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The North American Free Trade Agreement (NAFTA)

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Summary

The North American Free Trade Agreement (NAFTA) entered into force on January 1, 1994. The agreement was signed by President George H. W. Bush on December 17, 1992, and approved by Congress on November 20, 1993. The NAFTA Implementation Act was signed into law by President William J. Clinton on December 8, 1993 (P.L. 103-182). The overall economic impact of NAFTA is difficult to measure since trade and investment trends are influenced by numerous other economic variables, such as economic growth, inflation, and currency fluctuations. The agreement may have accelerated the trade liberalization that was already taking place, but many of these changes may have taken place with or without an agreement. Nevertheless, NAFTA is significant because it was the most comprehensive free trade agreement (FTA) negotiated at the time and contained several groundbreaking provisions. A legacy of the agreement is that it has served as a template or model for the new generation of FTAs that the United States later negotiated and it also served as a template for certain provisions in multilateral trade negotiations as part of the Uruguay Round.

The 114th Congress faces numerous issues related to international trade. Canada and Mexico are the first- and third-largest U.S. trading partners, respectively. With the two countries participating in the negotiations to conclude a Trans-Pacific Partnership (TPP) free trade agreement among the United States and 11 other countries, policy issues related to NAFTA continue to be of interest for Congress. If an agreement is concluded, it could affect the rules and market access commitments governing North American trade and investment since NAFTA entered into force. A related trade policy issue in which the effects of NAFTA may be explored is the possible renewal of Trade Promotion Authority (TPA; formerly known as "fast-track authority") to provide expedited procedures for the consideration of bills to implement trade agreements.

NAFTA was controversial when first proposed, mostly because it was the first FTA involving two wealthy, developed countries and a developing country. The political debate surrounding the agreement was divisive with proponents arguing that the agreement would help generate thousands of jobs and reduce income disparity in the region, while opponents warned that the agreement would cause huge job losses in the United States as companies moved production to Mexico to lower costs. In reality, NAFTA did not cause the huge job losses feared by the critics or the large economic gains predicted by supporters. The net overall effect of NAFTA on the U.S. economy appears to have been relatively modest, primarily because trade with Canada and Mexico accounts for a small percentage of U.S. GDP. However, there were worker and firm adjustment costs as the three countries adjusted to more open trade and investment among their economies.

The rising number of bilateral and regional trade agreements throughout the world and the rising presence of China in Latin America could have implications for U.S. trade policy with its NAFTA partners. Some proponents of open and rules-based trade maintain that a further deepening of economic relations with Canada and Mexico will help promote a common trade agenda with shared values and generate economic growth. Some opponents argue that the agreement has caused worker displacement and that NAFTA needs to be reopened. One possible way of doing this is through the proposed TPP. The ongoing TPP negotiations, launched in the fall of 2008, may not result in a reopening of NAFTA, but could alter some of the rules and market access commitments governing North American trade and investment.

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Introduction

The North American Free Trade Agreement (NAFTA) has been in effect since January 1, 1994. Signed by President George H. W. Bush on December 17, 1992, and approved by Congress on November 20, 1993, the NAFTA Implementation Act was signed into law by President William J. Clinton on December 8, 1993 (P.L. 103-182). NAFTA continues to be of interest to Congress because of the importance of Canada and Mexico as U.S. trading partners, and also because of the implications NAFTA has for U.S. trade policy. This report provides an overview of North American trade liberalization before NAFTA, an overview of NAFTA provisions, the economic effects of NAFTA, and policy considerations.

The 114th Congress, in both its legislative and oversight capacities, faces numerous issues related to international trade. The Obama Administration has made the proposed Trans-Pacific Partnership (TPP) free trade agreement one of its top trade priorities.[1] The United States, Canada, and Mexico, along with nine other countries, are participating in the TPP negotiations. If negotiations are concluded and Congress approves an agreement, it would affect the rules and market access commitments governing North American trade since NAFTA entered into force. A related trade policy issue in which the effects of NAFTA may be explored is the possible renewal of Trade Promotion Authority (TPA; formerly known as "fast-track authority") to provide expedited procedures for the consideration of bills to implement trade agreements.[2]

Some trade policy experts and economists give credit to NAFTA and other free trade agreements (FTAs) for enhancing economic linkages between countries, creating more efficient production processes, increasing the availability of lower-priced consumer goods, and improving living standards and working conditions. Others have blamed FTAs for disappointing employment trends, a decline in U.S. wages, and for not having done enough to improve labor standards and environmental conditions abroad.

NAFTA influenced other FTAs that the United States later negotiated and also influenced multilateral negotiations. NAFTA initiated a new generation of trade agreements in the Western Hemisphere and other parts of the world, influencing negotiations in areas such as market access, rules of origin, intellectual property rights, foreign investment, dispute resolution, worker rights, and environmental protection. The United States currently has FTAs with 20 countries. As with NAFTA, these trade agreements have often been supported or criticized on similar arguments related to jobs.

Market Opening Prior to NAFTA

The concept of economic integration in North America was not a new one at the time NAFTA negotiations started. In 1911, President William Howard Taft signed a reciprocal trade agreement

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[1] See CRS Report R42694, *The Trans-Pacific Partnership (TPP) Negotiations and Issues for Congress*, coordinated by (name redacted).

[2] Trade Promotion Authority, formerly called "fast-track authority" is the authority Congress grants to the President to enter into certain reciprocal trade agreements, and to have their implementing bills considered under expedited legislative procedures, provided the President observes certain statutory obligations. For more information, see CRS Report RL33743, *Trade Promotion Authority (TPA) and the Role of Congress in Trade Policy*, by (name redacted).

with Canadian Prime Minister Sir Wilfred Laurier. After a bitter election, Canadians rejected free trade and ousted Prime Minister Laurier, thereby ending the agreement. In 1965, the United States and Canada signed the U.S.-Canada Automotive Products Agreement that liberalized trade in cars, trucks, tires, and automotive parts between the two countries.[3] The Auto Pact was credited as a pioneer in creating an integrated North American automotive sector. In the case of Mexico, the government had been implementing reform measures since the mid-1980s, prior to NAFTA, to liberalize its economy. By 1990, when NAFTA negotiations began, Mexico had already taken significant steps towards liberalizing its protectionist trade regime.

The U.S.-Canada Free Trade Agreement of 1989

The United States and Canada recently marked the 25th anniversary of the October 3, 1987, signing of the U.S.-Canada Free Trade Agreement (FTA). The FTA was the first economically significant bilateral FTA signed by the United States.[4] Implementing legislation[5] was approved by both houses of Congress under "fast-track authority"—now known as trade promotion authority (TPA)—and signed by President Ronald Reagan on September 28, 1988. While the FTA generated significant policy debate in the United States, it was a watershed moment for Canada. Controversy surrounding the proposed FTA led to the so-called "free trade election" in 1988, in which sitting Progressive Conservative Prime Minister Brian Mulroney, who negotiated the agreement, defeated Liberal party leader John Turner, who vowed to reject it if elected. After the election, the FTA was passed by Parliament in December 1988, and it came into effect between the two nations on January 1, 1989. At the time, it probably was the most comprehensive bilateral FTA negotiated worldwide and contained several groundbreaking provisions. It

- Eliminated all tariffs by 1998. Many were eliminated immediately, and the remaining tariffs were phased out in 5-10 years.
- Continued the 1965 U.S.-Canada Auto Pact, but tightened its rules of origin. Some Canadian auto sector practices not covered by the Auto Pact were ended by 1998.
- Provided national treatment for covered services providers and liberalized financial services trade. Facilitated cross-border travel for business professionals.
- Committed to provide prospective national treatment for investments originating in the other, although established derogations from national treatment such as for national security or prudential reasons were allowed to continue. Banned imposition of performance requirements, such as local content, import substitution, or local sourcing requirements.
- Expanded the size of federal government procurement markets available for competitive bidding from suppliers of the other country. It did not include sub-federal government procurement.
- Provided for a binding binational panel to resolve disputes arising from the agreement (a Canadian insistence).

[3] The Canada-United States Automotive Products Agreement removed tariffs on cars, trucks, buses, tires, and automotive parts between the two countries. NAFTA effectively superseded this agreement.

[4] Prior to the U.S.-Canada FTA, the only bilateral U.S. FTA was with Israel.

[5] United States-Canada Free-Trade Agreement Implementation Act of 1988 (P.L. 100-449).

- Prohibited most import and export restrictions on energy products, including minimum export prices. This was carried forth in NAFTA only with regard to Canada-U.S. energy trade.

Many of these provisions were incorporated into, or expanded in, NAFTA. However, the FTA did not include, or specifically exempted, some issues that would appear in NAFTA for the first time. These include

- **Intellectual property rights (IPR).** The FTA did not contain language on intellectual property rights. NAFTA was the first FTA to include meaningful disciplines on IPR.
- **Cultural exemption.** It exempted the broadcasting, film, and publishing sectors. This exemption continues in NAFTA.
- **Transportation services and investment** in the Canadian energy sector were excluded from the FTA. These exclusions were limited in NAFTA.
- **Trade remedies**. Neither the FTA nor NAFTA ended the use of trade remedy actions (anti-dumping, countervailing duty, or safeguards) against the other. This was a key Canadian goal of the FTA. NAFTA did create a separate dispute settlement mechanism to adjudicate trade remedy disputes, but this mechanism has not been replicated in other FTAs.
- **Softwood lumber.** The FTA grandfathered in the then-present 1986 Memorandum of Understanding (MOU) governing softwood lumber trade. Over time, the MOU has been replaced by other agreements—such as the current Softwood Lumber Agreement (SLA) expiring in October 2015—and, at times, by resort to trade remedy actions.
- **Agricultural supply management**. Canada was able to exempt its agriculture supply management system, although it committed to allow a small increase in imports of dairy, poultry, and eggs, which carried over into the NAFTA. The United States was also able to exclude certain products from liberalization commitments under the FTA and the NAFTA.

