NAFTA

Q: Will American companies move to Mexico to avoid strict environmental laws in the U.S.?

Almost all environmental and labor groups argue that lax environmental enforcement and lower standards in Mexico give an unfair advantage to companies based there. Lower standards, they say, will encourage U.S. companies to reduce environmental compliance costs by moving their factories to Mexico.

Such criticism, however, overlooks a number of facts.

1) Mexico's environmental laws and regulations are roughly equal to those in the U.S. In fact, the Mexican environmental agency, *Secretaria del Desarrollo Urbano y Ecologia* (SEDUE), is adopting Environmental Protection Agency (EPA) standards wholesale;

2) Most multinational companies already follow U.S. environmental standards when operating in Mexico; and

3) For most industries, the difference in environmental compliance costs between Mexico and the U.S. is not substantial.

For example, Mexican laws regulating the transportation of cross-border toxic waste are equivalent to those in the U.S. Mexican regulations require any U.S. company locating within 62 miles (100 kilometers) of the U.S.-Mexico border to comply with all EPA standards on the disposal of toxic wastes. Under new Mexican environmental laws, any U.S. company using

18 For a more comprehensive state-by-state analysis on exports to Mexico, see *ibid.*

toxic materials in Mexican plants must dispose of these materials and their waste by-products by shipping them back to the U.S.

SEDUE's civil penalties for violations include plant closure, up to $80,000 in fines for first-time violators, and administrative arrest of company officials for up to 36 hours; criminal penalties include up to six years in prison. Mexican environmental regulators also have policing powers that their U.S. counterparts regulators do not. Although enforcement of Mexico's environmental laws has not been perfect, President Carlos Salinas de Gortari has shown a strong commitment to environmental protection since taking office. Government expenditures for environmental enforcement have increased 1,800 percent to $1.8 billion in 1991.

In some specific cases, U.S. companies have relocated to Mexico for environmental reasons. However, this has usually been in response to draconian environmental regulations on air emissions in U.S. cities rather than lax standards in Mexico. For instance, several furniture makers based in the Los Angeles area basin moved their facilities to Tijuana, Mexico, when new rules by the state and local governments placed extremely low limits on the use of solvent-based paint and stain emissions. Although many of those companies moved to Tijuana, some relocated to neighboring states like Arizona and Nevada. According to a study by the U.S. Trade Representative's Inter-Agency Task Force, this relocation was not part of a general flight of U.S. industry to Mexico to avoid general environmental standards.[19]

Most U.S. companies have little incentive to move south to avoid strict U.S. environmental standards because Mexico operates by those same standards. According to this Task Force study, "U.S. firms, particularly the larger multinational firms most likely to undertake large process industry investments [in Mexico], often hold subsidiaries to a worldwide standard, usually at least as high as standards with which they must comply in the U.S."[20] An example is Ford Motor Company, which has a policy of applying U.S. environmental practices in its automotive manufacturing plants in Mexico.

Q: Will economic growth in Mexico lead to more environmental degradation in that country, and North America generally?

Some environmental groups oppose the NAFTA because it will promote economic growth in Mexico. These critics are against economic development because of the increase of pollution that development brings. Thus, they believe the best way of improving the environment is to prevent economic growth from taking place.

Environmental critics of the NAFTA misunderstand the relationship between economic development and a clean environment. Without economic growth, Mexico can never adequately address its environmental problems. As countries become wealthier, the priorities of their people change from subsistence living to such quality of life concerns as environmental protection. That is why every industrialized country spends a far greater percentage of its GDP on

19 "Review of U.S.-Mexico Environmental Issues," Prepared by an Inter-Agency Task Force Coordinated by the Office of the United States Trade Representative, Draft, October 1991, p. 194. (The Trade Policy Staff of the Inter-Agency Task Force, during six public hearings held from August 20 to September 11, 1991, gathered data on the alleged movement of U.S. companies to Mexico for environmental reasons. They found these allegations to be untrue, except in the specific case of furniture refinishing companies relocating from Los Angeles to Mexico and other U.S. states.)

