

The Future of North American Integration post-Bush

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North America Running Out of Steam

North American Integration is an economic not political challenge, no one wants to integrate the three countries into one. But since NAFTA-induced economic growth ran out of steam around 2000, political issues have taken the forefront, casting a new light on the future of this process. Since 2001, a series of bilateral security measures have taken the forefront. To the degree that these local security agreements have an economic justification – keeping the U.S.-Canadian and U.S.-Mexican borders open to trade — they have been well received. However, any suggestion of support for Bush's war in Iraq has already been rejected. Canada and Mexico are extremely wary of becoming too closely associated with the United States for fear of becoming surrogate targets for terrorism.

Yet George Bush's departure isn't enough to put North American Integration back on track. If John McCain wins the presidency, as a supporter of the Iraq war, he would be unable to provide the kind of leadership that could dissolve the hesitancy felt by other countries towards association with the U.S. And even though the Democratic candidates' anti-war stand is more palatable, they are unfortunately riding the anti-trade wave in the U.S.

Hillary's Sprint

Hillary Clinton inherited economic advisors, such as ex-Treasury Secretary Robert Rubin and ex-Deputy Secretary Roger Altman, but seems to be increasingly influenced by her additional consultations with AFL-CIO officials. Hence, she recently began to promote “smart trade” and a “time out” before any new trade agreements are made, until these “can be made to raise the living-standards of average Americans”. Furthermore, as Senator, Clinton maintained that the U.S. should be just as protectionist as other countries. For example, in regards to Mexican long-haul trucking entering the U.S., as agreed to under NAFTA, Clinton co-sponsored an amendment refusing to fund the pilot program that would attest to its safety. Were it just tough enforcement of environmental and labor regulations, it would be one thing, but violating the NAFTA agreement seems to preclude further regional integration.

Obama's Marathon

Barack Obama might be more in support of free trade, because his top economic advisor is Austin Goolsbee, from the University of Chicago, who espouses the free movement of both capital and labor as the best means for promoting social justice. Hence, even when speaking before workers at the General Motors factory in Janesville, Wisconsin, Obama said “I won't stand here and tell you that we can –or should– stop free trade. We can't stop every job from going overseas. ... I don't know about a “time-out”, but ... I will not sign another trade agreement unless it has protections for our environment and protections for American workers. And I'll pass the Patriot Employer Act that ... will end the tax breaks for

companies who ship our jobs overseas...”. While it’s true that, as Senator, Obama defended the interests of the Illinois Corn Growers and Soybean Associations, as president he has promised to “work with the leaders of Canada and Mexico to fix NAFTA so that it works for American workers”, which sounds more promising than having the three countries back out of the parts of the agreement that are disagreeable to their special interests.

NAFTA Challenges

The big question is whether fixing NAFTA means deepening North American Integration or letting it stay at it’s present levels. As a regional agreement, NAFTA was originally intended to give certain preferences to its members; but the World Trade Organization (WTO), which was created one year afterwards, extended most of the regional concessions to WTO member countries, and at the same time put China and other countries on a schedule for WTO admission. In addition the U.S. has, since NAFTA, signed many other new bi-lateral trade agreements, forcing Canada and Mexico to follow suit. As a result, NAFTA has lost its specificity, changing from a regional to a globalizing free trade agreement. This hits Mexico especially hard because its place as the low-cost North American partner was quickly supplanted by newcomers to the WTO. Under NAFTA, the U.S. was expected to relocate a large share of their labor intensive industrial processes in Mexico, as a result of which industrial activity would increase to the extent where it could absorb the rural population displaced by increased agricultural imports. Even though there was significant *maquiladora* growth at the beginning of the NAFTA period, Mexico has

been having trouble keeping investors in the country since 2001, when China came aboard.

In theory, industrial salaries should also have risen as a result of NAFTA. Even though they did, slightly, in the *maquiladora* industry after 1994 when NAFTA went into effect, they started to drop again after 2001. In the manufacturing industry, salaries have suffered sharp declines after the 1982 crisis, and again in 1995, never recovering their former levels. What this means for the U.S. and Canada is that, in lieu of growing industrial employment and salaries in Mexico, the excess population migrates North, competing directly with northern workers. There is, however, a solution to this regional conundrum that would benefit the entire region: returning to the original NAFTA proposal to create a regional subcontracting system that would go beyond the assembly of goods in Mexico, helping certain branches of the Mexican manufacturing sector reconvert into producers of some of parts for the *maquiladora* industry, thereby stimulating both employment growth and salary gains.

NAFTA discourages imports from non-member countries by charging tariffs on them, while allowing duty-free entry of North American goods. Under NAFTA rules, this was supposed to be the case in the *maquiladora* industry as well, but things changed. Mexico was supposed to start charging its general tariff on temporary imports from “third-parties” for assembly in the *maquiladoras* and re-export to the U.S. This would have represented a significant change from the old system in which *maquiladoras* imported duty-free and only paid duties in the U.S. when the final consumer goods were imported. The obligation to pay extra tariffs

could have stimulated production of intermediary goods in Mexico; however, the transition period before duties would have to be paid ended January 1st 2001. As it turned out this was too short a time-span for substitute production to get underway in Mexico, especially considering the context of its 1995 financial crisis which dried up all credit and threw the manufacturing industry into a downward spiral.

Therefore, the *maquiladora* industry was faced with paying additional Mexican tariffs on imported “third-party” intermediary goods, or with importing through the U.S. where tariffs are low but additional transport costs would incur. The end result of either would compromised the industry’s competitiveness, which led Mexico a different strategy: reducing its general tariffs on all these “third-party” intermediary imports to the same level as the U.S. tariff, thereby making it feasible to import directly into the country of assembly with no extra duties on the way through. Hence, Mexico was able to keep its maquiladora industry but lost the opportunity it had bargained for under NAFTA to turn it into the manufacturing hub of parts for the *maquiladora* industry. This is not just Mexico’s misfortune; it is a North American problem to the degree it has caused the exodus of Mexican migrants fleeing the consequences of a failed NAFTA.

A Post-Bush Solution

The solution to this regional conundrum is to recreate the original NAFTA proposal. This could be accomplished by means of a combination of cooperative measures: for example, pledges on the part of companies to source their intermediary goods in North America; pro-active regional industrial policies to promote regional production of intermediary goods;

and time-frames within which Mexico would reestablish its general tariff on select “third-party” intermediary goods, which would not entail breaking any trade agreements since these tariffs were lowered unilaterally within the context of temporary programs. Taken as a whole, this would be a practical policy to solve a tandem of regional problems: production would be encouraged to return to North America, with Mexico as its preferred low-cost alternative site. Such a strategy would enable Mexican employment to grow to the point where eventually, salaries for Mexico’s hard-pressed millions would rise, and immigration would finally start to fall. There is no other logic that would address Mexico’s deep-seated structural problems.