Mexico's Pre-NAFTA Trade Liberalization Efforts

Well before NAFTA negotiations began, Mexico was liberalizing its protectionist trade and investment policies that had been in place for decades (see **Appendix B** for more information on Mexico's pre-NAFTA protectionist policies). The restrictive trade regime began after Mexico's revolutionary period and remained until the early- to mid-1980s when the country was facing a debt crisis. It was at this time that the government took unilateral steps to open and modernize its economy by relaxing investment policies and liberalizing trade barriers. The trade liberalization measures that began in the mid-1980s shifted Mexico from one of the world's most protected economies into one of the most open. Mexico now has 12 FTAs involving 44 countries.[6]

Mexico's first steps in opening its closed economy focused on reforming its import substitution policies in the mid-1980s. Further reforms were made in 1986 when Mexico became a member of

[6] See CRS Report R40784, *Mexico's Free Trade Agreements*, by (name redacted).

the General Agreement on Tariffs and Trade (GATT). As a condition of becoming a GATT member, for example, Mexico agreed to lower its maximum tariff rates to 50%. Mexico went further by reducing its highest tariff rate from 100% to 20%. Mexico's trade-weighted average tariff fell from 25% in 1985 to about 19% in 1989.[7]

Although Mexico had been lowering trade and investment restrictions since 1986, the number of remaining barriers for U.S. exports remained high at the time of the NAFTA negotiations. Mexico required import licenses on 230 products from the United States, affecting about 7% of the value of U.S. exports to Mexico. Prior to its entry into GATT, Mexico required import licenses on all imports. At the time of the NAFTA negotiations, about 60% of U.S. agricultural exports to Mexico required import licenses. Mexico also had numerous other nontariff barriers, such as "official import prices," an arbitrary customs valuation system that raised duty assessments.[8]

For Mexico, an FTA with the United States represented a way to lock in the reforms of its market opening measures from the mid-1980s to transform Mexico's formerly statist economy after the devastating debt crisis of the 1980s.[9] The combination of the severe economic impact of the debt crisis, low domestic savings, and an increasingly overvalued peso put pressure on the Mexican government to adopt market-opening economic reforms and boost imports of goods and capital to encourage more competition in the Mexican market. An FTA with the United States was a way of blocking domestic efforts to roll back Mexican reforms, especially in the politically sensitive agriculture sector. NAFTA helped deflect protectionist demands of industrial groups and special interest groups in Mexico.[10] One of the main goals of the Mexican government was to increase investment confidence in order to attract greater flows of foreign investment and spur economic growth. Since the entry into force of NAFTA, Mexico has used the agreement as a basic model for other FTAs Mexico has signed with other countries.[11]

For the United States, NAFTA represented an opportunity to expand the growing export market to the south, but it also represented a political opportunity for the United States and Mexico to work together in resolving some of the tensions in the bilateral relationship.[12] An FTA with Mexico would help U.S. businesses expand exports to a growing market of almost 100 million people. U.S. officials also recognized that imports from Mexico would likely include higher U.S. content than imports from Asian countries. In addition to the trade and investment opportunities that NAFTA represented, an agreement with Mexico would be a way to support the growth of political pluralism and a deepening of democratic processes in Mexico. NAFTA also presented an opportunity for the United States to spur the slow progress on the Uruguay Round of multilateral trade negotiations.[13]

[7] United States International Trade Commission (USITC), *The Likely Impact on the United States of a Free Trade Agreement with Mexico,* Publication 2353, February 1991.

[8] Ibid., pp. 1-2.

[9] Gary Clyde Hufbauer and Jeffrey J. Schott, *NAFTA Revisited: Achievements and Challenges,* Institute for International Economics, October 2005.

[10] Ibid.

[11] Mexico has a total of 12 free trade agreements involving 44 countries. These include agreements with most countries in the Western Hemisphere including the United States, Canada, Chile, Colombia, Costa Rica, Nicaragua, Peru, Guatemala, El Salvador, and Honduras. In addition, Mexico has negotiated FTAs outside of the Western Hemisphere and entered into agreements with Israel, Japan, and the European Union.

[12] Hufbauer and Schott, *NAFTA Revisited: Achievements and Challenges*, pp. 2-3.

[13] Ibid.

Overview of NAFTA Provisions

At the time that NAFTA was implemented, the U.S.-Canada FTA was already in effect and U.S. tariffs on most Mexican goods were low. NAFTA opened up the U.S. market to increased Mexican imports and the Mexican market to the United States and Canada, creating one of the largest single markets in the world. Some of the key NAFTA provisions included tariff and non-tariff trade liberalization, rules of origin, services trade, foreign investment, intellectual property rights protection, government procurement, and dispute resolution. Labor and environmental provisions were included in separate NAFTA side agreements.

Removal of Trade Barriers

The market opening provisions of the agreement gradually eliminated all tariffs and most non-tariff barriers on goods produced and traded within North America over a period of 15 years after it entered into force. Some tariffs were eliminated immediately, while others were phased out in various schedules of 5 to 15 years. U.S. import-sensitive sectors, such as glassware, footwear, and ceramic tile, received longer phase-out schedules.[14] NAFTA provided the option of accelerating tariff reductions if the countries involved agreed.[15] The agreement included safeguard provisions in which the importing country could increase tariffs, or impose quotas in some cases, on imports during a transition period if domestic producers faced serious injury as a result of increased imports from another NAFTA country. It terminated all existing drawback programs by January 1, 2001.[16]

Given that the U.S.-Canada FTA was already in place, most of the market opening measures resulted in the removal of U.S. tariffs and quotas applied to imports from Mexico, and Mexican trade barriers applied to imports from the United States and Canada. At the time that NAFTA went into effect, about 40% of U.S. imports from Mexico entered duty-free and the remainder faced duties of up to 35%, with a trade-weighted average rate of about 7%. Mexico's trade-weighted tariff on U.S. agricultural products averaged about 11%. Also affecting U.S.-Mexico trade were both countries' phytosanitary rules, Mexican import licensing requirements, and U.S. marketing orders.[17]

Some of the more significant changes took place in the textiles, apparel, automotive, and agricultural industries. Elimination of trade barriers in these key industries are summarized below.

- **Textiles and Apparel Industries.** NAFTA phased out all duties on textile and apparel goods within North America meeting specific NAFTA rules of origin[18]

[14] Governments of Canada, the United Mexican States, and the United States of America, *Description of the Proposed North American Free Trade Agreement*, August 12, 1992.

[15] Congressional Quarterly Almanac 1993, pp. 171-175, 180-181.

[16] A duty drawback is the refund or waiver in whole or in part of customs duties assessed or collected upon importation of an article or materials which are subsequently exported.

[17] Marketing orders were designed to set national guidelines for product quality, market promotion, and supply levels. The most significant Mexican products that were affected by U.S. marketing orders included tomatoes, onions, avocados, grapefruit, oranges, olives, and table grapes.

[18] NAFTA rules of origin for textiles and apparel define when imported textile or apparel goods qualify for preferential treatments. For most products, the rule of origin is "yarn forward", which means that goods must be produced from yarn made in a NAFTA country to benefit from preferential treatment.

over a 10-year period. Prior to NAFTA, 65% of U.S. apparel imports from Mexico entered duty-free and quota-free, and the remaining 35% faced an average tariff rate of 17.9%. Mexico's average tariff on U.S. textile and apparel products was 16%, with duties as high as 20% on some products.[19]

- **Automotive Industry.** NAFTA phased out Mexico's restrictive auto decree. It phased out all U.S. tariffs imports from Mexico and Mexican tariffs on U.S. and Canadian products as long as they met the rules of origin requirements of 62.5% North American content for autos, light trucks, engines and transmissions; and 60% for other vehicles and automotive parts. Some tariffs were eliminated immediately, while others were phased out in periods of 5 to 10 years. Prior to NAFTA, the United States assessed the following tariffs on imports from Mexico: 2.5% on automobiles, 25% on light-duty trucks, and a trade-weighted average of 3.1% for automotive parts. Mexican tariffs on U.S. and Canadian automotive products were as follows: 20% on automobiles and light trucks, and 10%-20% on auto parts.[20]
- **Agriculture.** NAFTA set out separate bilateral undertakings on cross-border trade in agriculture, one between Canada and Mexico, and the other between Mexico and the United States. As a general matter, U.S.-Canada FTA provisions continued to apply on trade with Canada.[21] Regarding U.S.-Mexico agriculture trade, NAFTA eliminated most non-tariff barriers in agricultural trade, either through their conversion to tariff-rate quotas (TRQs)[22] or ordinary tariffs. Tariffs were phased out over a period of 15 years with sensitive products such as sugar and corn receiving the longest phase-out periods. Approximately one-half of U.S.-Mexico agricultural trade became duty-free when the agreement went into effect. Prior to NAFTA, most tariffs, on average, in agricultural trade between the United States and Mexico were fairly low though some U.S. exports to Mexico faced tariffs as high as 12%. However, approximately one-fourth of U.S. agricultural exports to Mexico (by value) were subjected to restrictive import licensing requirements.[23]

Services Trade Liberalization

NAFTA services provisions established a set of basic rules and obligations in services trade among partner countries. The agreement expanded on initiatives in the U.S.-Canada FTA and the Uruguay Round of multilateral trade negotiations to create internationally agreed disciplines on government regulation of trade in services.[24] The agreement granted services providers certain

[19] Business Roundtable, *NAFTA: A Decade of Growth,* Prepared by The Trade Partnership, Washington, DC, February 2004, p. 33.

[20] Ibid., p. 30.

[21] Governments of Canada, the United Mexican States, and the United States of America, *Description of the Proposed North American Free Trade Agreement*, August 12, 1992, p. 12.

[22] Tariff-rate quotas (TRQs) allowed NAFTA partners to export specified quantities of a product to other NAFTA countries at a relatively low tariff, but subjected all imports of the product above a pre-determined threshold to a higher tariff.

[23] Business Roundtable, *NAFTA: A Decade of Growth,* p. 35.

[24] The Governments of Canada, the United Mexican States, and the United States of America, *Description of the Proposed North American Free Trade Agreement*, August 12, 1992, pp. 23-24.

rights concerning nondiscriminatory treatment, cross-border sales and entry, investment, and access to information. However, there were certain exclusions and reservations by each country. These included maritime shipping (United States), film and publishing (Canada), and oil and gas drilling (Mexico).[25] Although NAFTA liberalized certain service sectors in Mexico, particularly financial services, which profoundly altered its banking sector, other sectors were barely affected.[26] In telecommunications services, NAFTA partners agreed to exclude provision of, but not the use of, basic telecommunications services. NAFTA granted a "bill of rights" for the providers and users of telecommunications services, including access to public telecommunications services; connection to private lines that reflect economic costs and available on a flat-rate pricing basis; and the right to choose, purchase, or lease terminal equipment best suited to their needs.[27] However, NAFTA did not require parties to authorize a person of another NAFTA country to provide or operate telecommunications transport networks or services. NAFTA did not bar a party from maintaining a monopoly provider of public networks or services, such as Telmex, Mexico's dominant telecommunications company.[28]

Other Provisions

In addition to market opening measures through the elimination of tariff and non-tariff barriers, NAFTA incorporated numerous other provisions, including foreign investment, intellectual property rights (IPR), dispute resolution, and government procurement.