20 *Ibid.*, p. 195.

environmental protection than any underdeveloped country. When the choice is between jobs and stricter environmental standards, poorer countries choose jobs.

When Mexican companies were heavily debt-ridden and on the verge of bankruptcy during the 1980s, it was difficult for the government to force compliance with environmental regulations. The reason: the government feared throwing people out of work by closing polluting factories. Only with economic growth does sustained environmental improvement become possible.

Of 42 countries analyzed in a recent Princeton University study, pollution levels began to decrease in those with per capita GDP rising above $4,000 to $5,000. Mexico, with a current per capita GDP of $3,700, already is beginning to devote larger resources toward environmental purposes. Example: a 200 percent increase in environmental inspectors since 1989. This process will continue as the economy grows. Unfortunately, Mexico's growth would be stalled without the NAFTA, postponing future environmental protection.

Q: Is extensive government regulation necessary to protect the North American environment?

Economic growth is not inherently harmful to the environment; pervasive government intervention in industry and commerce is. Surprisingly, some U.S. labor and environmental groups are promoting traditional protectionism as the best way to avert further environmental degradation in Mexico. For instance, labor groups are advocating placing tariffs on goods produced in Mexican factories that have lower environmental standards than those in the U.S.

Mexico, like many socialist countries in Eastern Europe, has learned that planned economies and authoritarian governments have created far more seriously degraded environments than their free market, democratic counterparts. For most of the period since the 1930s, Mexico has been ruled by an authoritarian, quasi-socialist government. The economy was subjected to central planning and control, and the Mexican government protected domestic industries through high import tariffs, quotas, and licensing. The government also created an enormously burdensome system of rules and regulations to shield workers from exploitation, control production, and direct resources to government priorities.

The result of this legacy was not only economic ruin but environmental degradation. Protectionism and overregulation made domestic industries inefficient and wasteful, impoverished the country as a whole, and discouraged private investment. Without new capital, antiquated polluting factories could not be replaced with more modern, cleaner ones. Nationalized or heavily regulated industries also had little reason to obey existing environmental laws, since the government was loath to punish its own companies or companies it so closely directed.

Inefficient production eventually led to excessive pollution in Mexico. For example, 76 percent of the air pollution in Mexico City comes from automobiles using low-grade leaded gasoline refined by the inefficiently run, government-owned oil monopoly PEMEX. Most of the remaining 24 percent of the air pollution in Mexico City comes from factories, two-thirds of which were controlled or owned by the government before privatization began five years ago.

Now environmentalists and labor unions wish to create a complex set of regulations as part of the NAFTA. They argue that only the government has the detached interest and expertise needed to set priorities, direct private funds, and mandate industry practices and procedures in order to protect the environment. There is no evidence, however, that new central planning of North America's production and commerce will protect the environment. In fact, the U.S. government has a lackluster record of protecting the environment through complex regulations.

For example, the environmental Superfund, designed to assist in toxic waste cleanups has produced steady employment for lawyers, accountants, and consultants, while failing to adequately address environmental cleanup. Additional government intervention is most likely to lead to further wasteful spending without a commensurate improvement in the environment.

Q: Will the *maquiladora* industry simply expand under the NAFTA, causing more pollution along the U.S.-Mexico border?

Some environmentalists charge that the *maquiladora* industry has ruined the environment along the 2,000-mile U.S.-Mexican border. They argue that NAFTA would spread this problem throughout Mexico by encouraging *maquiladora*-type operations throughout the entire country.

There are two main environmental problems plaguing the border region: a lack of sewage systems and other infrastructure to service the population, and facilities and resources to dispose of and clean up contaminants dumped into the environment by industry. Both of these problems result from the tax codes under which the *maquiladora* program operates, not the development resulting from the maquiladora program.