- **Foreign Investment.** NAFTA removed significant investment barriers, ensured basic protections for NAFTA investors, and provided a mechanism for the settlement of disputes between investors and a NAFTA country. NAFTA provided for "non-discriminatory treatment" for foreign investment by NAFTA parties in certain sectors of other NAFTA countries. The agreement included explicit country-specific liberalization commitments and exceptions to national treatment. Exemptions from NAFTA investment provisions include the energy sector in Mexico in which the Mexican government reserved the right to prohibit foreign investment. It also included exceptions related to national security and to Canada's cultural industries.[29]
- **IPR.** NAFTA built upon the then-ongoing Uruguay Round negotiations that would create the Trade Related Aspects of Intellectual Property Rights (TRIPS) agreement in the World Trade Organization and on various existing international intellectual property treaties. The agreement set out specific enforceable commitments by NAFTA parties regarding the protection of copyrights, patents, trademarks, and trade secrets, among other provisions.
- **Dispute Settlement Procedures.** NAFTA's provisions for preventing and settling disputes were built upon provisions in the U.S.-Canada FTA. NAFTA created a system of arbitration for resolving disputes that included initial consultations,

[25] United States General Accounting Office (GAO), "North American Free Trade Agreement: Assessment of Major Issues, Volume 2," *Report to the Congress,* September 1993, pp. 35-36.

[26] Hufbauer and Schott, *NAFTA Revisited,* pp. 25-29.

[27] GAO, *Report to Congress,* September 1993, pp. 38-39.

[28] *Description of the Proposed North American Free Trade Agreement*, August 12, 1992, p. 29.

[29] Ibid., pp. 30-32.

taking the issue to the NAFTA Trade Commission, or going through arbitral panel proceedings.[30] NAFTA included separate dispute settlement provisions for addressing disputes over antidumping and countervailing duty determinations.

- **Government Procurement**. NAFTA opened up a significant portion of federal government procurement in each country on a nondiscriminatory basis to suppliers from other NAFTA countries for goods and services. It contains some limitations for procurement by state-owned enterprises.[31]

NAFTA Side Agreements on Labor and the Environment

The NAFTA text did not include labor or environmental provisions, which was a major concern to many in Congress at the time of the agreement's consideration. Some policymakers called for additional provisions to address numerous concerns about labor and environmental issues, specifically in Mexico. Other policymakers argued that the economic growth generated by the FTA would increase Mexico's resources available for environmental and worker rights protection. However, congressional concerns from policymakers, as well as concerns from labor and environmental groups, remained strong.

Shortly after he began his presidency, President Clinton addressed labor and environmental concerns by joining his counterparts in Canada and Mexico in negotiating formal side agreements. The NAFTA implementing legislation included provisions related to the side agreements, authorizing U.S. participation in NAFTA labor and environmental commissions and appropriations for these activities. The North American Agreement on Labor Cooperation (NAALC) and the North American Agreement on Environmental Cooperation (NAAEC) entered into force on January 1, 1994, the same day as NAFTA.[32] NAFTA implementing legislation also included two adjustment assistance programs, designed to ease trade-related labor problems: the NAFTA Transitional Adjustment Assistance (NAFTA-TAA) Program and the U.S. Community Adjustment and Investment Program (USCAIP).

The labor and environmental side agreements included language to promote cooperation on labor and environmental matters as well as provisions to address a party's failure to enforce its own labor and environmental laws. Perhaps most notable were the side agreements' dispute settlement processes that, as a last resort, may impose monetary assessments and sanctions to address a party's failure to enforce its laws.[33] NAFTA marked the first time that labor and environmental provisions were associated with an FTA. For many, it represented an opportunity for cooperating on environmental and labor matters across borders and for establishing a new type of relationship among NAFTA partners.[34]

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[30] If the parties are unable to resolve the issue through consultations, they may take the dispute to the NAFTA Trade Commission, which is comprised of Ministers or cabinet-level officers designated by each country. A party may also request the establishment of an arbitral panel, which may make recommendations for the resolution of the dispute.

[31] GAO, *Report to Congress,* September 1993, pp. 69-71.

[32] The USCAIP, administered by the North American Development Bank, provides financial assistance to communities with significant job losses due to changes in trade patterns with Mexico or Canada as a result of NAFTA.

[33] For more information, see CRS Report RS22823, *Overview of Labor Enforcement Issues in Free Trade Agreements*, by (name redacted), and CRS Report 97-291, *NAFTA: Related Environmental Issues and Initiatives*, by (name redacted).

[34] Woodrow Wilson International Center for Scholars, *NAFTA at 10: Progress, Potential, and Precedents*, pp. 20-30.

In addition to the two trilateral side agreements, the United States and Mexico entered into a bilateral side agreement to NAFTA on border environmental cooperation.[35] In this agreement, the two governments committed to cooperate on developing environmental infrastructure projects along the U.S.-Mexico border to address concerns about the degradation of the environment along the U.S.-Mexico border due to increased economic activity. The agreement established two organizations to address these concerns: the Border Environment Cooperation Commission (BECC), located in Juárez, Mexico, and the North American Development Bank (NADBank), located in San Antonio, Texas. The sister organizations work closely together and with other partners at the federal, state and local level in the United States and Mexico to develop, certify, and facilitate financing for water and wastewater treatment, municipal solid waste disposal, and related projects on both sides of the U.S.-Mexico border region. Both organizations also have ongoing efforts to measure the results of the projects on the border region. From 1995 to 2011, BECC certified 189 projects (86 in the United States and 103 in Mexico), representing nearly $4.3 billion in environmental infrastructure investment, directly benefiting 14 million border residents. NADBank has financed 152 of these projects with approximately $1.33 billion in loans and grants.[36] These projects have provided border residents with more access to drinking water, sewer and wastewater treatment. They also include water conservation, air quality, and renewable energy projects.[37]

Trade Trends and Economic Effects

Many economists contend that trade liberalization promotes overall economic growth and efficiency among trading partners, although there are short-term adjustment costs. NAFTA was unusual in global terms because it was the first time that an FTA linked two wealthy, developed countries with a low-income developing country. For this reason, the agreement received considerable attention by U.S. policymakers, manufacturers, service providers, agriculture producers, labor unions, non-government organizations, and academics. Proponents argued that the agreement would help generate thousands of jobs and reduce income disparity between Mexico and its northern neighbors. Opponents warned that the agreement would create huge job losses in the United States as companies moved production to Mexico to lower costs.[38]

Estimating the economic impact of trade agreements is a daunting task due to a lack of data and important theoretical and practical matters associated with generating results from economic models. In addition, such estimates provide an incomplete accounting of the total economic effects of trade agreements.[39] Numerous studies suggest that NAFTA achieved many of the intended trade and economic benefits.[40] Other studies suggest that NAFTA has come at a cost to

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[35] *The Agreement Between the Government of the United States of America and the Government of the United Mexican States Concerning the Establishment of a Border Environment Cooperation Commission and a North American Development Bank*, November 1993.

[36] Border Environment Cooperation Commission, *2011 Annual Report,* p. 7.

[37] Ibid.

[38] See Ross Perot with Pat Choate, *Save Your Job, Save Our Country: Why NAFTA Must be Stopped-Now!,* New York, 1993.

[39] For more information, see CRS Report R41660, *U.S.-South Korea Free Trade Agreement and Potential Employment Effects: Analysis of Studies*, by (name redacted) and (name redacted).

[40] See for example, Gary Clyde Hufbauer and Jeffrey J. Schott, *NAFTA Revisited: Achievements and Challenges,* Institute for International Economics, October 2005; Center for Strategic and International Studies, *NAFTA's Impact on North America: The First Decade,* Edited by Sidney Weintraub, 2004; and U.S. Chamber of Commerce, *Opening* (continued...)

U.S. workers.[41] This has been in keeping with what most economists maintain, that trade liberalization promotes overall economic growth among trading partners, but that there are both winners and losers from adjustments.

Not all changes in trade and investment patterns within North America since 1994 can be attributed to NAFTA because trade has also been affected by a number of factors. The sharp devaluation of the peso at the end of the 1990s and the associated recession in Mexico had considerable effects on trade, as did the rapid growth of the U.S. economy during most of the 1990s and, more recently, the economic slowdown caused by the 2008 financial crisis. Trade-related job gains and losses since NAFTA may have accelerated trends that were ongoing prior to NAFTA and may not be totally attributable to the trade agreement.

U.S. Trade Trends with NAFTA Partners

Overall Trade

U.S. trade with its NAFTA partners has more than tripled since the agreement took effect. It has increased more rapidly than trade with the rest of the world. In 2011, trilateral trade among NAFTA partners reached the $1 trillion threshold. Since 1993, total U.S. trade with Mexico increased more rapidly than total trade with Canada and trade with non-NAFTA countries. In 2014, Canada was the leading market for U.S. exports, while Mexico ranked second. The two countries accounted for 34% of total U.S. exports in 2014. In imports, Canada and Mexico ranked second and third, respectively, as suppliers of U.S. imports in 2014. The two countries accounted for 27% of U.S. imports.[42]

Most of the trade-related effects of NAFTA may be attributed to changes in trade and investment patterns with Mexico because economic integration between Canada and the United States had already been taking place. As mentioned previously, while NAFTA may have accelerated U.S.-Mexico trade since 1993, other factors, such as economic growth patterns, also affected trade. As trade tends to increase during cycles of economic growth, it tends to decrease as growth declines. The economic downturns in 2001 and 2009, for example, likely played a role in the decline in both U.S. exports to and imports from Canada and Mexico, as shown in **Figure 1**.

(...continued)

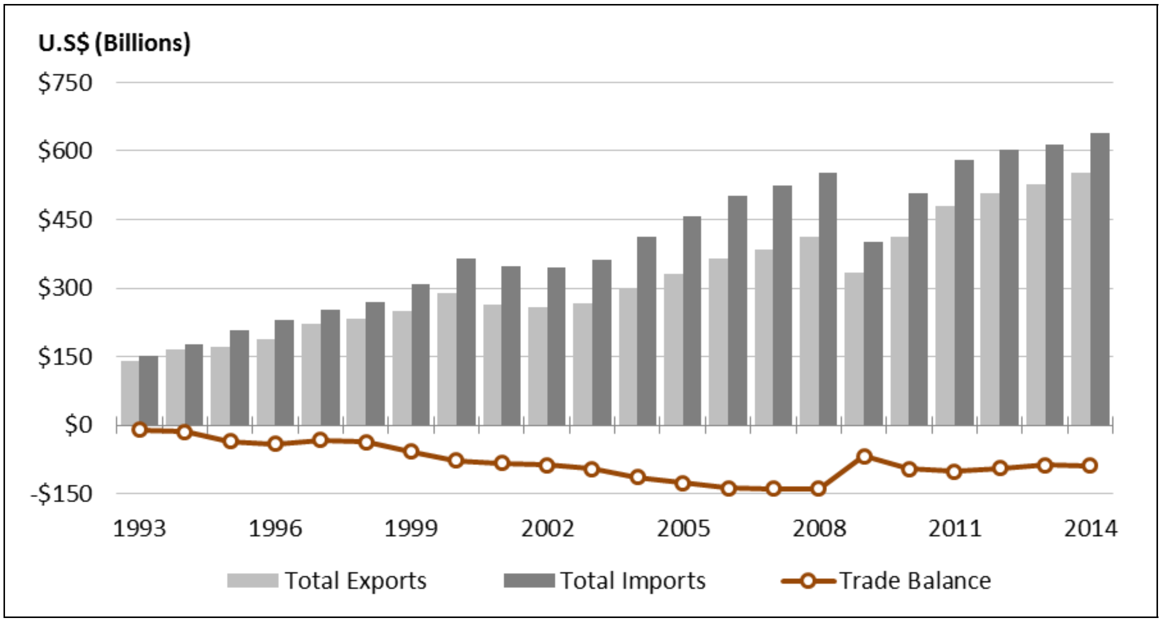
Markets, Creating Jobs: Estimated U.S. Employment Effects of Trade with FTA Partners, 2010.

[41] See for example, Robert E. Scott, *Heading South: U.S.-Mexico Trade and Job Displacement under NAFTA,* Economic Policy Institute, May 3, 2011; and The Frederick S. Pardee Center, *The Future of North American Trade Policy: Lessons from NAFTA,* Boston University, November 2009.

[42] Trade statistics in this paragraph are derived from data from the U.S. International Trade Commission's Interactive Tariff and Trade Data Web, at http://dataweb.usitc.gov.

Figure 1. U.S. Merchandise Trade with NAFTA Partners: 1993-2014

(billions of nominal U.S. dollars)



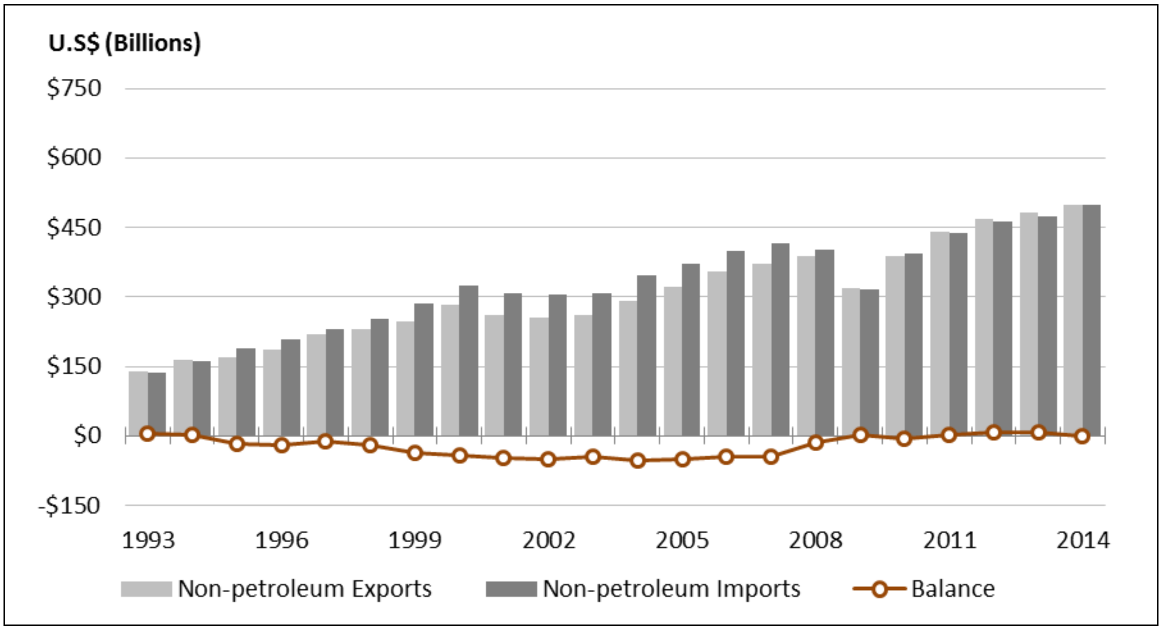
Source: Compiled by CRS using trade data from the U.S. International Trade Commission's Interactive Tariff and Trade Data Web, at http://dataweb.usitc.gov.

Energy Trade Implications

Trade in petroleum products is a central component of U.S. trade with both Canada and Mexico. Approximately 16% of total trade with NAFTA partners is in petroleum products. Canada and Mexico accounted for 46% ($110.9 billion) of total U.S. crude oil imports ($241.8 billion) in 2014. Canada is the leading supplier of crude petroleum oil to the United States, followed by Saudi Arabia and Mexico. If petroleum products are excluded from trade statistics, the United States had a trade surplus with NAFTA partners in merchandise trade between 2011 and 2013, before going to zero in 2014, as shown in **Figure 2**. In 2013, the trade surplus in non-petroleum products was an estimated $9.2 billion.

Figure 2. Non-Petroleum Trade with NAFTA Partners: 1993-2014

(billions of nominal U.S. dollars)



Source: Compiled by CRS using trade data from the U.S. International Trade Commission's (USITC's) Interactive Tariff and Trade Data Web, at http://dataweb.usitc.gov.

Notes: The United States uses different classifications of trade for trade statistics. Trade data in this chart excludes energy trade in three categories: Harmonized Tariff Schedule (HTS) code 2709, petroleum oils and oils from bituminous minerals, crude; HTS code 2710, petroleum oils and oils from bituminous minerals (other than crude) and products therefrom, NESOI, containing 70% (by weight) or more of these oils; and HTS code 2711, petroleum gases and other gaseous hydrocarbons. See http://dataweb.usitc.gov.

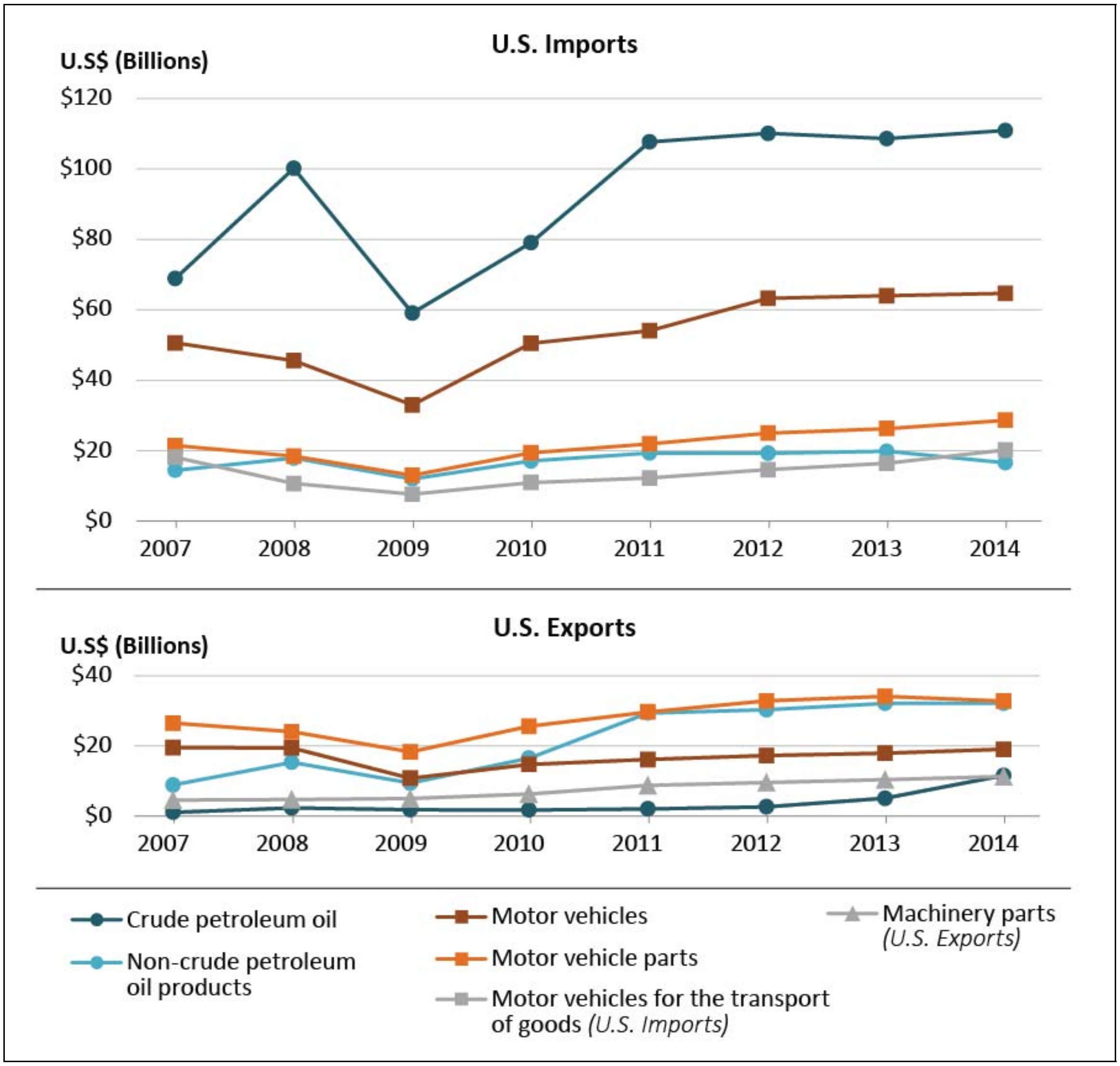
Trade by Product

In 2014, U.S. imports in crude petroleum oil ranked first among the five leading import items from NAFTA partners, as shown in **Figure 3**.[43] The next leading import items were motor vehicles, motor vehicle parts, motor vehicles for the transport of goods, and non-crude petroleum products. The value of crude oil imports from both Canada and Mexico in 2014 totaled $110.9 billion. In 2009, the value of crude oil imports dropped considerably, from $100.1 billion in 2008 to $59.1 billion in 2009, reflecting a drop in oil prices that year. In 2014, the top five U.S. export items to NAFTA partners were motor vehicle parts, non-crude petroleum oil products, motor vehicles, crude petroleum oil, and machinery parts, as shown in **Figure 3**.