For example, under existing laws, local authorities have little power to tax industry involved in *maquiladora* operations. American companies can locate in a Mexican state along the border, but are required to pay taxes only in the U.S. state where the company is incorporated. This has effectively impoverished the Mexican side of the border region, denying it essential tax revenues from its major industry with which to build infrastructure, monitor compliance of environmental regulations, and dispose of industrial waste.

Under the NAFTA, however, the preferences that *maquiladora* industries in the border region now enjoy relative to other areas in Mexico will be eliminated. The Mexican federal system and the states in the U.S. will be able to set their own taxes. This will provide municipalities and regional governments with the funds to build the sewage systems, waste dumps, and water purification systems they need.

RULE OF LAW, SOVEREIGNTY, AND PARTICIPATION UNDER THE AGREEMENT

Q: Will cross-border commercial disputes under the NAFTA be decided in a way that infringes on U.S. sovereignty?

Liberal and conservative critics of the NAFTA charge that the agreement infringes on national sovereignty and limits local power to control laws, enforce environmental standards, and uphold health and safety regulations. For instance, Ralph Nader's Public Citizen group alleges that the NAFTA will prevent local governments from setting limits on pesticide use or regulations on how milk is processed.

However, NAFTA dispute mechanisms will give U.S. citizens and businesses more direct participation in resolving commercial, environmental, and investment disputes between the three countries, by allowing them their day in court.

The NAFTA rules for settling commercial disputes arising under the agreement are similar to those of the U.S.-Canada Free Trade Agreement (FTA) of 1988. Under the FTA, regular cross-border commercial disputes are settled by either country's domestic courts. The free trade agreement with Canada does not limit domestic control over these types of commercial disputes. The same is true of the NAFTA. Under the NAFTA, traditional commercial disputes will be handled by the courts that would naturally have jurisdiction in such cases—depending on the type of commercial activity and the jurisdiction the parties had agreed to in advance.

The U.S.-Canada agreement mandates the creation of expert panels to determine whether a government's laws, regulations, and policies violate its rules. These panels are made up of experts appointed by each country. The NAFTA also requires the creation of similar panels to decide NAFTA-related disputes. However, as with the FTA, the NAFTA panels do not have the power to force a country to abide by its decisions. For instance, in the case of countervailing duty and anti-dumping disputes, a party can challenge a panel decision by requesting a special review panel. If the party's government objects to the finding of the review panel, it can suspend the binational panel system entirely. Despite this lack of enforcement power, these panels have worked smoothly and effectively to resolve trade disputes.

State, local, and national governments are free to set higher environmental, health, and safety standards of their own under the NAFTA. Such standards can only be challenged through NAFTA panels if they are based on political rather than scientific considerations or discriminate against imports. Thus, the power to enforce U.S. laws, regulations, and standards through domestic courts ultimately remains in the hands of domestic national, state, and local governments.

The dispute panels, in turn, will help U.S. companies seek redress for violations of the law in Mexico and Canada that traditionally have been difficult to obtain. For instance, conflicts arising over lax enforcement in protecting such intellectual property as patents will be decided by panels created under the NAFTA. This will help U.S. companies recoup the approximately $900 million they lose annually because of non-existent or lax enforcement of intellectual property rights in Canada and Mexico.[21]

Q: Will citizens be prohibited from participating in the judicial process in disputes that arise under the NAFTA?

Ideological opponents of the NAFTA, such as the Alliance for Responsible Trade and the Citizen Trade Campaign, have called the dispute resolution mechanisms in the NAFTA undemocratic and secretive because these allegedly do not provide the "broadest possible participation by workers, consumers, environmentalists, and human rights organizations."[22]

However, NAFTA commissions and panels review only disputes arising out of interpretations of the agreement itself. NAFTA commissions will not review regular commercial disputes between companies. The vast majority of commercial disputes will be decided by the domestic courts of the country which have jurisdiction over the dispute. The NAFTA will not change the long-standing tradition of commercial law. Both legal systems (America's common law and Mexico's civil or code-based law) allow only those parties whose involvement gave rise to the dispute to be directly involved in the judicial process. If numerous parties, each with separate grievances, were allowed to participate in the same judicial proceeding, the government could not narrow the issues being adjudicated or ever come to a final decision based in law. Since the NAFTA dispute panels will have the right to assess penalties against a

21 Exact figures on past losses are unavailable. However, the International Trade Commission estimates that in 1986 U.S. companies lost $533 million to Mexico and $367 million in Canada due to non-enforcement of intellectual property rights.