[43] This statistic is derived from the Harmonized Tariff Schedule of the United States (HTS), using HTS number 2709 for petroleum oils and oils from bituminous minerals, crude. The HTS comprises a hierarchical structure for describing all goods in trade for duty, quota, and statistical purposes. This structure is based upon the international Harmonized Commodity Description and Coding System (HS), administered by the World Customs Organization in Brussels.

Figure 3. Top Five U.S. Import and Export Items to and from NAFTA Partners

(billions of nominal U.S. dollars)



Source: Compiled by CRS using trade data from the USITC at http://dataweb.usitc.gov.

Notes: Statistics in this figure are derived from the Harmonized Tariff Schedule (HTS) of the United States at the 4-digit level. The HTS comprises a hierarchical structure for describing all goods in trade for duty, quota, and statistical purposes. This structure is based upon the international Harmonized Commodity Description and Coding System (HS), administered by the World Customs Organization in Brussels. See http://dataweb.usitc.gov.

Trade with Canada

U.S. trade with Canada more than doubled in the first decade of the FTA/NAFTA (1989-1999) from $166.5 billion to $362.2 billion. U.S. exports to Canada increased from $100.2 billion in 1993 to $312.1 billion in 2014, an increase of 211%. U.S. imports from Canada increased from $110.9 billion in 1993 to $346.1 billion in 2014, an increase of 212% (see **Table A-1**). After falling off during the recession of 2001, total trade with Canada reached a new high of $596.5 billion in 2008, only to fall victim to the financial crisis in 2009 when it fell to $429.6 billion. In 2011, total trade had returned to 2008 levels at $596.6 billion. The United States has run a trade deficit with Canada since the FTA/NAFTA era, increasing from $9.9 billion in 1989 to $74.6 billion in 2008, before falling back during the 2009 recession. In 2014, the trade deficit with Canada was $33.9 billion. While the increase in the trade deficit with Canada has been attributed to the FTA/NAFTA, the increase has been uneven and may also be attributed to other economic factors, such as energy prices.[44]

In services, the United States had a surplus of $32.8 billion in 2013 in trade with Canada. U.S. private services exports to Canada increased from $17.0 billion in 1993 to $63.3 billion in 2013. U.S. private services imports from Canada increased from $9.1 billion in 1993 to $30.5 billion in 2013, as shown in **Table A-2**.[45]

Trade with Mexico

The United States is, by far, Mexico's leading partner in merchandise trade. U.S. exports to Mexico increased rapidly since NAFTA, increasing from $41.6 billion in 1993 to $240.3 billion in 2014, an increase of 478% (see **Table A-1** in **Appendix A**). U.S. imports from Mexico increased from $39.9 billion in 1993 to $294.2 billion in 2014, an increase of 637%. The trade balance with Mexico went from a surplus of $1.7 billion in 1993 to a deficit of $74.3 billion in 2007. Since then, the trade deficit with Mexico has fallen to $53.8 billion in 2014.[46]

In services, the United States had a surplus of $12.1 billion in 2013 in trade with Mexico. U.S. private services exports to Mexico increased from $10.4 billion in 1993 to $29.9 billion in 2013. U.S. private services imports from Mexico increased from $7.4 billion in 1993 to $17.8 billion in 2013, as shown in **Table A-2**.[47]

Effect on the U.S. Economy

The overall net effect of NAFTA on the U.S. economy has been relatively small, primarily because total trade with both Mexico and Canada was equal to less than 5% of U.S. GDP at the time NAFTA went into effect. Because many, if not most, of the economic effects came as a result of U.S.-Mexico trade liberalization, it is also important to take into account that two-way trade with Mexico was equal to an even smaller percentage of GDP (1.4%) in 1994. Thus, any changes in trade patterns would not be expected to be significant in relation to the overall U.S. economy. A major challenge in assessing NAFTA is separating the effects that came as a result of the agreement from other factors. U.S. trade with Mexico and Canada was already growing prior to NAFTA and it likely would have continued to do so without an agreement. A 2003 report by the Congressional Budget Office observed that it was difficult to precisely measure the effects of NAFTA. It estimated that NAFTA likely increased annual U.S. GDP, but by a very small amount—"probably no more than a few billion dollars, or a few hundredths of a percent."[48] In

[44] Trade statistics in this paragraph are derived from data from the U.S. International Trade Commission's Interactive Tariff and Trade Data Web, at http://dataweb.usitc.gov.

[45] Services trade statistics in this paragraph are derived from the Bureau of Economic Analysis online database at http://www.bea.gov.

[46] Merchandise trade statistics in this paragraph are derived from data from the U.S. International Trade Commission's Interactive Tariff and Trade Data Web, at http://dataweb.usitc.gov.

[47] Services trade statistics in this paragraph are derived from the Bureau of Economic Analysis online database at http://www.bea.gov.

[48] Congressional Budget Office of the United States, "The Effects of NAFTA on U.S.-Mexican Trade and GDP," *A*
(continued...)

some sectors, trade-related effects could have been more significant, especially in those industries that were more exposed to the removal of tariff and non-tariff trade barriers, such as the textile, apparel, automotive, and agriculture industries.

Studies by the U.S. International Trade Commission (USITC) on the effects of NAFTA pointed out the difficulty in isolating the agreement's effects from other factors. Although the effects of NAFTA are not easily measured, the USITC provided some estimates over the years. A 2003 study estimated that U.S. GDP could experience an increase between 0.1% and 0.5% upon full implementation of the agreement.[49] Another USITC study that was congressionally mandated in 1997 offered a comprehensive assessment of the operation and effects of NAFTA after three years.[50] The report estimated that NAFTA had a small, but positive, effect on the overall U.S. economy. Some of the findings include the following: data inadequacies at the industry level made it difficult to isolate the effects of NAFTA on absolute trade flows; U.S. trade with NAFTA partners increased more rapidly than U.S. trade with the rest of the world; the share of U.S. exports in the Mexican market increased by a higher percentage than the share of total imports from other countries; industries such as autos, chemicals, textiles, and electronics benefitted by achieving synergies across the North American market.[51]

U.S. Industries and Supply Chains

Many economists and other observers have credited NAFTA with helping U.S. manufacturing industries, especially the U.S. auto industry, become more globally competitive through the development of supply chains.[52] Much of the increase in U.S.-Mexico trade, for example, can be attributed to specialization as manufacturing and assembly plants have reoriented to take advantage of economies of scale. As a result, supply chains have been increasingly crossing national boundaries as manufacturing work is performed wherever it is most efficient.[53] A reduction in tariffs in a given sector not only affects prices in that sector but also in industries that purchase intermediate inputs from that sector. The importance of these direct and indirect effects is often overlooked, according to one study. The study suggests that these linkages offer important trade and welfare gains from free trade agreements and that ignoring these input-output linkages could underestimate potential trade gains.[54]

Much of the trade between the United States and its NAFTA partners occurs in the context of production sharing as manufacturers in each country work together to create goods. The expansion of trade has resulted in the creation of vertical supply relationships, especially along the U.S.-Mexico border. The flow of intermediate inputs produced in the United States and exported to Mexico and the return flow of finished products greatly increased the importance of

(...continued)

CBO Paper, May 2003, p. xiv.

[49] USITC, "The Impact of Trade Agreements: Effect of the Tokyo Round, U.S.-Israel FTA, U.S.-Canada FTA, NAFTA, and the Uruguay Round on the U.S. Economy," Publication 3621, August 2003.

[50] USITC, "The Impact of the North American Free Trade Agreement on the U.S. Economy and Industries: A Three-Year Review," Publication 3045, June 1997.

[51] Ibid.

[52] Hufbauer and Schott, *NAFTA Revisited,* pp. 20-21.

[53] Ibid., p. 21.

[54] Lorenzo Caliendo and Fernando Parro, *Estimates of the Trade and Welfare Effects of NAFTA,* National Bureau of Economic Research, November 2012, pp. 1-5.

the U.S.-Mexico border region as a production site.[55] U.S. manufacturing industries, including automotive, electronics, appliances, and machinery, all rely on the assistance of Mexican manufacturers. One report estimates that 40% of the content of U.S. imports from Mexico and 25% of the content of U.S. imports from Canada are of U.S. origin. In comparison, U.S. imports from China are said to have only 4% U.S. content. Taken together, goods from Mexico and Canada represent about 75% of all the U.S. domestic content that returns to the United States as imports.[56]

Auto Sector

NAFTA was instrumental in the integration of the North American auto industry, which experienced some of the most significant changes in trade following the agreement. U.S. auto parts producers may use inputs and components produced by another NAFTA partner to assemble parts, which are then shipped to another NAFTA country where they are assembled into a vehicle that is sold in any of the three NAFTA countries.[57] NAFTA provisions consisted of a phased elimination of tariffs and the gradual removal of many non-tariff barriers to trade. It provided for uniform country of origin provisions, enhanced protection of intellectual property rights, adopted less restrictive government procurement practices, and eliminated performance requirements on investors from other NAFTA countries. NAFTA established the removal of Mexico's restrictive trade and investment policies and the elimination of U.S. tariffs on autos and auto parts.

After NAFTA's entry into force, U.S. trade in vehicles and auto parts increased rapidly. Mexico became a more significant trading partner in the U.S. motor vehicle market as U.S. auto exports to Mexico increased 251% while imports increased 679% between 1993 and 2014 (see

[55] Gordon H. Hanson, *North American Economic Integration and Industry Location,* National Bureau of Economic Research, June 1998.

[56] Robert Koopman, William Powers, and Zhi Wang, et al., *Give Credit Where Credit is Due: Tracing Value Added in Global Production Chains*, National Bureau of Economic Research, Working Paper 16426, Cambridge, MA, September 2010, p. 8.

[57] Business Roundtable, *NAFTA: A Decade of Growth,* p. 8.

Table 1). Mexico's share in U.S. total trade in motor vehicles increased during this time period, while the share from Canada and other countries decreased. Mexico was the leading supplier of automotive goods for the United States in 2014, accounting for 30% ($86.5 billion) of total U.S. motor vehicle and auto parts imports. Canada ranked second, accounting for 21% ($58.8 billion) of total U.S. imports in motor vehicles and auto parts in 2014.[58]

[58] Merchandise trade statistics in this paragraph are derived from data from the U.S. International Trade Commission's Interactive Tariff and Trade Data Web, at http://dataweb.usitc.gov.

Table 1. U.S. Trade in Motor Vehicles and Parts: 1993 and 2014

(billions of U.S. dollars)

	1993			2014			% Change 1993-2014	
	Exports	Imports	Total	Exports	Imports	Total	Exports	Imports
Mexico								
Vehicles	0.2	3.7	3.9	4.8	46.4	51.2	2300%	1154%
Parts	7.3	7.4	14.7	21.5	40.1	61.6	195%	442%
Total	7.5	11.1	18.6	26.3	86.5	112.8	251%	679%
Canada								
Vehicles	8.2	26.7	34.9	26.9	44.2	71.1	228%	66%
Parts	18.2	10.3	28.5	26	14.6	40.6	43%	42%
Total	26.4	37.0	63.4	52.9	58.8	111.7	100%	59%
World								
Vehicles	18.9	63.0	81.9	76.8	182.1	258.9	306%	189%
Parts	33.4	38.3	71.7	62.1	109.8	171.9	86%	187%
Total	52.3	101.3	153.6	138.9	291.9	430.8	166%	188%

Source: Compiled by CRS using trade data from the USITC at http://dataweb.usitc.gov. For 2013, "vehicles" consists of items under the North American Industrial Classification System (NAICS) number 3361 and "parts" consists of items under NAIC number 3363.

Note: The NAICS is the standard used by Federal statistical agencies in classifying business establishments for the purpose of collecting, analyzing, and publishing statistical data related to the U.S. business economy.

Effect on Mexico

A number of studies have found that NAFTA has brought economic and social benefits to the Mexican economy as a whole, but that the benefits have not been evenly distributed throughout the country.[59] The agreement also had a positive impact on Mexican productivity. A 2011 World Bank study found that the increase in trade integration after NAFTA had a positive effect on stimulating the productivity of Mexican plants.[60] Most post-NAFTA studies on economic effects have found that the net overall effects on the Mexican economy tended to be positive but modest. While there have been periods of positive and negative economic growth in Mexico after the agreement was implemented, it is difficult to measure precisely how much of these economic changes was attributed to NAFTA. A World Bank study assessing some of the economic impacts from NAFTA on Mexico concluded that NAFTA helped Mexico get closer to the levels of development in the United States and Canada. The study states that NAFTA helped Mexican

[59] See for example, Robert A. Blecker and Gerardo Esquivel, *NAFTA, Trade, and Development,* Center for U.S.-Mexican Studies (San Diego), El Colegio de la Frontera Norte, Woodrow Wilson International Center for Scholars, and El Colegio de Mexico, WP 10-03, 2010; and Daniel Lederman, William F. Maloney, and Luis Servén, *Lessons from NAFTA for Latin America and the Caribbean,* The World Bank, 2005.

[60] Rafael E. de Hoyos and Leonardo Iacovone, *Economic Performance under NAFTA,* The World Bank Development Research Group, May 2011, pp. 25-27.

manufacturers adapt to U.S. technological innovations more quickly; likely had positive impacts on the number and quality of jobs; reduced macroeconomic volatility, or wide variations in the GDP growth rate, in Mexico; increased the levels of synchronicity in business cycles in Mexico, the United States, and Canada; and reinforced the high sensitivity of Mexican economic sectors to economic developments in the United States.[61]

Other studies suggest that NAFTA has been disappointing in that it failed to significantly improve the Mexican economy or lower income disparities between Mexico and its northern neighbors.[62] Some argue that the success of NAFTA in Mexico was probably limited by the fact that NAFTA was not supplemented by complementary policies that could have promoted a deeper regional integration effort. These policies could have included improvements in education, industrial policies, and/or investment in infrastructure.[63]

One of the more controversial aspects of NAFTA is related to the agricultural sector in Mexico and the perception that NAFTA has caused a higher amount of worker displacement in this sector than in other economic sectors. Many critics of NAFTA say that the agreement led to severe job displacement in agriculture, especially in the corn sector. One study estimates these losses to have been over 1 million lost jobs in corn production between 1991 and 2000.[64] However, while some of the changes in the agricultural sector are a direct result of NAFTA as Mexico began to import more lower-priced products from the United States, many of the changes can be attributed to Mexico's unilateral agricultural reform measures in the 1980s and early 1990s. Most domestic reform measures consisted of privatization efforts and resulted in increased competition. Measures included eliminating state enterprises related to agriculture and removing staple price supports and subsidies.[65] These reforms coincided with NAFTA negotiations and continued beyond the implementation of NAFTA in 1994. The unilateral reforms in the agricultural sector make it difficult to separate those effects from the effects of NAFTA.

U.S.-Mexico Trade Market Shares

Mexico relies heavily on the United States as an export market; this reliance has diminished very slightly over the years. The percentage of Mexico's total exports going to the United States decreased from 83% in 1993 to 78% in 2013 (see **Figure 4**). In addition, its share of the U.S. market has lost ground since 2003 when China surpassed Mexico as the second-leading supplier of U.S. imports. The United States is losing market share of Mexico's import market. Between

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[61] Daniel Lederman, William F. Maloney, and Luis Servén, *Lessons from NAFTA for Latin America and the Caribbean,* The World Bank, 2005.

[62] Robert A. Blecker and Gerardo Esquivel, *NAFTA, Trade, and Development,* Center for U.S.-Mexican Studies, the Mexico Institute of the Woodrow Wilson Center, El Colegio de la Frontera Norte, and El Colegio de México, USMEX WP 10-03, 2010.

[63] Ibid., p. 22.

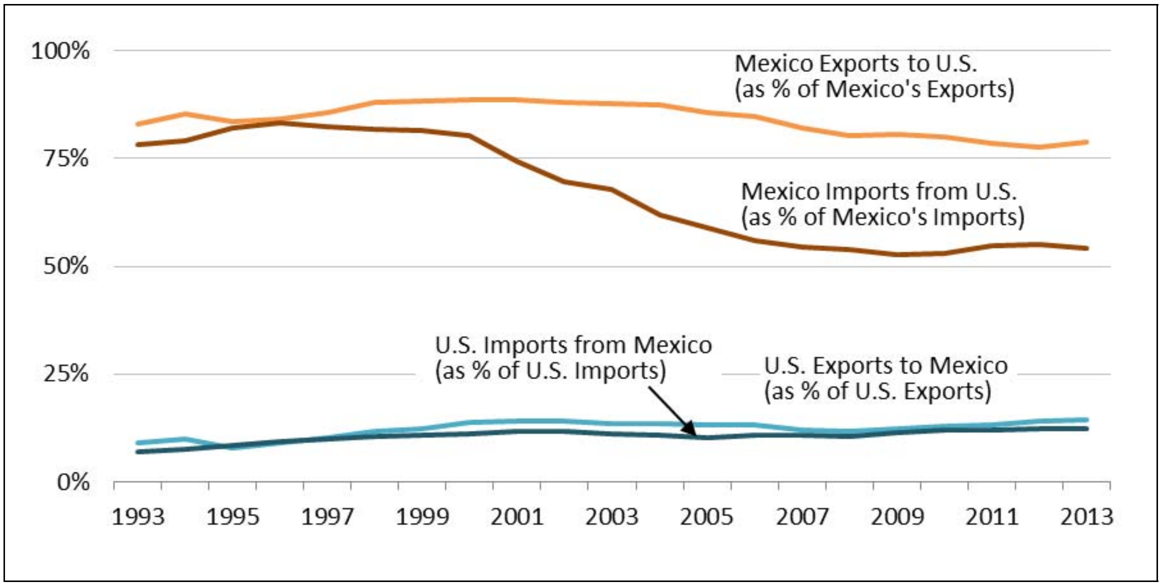
[64] Robert E. Scott, Carlos Salas, Bruce Campbell and Jeff Faux, *Revisiting NAFTA: Still Not Working for North America's Workers,* Economic Policy Institute, Briefing Paper #173, p. 43.

[65] Mexico's unilateral agricultural reform measures removed government subsidies and price controls in the agricultural sector that resulted in rising prices for tortillas. Tortillas are the basic staple for the Mexican diet and a necessity of the poor. For this reason, higher prices had a greater effect on the poor than on middle- and higher-income Mexicans. Mexico also reformed its Agrarian Law. Lands that had been distributed to *ejidos* or community rural groups following the 1910 revolution gained the right to privatize. This led to more efficient production processes, especially in Northern states.

1993 and 2013, the U.S. share of Mexico's imports decreased from 78% to 55%. China is Mexico's second-leading source of imports.

Figure 4. Market Share as Percentage of Total Trade: Mexico and the United States

(1993-2013)



Source: Economist Intelligence Unit, from IMF International Financial Statistics.

Notes: Represents exports to and imports from other country as percentage of country's total trade. Statistics prior to 1993 are not available.

U.S. and Mexican Foreign Direct Investment

Foreign direct investment (FDI) has been an integral part of the economic relationship between the United States and Mexico for many years, especially after NAFTA. Two-way investment increased rapidly after the agreement went into effect. The United States is the largest source of FDI in Mexico. The stock of U.S. FDI in Mexico increased from $15.2 billion in 1993 to $101.0 billion in 2013, a 564% increase (see **Table A-4** in **Appendix A**). The flows of FDI have been affected by other factors over the years, with higher growth during the period of economic expansion during the late 1990s, and slower growth in recent years, possibly due to the economic downturn caused by the 2008 global financial crisis and/or the increased violence in Mexico. Mexican FDI in the United States, while substantially lower than U.S. investment in Mexico, has also increased rapidly, from $1.2 billion in 1993 to $17.6 billion in 2013, an increase of over 1000% (See **Table A-4**).[66]

While Mexico's unilateral trade and investment liberalization measures in the 1980s and early 1990s contributed to the increase of U.S. FDI in Mexico, NAFTA provisions on foreign investment may have helped to lock in Mexico's reforms and increase investor confidence. NAFTA helped give U.S. and Canadian investors nondiscriminatory treatment of their

[66] Foreign direct investment data in this section is derived from data from the Bureau of Economic Analysis online database at http://www.bea.gov.

investments as well as investor protection in Mexico. Nearly half of total FDI investment in Mexico is in the manufacturing industry.