22 Letter to Members of Congress from the Alliance For Responsible Trade/Citizen Trade Campaign, December 15, 1992.

company, the issues in a dispute need to be narrowly defined by law. So, too, should the parties that can participate in the dispute.

Balancing the grievances of numerous groups is a challenge more appropriately addressed by legislatures, not courts. To allow an open-ended participation "for cases involving challenges to social legislation"[23] would turn the judicial process into a purely political one. Although parties not directly involved in a judicial proceeding may be harmed by a court's decision, using the judicial process to address their grievances would weaken the rule of law in commercial disputes, and make a mockery of stable commercial transactions. This, in turn, would reduce commercial activity between the two countries.

Q: Was the NAFTA negotiated hastily, in secret, with little or no participation by citizens groups, unions, or Congress?

The NAFTA was negotiated by the Bush Administration under "fast track" authority given it by Congress. In giving the President fast track authority, Congress agrees in advance to either approve or reject the negotiated agreement as a whole, without amendments. Fast track negotiating procedures, authorized in the 1974 Trade Act, have given several Presidents the power to conclude trade agreements that would not later be unravelled by the Congress.

Some special interest groups, however, oppose fast track authority because it limits their ability to influence Congress. Thus, apparel and shoe manufacturers, and many unions which seek protection from foreign competition, argue that the NAFTA was negotiated in secret with little participation by groups affected by the accord.

In fact, fast track procedures required the Administration to work closely with Congress, labor, business, and environmental groups during the course of the negotiations. Months before formal negotiations began between the U.S. and Mexico in July 1991, Congress held a series of hearings on the NAFTA where all issues were presented by groups opposing and supporting the agreement. Congressional opponents of the agreement like Congressman Richard Gephardt, the Democrat from Missouri, made their preferences known to the Administration at that time.

Fast track procedures do not produce secret negotiations. Because they are rules that Congress has imposed on itself, fast track procedures do not limit congressional power to control trade issues, and can be overridden at any time. These procedures simply limit the ability of special interest groups with well-financed lobbying efforts to undermine an agreement that would be acceptable to Congress as a whole.

Q: Should the agreement be renegotiated since a new President will have to implement the agreement?

Now that the White House is occupied by a new President, NAFTA opponents are portraying the agreement as a Republican accord that must be renegotiated to accommodate the new policies of Bill Clinton. However, free trade in general and the NAFTA in particular are not partisan issues. The NAFTA was not planned, debated, or negotiated along partisan lines. Some of the strongest NAFTA supporters, such as former Texas Senator and now Treasury Secretary Lloyd Bentsen and New Mexico Congressman Bill Richardson, are Democrats. In

23 *Ibid.*

addition, President Clinton himself has long supported the agreement. The U.S. needs to demonstrate continuity and reliability in its dealings with foreign countries on trade issues if its interests are to be effectively advanced.

Q: Should NAFTA incorporate a "social charter" similar to the model the European Community has adopted?

Some groups opposing free trade are demanding that the Clinton Administration adopt a European-style social charter through the parallel negotiations on labor and environmental issues. A NAFTA that heavily regulates labor and environmental issues would be an albatross for U.S. competitiveness and significantly reduce the level of potential exports to Mexico from small and medium-sized U.S. businesses. A regulated commercial accord, modeled after Europe's Social Charter, would also set a bad precedent for future regional accords and multilateral trade agreements like the General Agreement on Tariffs and Trade (GATT), leading to an overall reduction in global trade.