Income Disparity

One of the main arguments in favor of NAFTA at the time it was being proposed by policymakers was that the agreement would improve economic conditions in Mexico and narrow the income disparity between Mexico and the United States and Canada. Studies that have addressed the issue of economic convergence[67] have noted that economic convergence in North America has failed to materialize. One study states that NAFTA failed to fulfill the promise of closing the Mexico-U.S. development gap and that this was partially due to the lack of deeper forms of regional integration or cooperation between Mexico and the United States.[68] The study contends that domestic policies in both countries, along with underlying geographic and demographic realities, contribute to the continuing disparities in income. The authors argue that neither Mexico nor the United States adopted complementary policies after NAFTA that could have promoted a more successful regional integration effort. These policies could include education, industrial policies, and more investment in border and transportation infrastructure. The authors also note that other developments, such as increased security along the U.S.-Mexico border after the September 11 terrorist attacks, have made it much more difficult for the movement of goods and services across the border and for improving regional integration. They argue that the two countries could cooperate on policies that foster convergence and economic development in Mexico instead of increasing security and "building walls."[69]

A World Bank study states that NAFTA brought economic and social benefits to the Mexican economy, but that it is not enough to help narrow the disparities in economic conditions between Mexico and the United States.[70] It contends that Mexico needs to invest more in education, innovation, and infrastructure, and in the quality of national institutions. The study also states that income convergence between a Latin American country and the United States is limited by the wide differences in the quality of domestic institutions, in the innovation dynamics of domestic firms, and in the skills of the labor force. While NAFTA had a positive effect on wages and employment in some Mexican states, the wage differential within the country increased as a result of trade liberalization.[71] Another study also notes that the ability of Mexico to improve economic conditions depends on its capacity to improve its national institutions, adding that Mexican institutions did not improve significantly more than those of other Latin American countries since NAFTA went into effect.[72]

[67] Economic convergence can be broadly defined as a narrowing of the disparities in the economic levels and the manufacturing performances of particular countries or their regions. The goal of the theory of economic convergence is to research and analyze the factors influencing the rates of economic growth and real per capita income in countries.

[68] Robert A. Blecker and Gerardo Esquivel, *NAFTA, Trade, and Development,* Working Paper 10-03, Center for U.S.-Mexican Studies (San Diego), the Mexico Institute of the Woodrow Wilson Center (Washington DC), El Colegio de la Frontera Norte (Tijuana), and El Colegio de México (Mexico City), 2010, p. 2.

[69] Ibid., pp. 19-23.

[70] Lederman, Maloney, and Servén, *Lessons from NAFTA for Latin America and the Caribbean,* The World Bank, 2005.

[71] Ibid.

[72] William Easterly, Norbert Fiess, and Daniel Lederman, "NAFTA and Convergence in North America: High Expectations, Big Events, Little Time," *Economía,* Fall 2003.

Effect on Canada

As noted earlier, the U.S.-Canada FTA came into effect on January 1, 1989. Thus, trade liberalization between the two countries was well underway—or already completed—by the time of the implementation of NAFTA. This section summarizes the effect of trade liberalization from both agreements on Canada.

From the Canadian perspective, the important consequence of the FTA may have been what did not happen, that is, that many of the fears of opening up trade with the United States did not come to pass. Canada did not become an economic appendage or "51st state" as many had feared. It did not lose control over its water or energy resources; its manufacturing sector was not gutted. Rather, as one Canadian commentator remarked, "free trade helped Canada to grow up, to turn its face out to the world, to embrace its future as a trading nation, [and] to get over its chronic sense of inferiority."[73] However, some hopes for the FTA, for example, that it would be a catalyst for greater productivity in Canadian industry, also have not come to pass.

U.S.-Canada Trade Market Shares

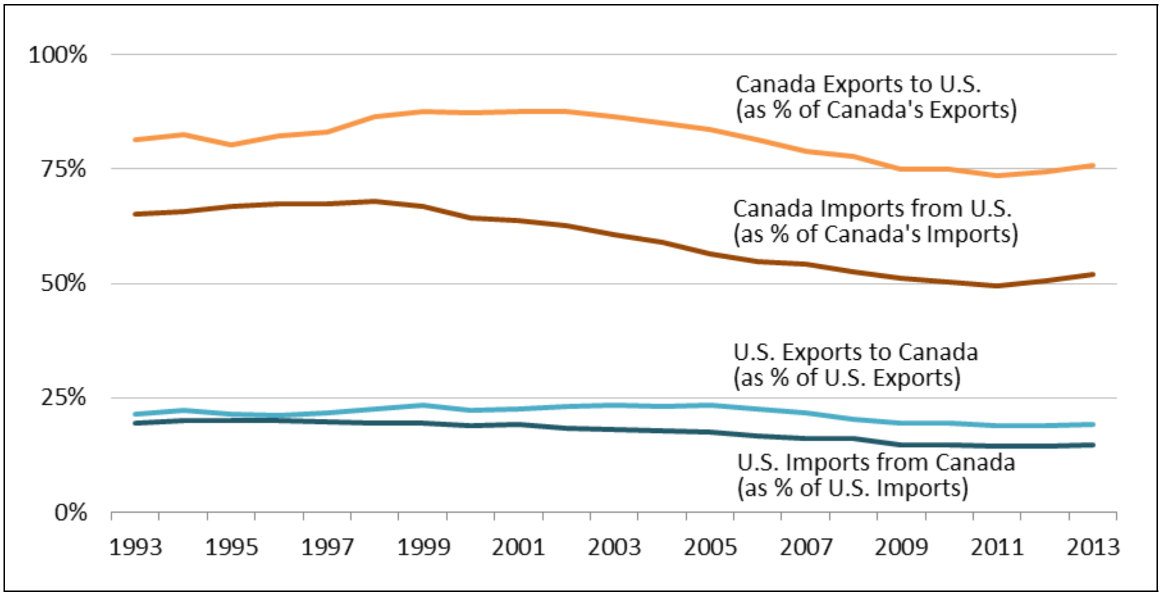
The United States is the number one purchaser of Canadian goods and supplier of imports to Canada. Canada's share of its exports going to the United States steadily increased during the 1980s, from 60.6% in 1980 to 70.7% in 1989, the first year of the FTA. Canada's percentage of total exports to the United States continued to increase, reaching 87.7% in 2002. The relative importance of the value of U.S. and Canadian trade with each other, however, has been falling in recent years. Since 2002, this percentage has fallen back to 75.8% in 2013. The U.S. share of Canada's total imports, which reached a peak of 70.0% in 1983, topped out at 68.7% during the free trade era and has been steadily dropping ever since to a low of 52.1% in 2013 (see **Figure 5**).

Traditionally, Canada was the largest purchaser of U.S. exports and supplier of U.S. imports; however, shares of both peaked before the free trade era. Canada purchased 23.5% of U.S. exports in 1987 and equaled that figure in 2005, but it has since fallen off to 18.9% in 2012. Canada traditionally was the largest supplier of U.S. imports, peaking at 20.6% in 1984, reaching a NAFTA high of 20.1% in 1996, but has declined thereafter to 14.6% in 2013. China displaced Canada as the largest supplier of U.S. imports in 2007.

[73] John Ibbitson, "After 25 Years, Free-Trade Deal with U.S. Has Helped Canada Grow Up," *The Globe and Mail*, September 29, 2012.

Figure 5. Market Share as Percentage of Total Trade: Canada and the United States

(1993-2013)



Source: Economic Intelligence Unit, from IMF International Financial Statistics.

Note: Represents exports to and imports from other country as percentage of country's total trade.

The composition of trade has also changed. Canada initially entered a manufacturing recession after the conclusion of the FTA as branch plants of U.S. companies set up behind the Canadian tariff wall were abandoned. However, more internationally competitive manufacturing sectors thrived as long as the Canadian dollar (nicknamed the loonie for the soaring loon pictured on its reverse) was relatively cheap. From a low point of a Canadian dollar worth US$0.65 in 2002, the loonie reached parity in 2007, and has hovered around the parity point until 2013 before sliding to a recent US$0.92. The appreciation has been attributed to the boom in Canada's natural resources—oil and gas displaced motor vehicles as Canada's largest export to the United States in 2005. The "great recession" and the woes of the integrated North American auto sector also took a toll on Canadian manufacturing.

For some advocates in Canada, free trade was meant to alleviate the long-term labor productivity gap between the United States and Canada. Open competition was seen as forcing Canadian industry to be more productive. In much of the free trade era, this gap could be accounted for by the low value of the Canadian dollar. As adding capital equipment (often purchased from the United States) was relatively more expensive than hiring extra workers, the latter was often employed. The appreciation of the Canadian dollar has made additional capitalization more attractive, but labor productivity recently remained only at 72% of U.S. levels.[74] The relatively low productivity levels of Canadian industry, as well as its relatively low investments in research and development (R&D), and relatively lower expenditures on information technology, are seen as threatening to Canadian long-term competitiveness, and remain of concern to Canadian

[74] Kevin Lynch, "Canada's Challenge—From Good to Great," *Inside Policy,* October 2012.

policymakers, despite leading the organization of Economic Cooperation and Development's ranking of the population with post-secondary education.[75]

U.S. and Canadian Foreign Direct Investment

Two-way investment has also increased markedly during the free trade era, both in terms of stock and flow of investment. The United States is the largest single investor in Canada with a stock of FDI into Canada reaching $368.3 billion in 2013, up from a stock of $69.9 billion in 1993 (see **Table A-4**). U.S. investment represents nearly 51.5% of the total stock of FDI in Canada from global investors. U.S. FDI flows into Canada averaged $3.28 billion in the five years prior to the FTA, and actually fell to an average of $1.7 billion in the first six years of the FTA, mainly attributed to divestments of U.S.-owned branch plants in Canada. However, U.S. flows into Canada increased markedly to an average of $14.9 billion during the years 1995 to 2012.[76] The stock of U.S. FDI is now equivalent to 18% of the value of Canadian GDP, in contrast to 1% at the beginning of the FTA.

While Canada is not the largest investor in the United States, the United States was the largest destination for Canadian FDI in 2013 with a stock of $237.9 billion, an increase from $26.6 billion in 1988.[77] Approximately 40.7% of Canadian FDI was invested in the United States in 2012. Canadian FDI flows into the United States annually averaged $2.3 billion in five years prior to the FTA, and an annual average of $1.8 billion during the FTA years, but increased to an annual average of $9.9 billion from 1995 to 2012.[78] These trends highlight the changing view of FDI among Canadians, from one that could be considered fearful or hostile to FDI as vehicles of foreign control over the Canadian economy, to one that is more welcoming of new jobs and techniques that result from FDI.

Issues for Congress

Many economists and business representatives generally look at NAFTA as a success and credit it for fueling unprecedented North American trade and creating job growth in the United States. They look to build on NAFTA's momentum to improve trade relations and economic integration within the region. However, labor groups and some consumer-advocacy groups argue that the agreement has had negative effects. They maintain that the agreement resulted in outsourcing and lower wages that have had a negative effect on the U.S. economy and that it has caused job dislocations in Mexico, especially in agriculture.

Given the increasing number of regional trade agreements throughout the world and the ongoing Trans-Pacific Partnership (TPP) free trade negotiations, one general question that policymakers may consider in forming future trade policy is whether or not NAFTA has lost its relevance. The numerous FTAs that the United States, Mexico, and Canada have put into effect have given other

[75] Glen Hodgson, "Canada U.S. Competitiveness, Addressing the Canadian Economic Contradiction," Woodrow Wilson Center, Canada Institute, June 2007; Lynch, *ibid.*

[76] Investment statistics are from the U.S. Department of Commerce, Bureau of Economic Analysis, and Statistics Canada.