Including non-commercial issues into a trade accord provides protectionists and others who oppose free trade in principle with endless excuses to raise trade barriers. Labor relations, environmental protection, and political reform are far more complicated for governments to manage than traditional commercial activities. The result is usually a trade arrangement that increases government intervention, regulation, and bureaucracy and decreases the amount of trade the agreement was intended to encourage.

The example of the European Community is instructive. Although the European Community set out to create a single market by removing barriers to trade, the economic benefits of this opening have been more than offset by the imposition of a heavy regulatory burden in a wide-ranging social charter that mandates costly standards for labor, wages, and the environment. A vast and unelected bureaucracy has arisen to administer these regulations, armed with extensive regulatory and enforcement powers.

Groups calling for a social charter speak of the virtues of global environmentalism and worker safety. Creating enforcement commissions, citizen's courts, and sanctions for divergent environmental and labor standards—the wish list of groups seeking a social charter—may appear to be cost-free. Unfortunately, an environmental and social charter imposed on North American commerce will take on a regulatory life of its own, forcing U.S. business to waste time and money dealing with expanding regulatory bureaucracies—money which would be better spent on investment. Companies with little political clout and few Washington lobbyists, especially small and medium-sized businesses, would be the principal victims.

Recent federal overregulation of U.S. small and medium-sized businesses provides an illustrative example. Between 1989 and 1992, increased environmental, labor, and health regulations imposed by Congress cost U.S. business an additional $130 billion. Small businesses were hit with a 34 percent increase in government regulations that significantly slowed job growth in the small business sector after 1990. The Congressional Joint Economic Committee called this federal regulatory intrusiveness "economic crib death." Increasing these burdens on U.S. exporters by imposition of an ambitious social charter would only further damage U.S. competitiveness.

CONCLUSION

The U.S. and Mexico have had a long and often difficult history as neighbors. For the last 150 years, cooperation between the two countries has been more the exception than the rule. Today, however, America and Mexico are entering a new era, one characterized by increasing cooperation. By removing the barriers to trade and investment that limit the growth of both countries, NAFTA will contribute not only to a cementing of good bilateral relations, but also to expanding economic opportunity throughout North America.

Fortunately, Mexico's modernization coincides with America's need to remain internationally competitive as it enters the 21st century. The world's largest exporter, the U.S. will rely increasingly upon international trade for its prosperity, which will require reducing barriers to trade world-wide. By creating a free trade area in North America, the NAFTA will help American industry grow at home and remain competitive abroad, while also giving a major boost to global free trade.

Despite the fact that all objective studies of the effects of the NAFTA clearly indicate that it will benefit all three countries, there is significant political opposition to the agreement in the U.S. Although many of the concerns raised are real, much of the opposition is based upon a desire to protect the special interests of politically powerful constituencies who are opposed to free trade.

There are indeed many problems in both Mexico and the U.S. that the agreement does not solve, such as environmental pollution. But the best method of addressing these is not through the creation of yet another regulatory bureaucracy that will inevitably limit economic growth, but through the increased prosperity that free trade will bring.

While not perfect, the NAFTA is a major step forward from the existing relationship between Mexico and the U.S. A rejection of the NAFTA, or a renegotiation of it to produce more governmental control of trade, would do little to protect U.S. jobs or promote environmental protection. In fact, a managed North American free trade zone could be worse than the existing trading system with Mexico. It would raise the costs for small and medium-size U.S. businesses and limit private resources available for environmental protection. Under a managed trade system, power would flow to the numerous government bureaucrats and industry lawyers that would result from increases in regulations in order to "manage" trade.

The NAFTA is a culmination of two years of close cooperation between the U.S., Mexican and Canadian governments. The NAFTA represents decades of increased trade among the three countries. Its creation will put the U.S. firmly on a more competitive footing with other industrialized nations into the 21st century. This will be good for U.S. businesses and U.S. workers alike.

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