[77] Ibid.

[78] Douglas Porter, "Free Trade at 25: How the FTA Positioned Canada for the 21st Century," *Inside Policy,* October 2012.

countries the same preferences to the U.S. market that Canada and Mexico benefit from under NAFTA. Similarly, these FTAs have lessened the preferences the United States has in other markets.

Both proponents and critics of NAFTA agree that the three countries should look at what the agreement has failed to do as they look to the future of North American trade and economic relations. Policies could include strengthening institutions to protect the environment and worker rights; considering the establishment of a border infrastructure plan; increasing regulatory cooperation; promoting research and development to enhance the global competiveness of North American industries; investing in more border infrastructure to make border crossings more efficient; and/or creating more efforts to lessen income differentials within the region.

Trans-Pacific Partnership (TPP)

In December 2012, Canada and Mexico began participating in the ongoing negotiations for a proposed TPP free trade agreement (FTA) among 12 countries in the Asia-Pacific region.[79] The United States is an active participant in the negotiations and was among the first tranche of countries to join the original four members of the Trans-Pacific Strategic Economic Partnership (Brunei, Chile, New Zealand, and Singapore) to launch the TPP negotiations in the fall of 2008. With 26 negotiating groups and 29 chapters under discussion, the TPP partners envision the agreement to be "comprehensive and high-standard," in that they seek to eliminate tariffs and non-tariff barriers to trade in goods, services, and agriculture, and to establish rules on a wide range of issues, including intellectual property rights, foreign direct investment, and other economic activities. They also strive to create a "21st century agreement" that addresses new and cross-cutting issues presented by an increasingly globalized economy.

The United States has indicated that it is only negotiating bilateral market access in the TPP talks with countries with which it does not have FTAs—Brunei, Japan, Malaysia, New Zealand, and Vietnam. The addition of Japan to the negotiations in the summer of 2013 may afford all three NAFTA countries with the possibility of additional market opening opportunities. However, the United States has sought to go beyond current U.S. FTAs in its proposed rules chapters. This has become a point of contention in the talks and may become an issue for Canada and Mexico as well. The TPP may have implications for NAFTA in several areas, including intellectual property rights (IPR), investment, services, and government procurement, as well as labor and environmental provisions. The related provisions in more recent free trade agreements that the United States has negotiated, such as those with Colombia, Panama, Peru, and South Korea, include commitments that go beyond NAFTA. If agreement is reached on a TPP, Canada and Mexico may have to adhere to stronger and more enforceable labor and environmental provisions, stronger IPR provisions, and some issues that were not addressed in detail in the NAFTA, such as disciplines on state-owned enterprises.

[79] The 12 countries involved in the Trans-Pacific Partnership (TPP) negotiations include the United States, Australia, Brunei, Canada, Chile, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore, and Vietnam. For more information on the TPP, see CRS Report R42694, *The Trans-Pacific Partnership (TPP) Negotiations and Issues for Congress*, coordinated by (name redacted).

Regulatory Cooperation

Policymakers may consider issues on how the United States can improve cooperation with its North American neighbors in the areas of trade, transportation, competitiveness, economic growth, and security enhancement. The United States, Canada, and Mexico have made efforts since 2005 to increase cooperation on these issues through various endeavors, most notably by participating in trilateral summits known as the North American Leaders Summits. The most recent Summit took place on February 19, 2014, in Toluca, Mexico. President Barack Obama met with Mexican President Enrique Peña Nieto and Canadian Prime Minister Stephen Harper to discuss the economic well-being of the region; education initiatives; energy and climate change; citizen security; and regional and global outreach.[80] Canada postponed the 2015 Summit that had been planned for January 2015, stating that it would take place sometime in the fall.

After the first North American Leaders' Summit on March 23, 2005, in Waco, TX, the three countries agreed on enhancing regulatory cooperation through the former initiative known as the Security and Prosperity Partnership of North America (SPP). The main goal was to increase and enhance prosperity in the United States, Canada, and Mexico through regulatory cooperation.[81] The Obama Administration has affirmed its commitment to continue past efforts on North American cooperation but under a different approach from the SPP initiative. While these efforts have served as mechanisms to increase communications on issues of mutual interest, their role has been limited because there are no binding agreements.

The former SPP initiative evolved to other efforts pursued by the Obama Administration for regulatory cooperation, which have included separate bilateral endeavors. For example, in May 2010, the United States and Mexico released the Declaration Concerning Twenty-first Century Border Management and, in December 2011, the United States and Canada announced the Beyond the Border Action Plan: A Shared Vision for Perimeter Security and Economic Competiveness. In February 2012, the United States and Mexico announced the High-Level Regulatory Cooperation Council (HLRCC) to help align regulatory principles, an effort similar to the U.S.-Canada Regulatory Cooperation Council. In March 2012, the Defense Ministers of the three countries met in Ottawa, Canada, for the first ever "Trilateral Meetings of North American Defense Ministers" to increase cooperation on national security issues.

Some critics of North American trilateral cooperation contend that the efforts are an attempt to create a common market or economic union in North America. Others contend that past efforts under the SPP were contributing to the creation of a so-called "NAFTA Superhighway" that would link the United States, Canada, and Mexico with a "super-corridor."[82] Proponents of North American competitiveness and security cooperation view the initiatives as constructive to addressing issues of mutual interest and benefit for all three countries. Business groups generally support increased North American cooperation and believe that it is necessary to enhance the competitiveness of U.S. businesses in the global market.

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[80] The White House, Office of the Press Secretary, *Fact Sheet: Key Deliverables for the 2014 North American Leaders Summit,* February 19, 2014.

[81] The SPP was endorsed by all three countries, but it was not a signed agreement or treaty and contained no legally binding commitments or obligations. Although the SPP built upon the existing trade and economic relationship of the three countries, it was distinct and separate from NAFTA.

[82] See for example, *Society for American Sovereignty*, at http://www.americansov.org.

Proposals for Deeper Regional Integration

The rising number of regional trade agreements throughout the world, in addition to the rising presence of China in Latin America, could have implications for U.S. trade policy with its NAFTA partners beyond the proposed TPP. Some trade policy experts contend that a deepening of economic relations with Canada and Mexico will help promote a common trade agenda with shared values. In addition to economic effects, forming deeper trade and investment ties would have positive implications for corporate governance, labor rights, environmental protection, and democratic governance.[83]

Some policy experts emphasize the importance of North American trade in intermediate goods and supply chains. They argue that the governments of the three countries should improve cooperation in this area and invest more in improving border infrastructure. The increased security measures that began after September 11, 2001, have resulted in a disruption in production chains due to extended and unpredictable wait times along the border. This has disproportionately hurt small and medium sized businesses.[84] The United States and Mexico have recognized the need to enhance cooperation on prioritizing the economic relationship and security and have developed the Twenty-First Century Border Initiative for this purpose.[85] While the initiative has resulted in improvements along the border, some observers contend that policymakers could devote more energy to improving cooperation and enhancing efficiency in cross-border trade.

Other experts have proposed ideas to address ongoing problems in the region and make North American industries more competitive. Some proposals that have emerged include calls for rethinking the current trade relationship under NAFTA by broadening the scope of North American integration and cooperation. One idea, for example, is to develop a North American Investment Fund to help close the income gap between Mexico and its northern neighbors. The proposed fund would be administered by the World Bank and used to fund infrastructure projects to connect the south of Mexico to the United States and Canada, and also to improve post-secondary education in Mexico.[86] Other ideas are to set up a Customs Union in North America, such as that of the European Union, with a common external tariff to facilitate trade and deepen North American integration; develop a cooperative approach on immigration; and promote regulatory convergence.[87] The proponents of these ideas admit that it would be very difficult for Congress to approve these proposals in the near future, but argue that it is important to think about such options based on the increasing interdependence among NAFTA partners and common interests concerning the future of the region.

[83] Testimony of Eric Farnsworth, Vice President, Council of the Americas, in U.S. Congress, Senate Committee on Foreign Relations, *Doing Business in Latin America: Positive Trends but Serious Challenges*, 112th Cong., 2nd sess., July 31, 2012, S.Hrg. 112-607 (Washington, DC: GPO, 2012), pp. 30-32.

[84] Christopher E. Wilson, *Working Together: Economic Ties Between the United States and Mexico,* Woodrow Wilson International Center for Scholars, November 2011, pp. 37-38.

[85] For more information, see CRS Report R41349, *U.S.-Mexican Security Cooperation: The Mérida Initiative and Beyond*, by (name redacted) and (name redacted).

[86] Robert A. Pastor, *The North American Idea: A Vision of a Continental Future,* Oxford University Press, 2011, pp. 169-172.

[87] Ibid., pp. 167-200.

Appendix A. U.S. Merchandise Trade with NAFTA Partners

Table A-1. U.S. Merchandise Trade with NAFTA Partners

(billions of nominal U.S. dollars)

	Canada			Mexico			Total NAFTA		
Year	Exports	Imports	Trade Balance	Exports	Imports	Trade Balance	Exports	Imports	Trade Balance
1993	100.2	110.9	-10.7	41.6	39.9	1.7	141.8	150.8	-9.0
1994	114.3	128.9	-14.6	50.8	49.5	1.3	165.1	178.4	-13.3
1995	126.0	145.1	-19.1	46.3	61.7	-15.4	172.3	206.8	-34.5
1996	132.6	156.5	-23.9	56.8	73.0	-16.2	189.4	229.5	-40.1
1997	150.1	168.1	-18	71.4	85.9	-14.5	221.5	254.0	-32.5
1998	154.2	174.8	-20.6	79.0	94.7	-15.7	233.2	269.5	-36.3
1999	163.9	198.3	-34.4	87.0	109.7	-22.7	250.9	308.0	-57.1
2000	176.4	229.2	-52.8	111.7	135.9	-24.2	288.1	365.1	-77.0
2001	163.7	217.0	-53.3	101.5	131.4	-29.9	265.2	348.4	-83.2
2002	160.8	210.6	-49.8	97.5	134.7	-37.2	258.3	345.3	-87.0
2003	169.5	224.2	-54.7	97.5	138.1	-40.6	267.0	362.3	-95.3
2004	187.7	255.9	-68.2	110.8	155.8	-45	298.5	411.7	-113.2
2005	211.4	287.9	-76.5	120.0	170.2	-50.2	331.4	458.1	-126.7
2006	230.3	303.4	-73.1	134.2	198.3	-64.1	364.5	501.7	-137.2
2007	248.4	313.1	-64.7	136.5	210.8	-74.3	384.9	523.9	-139.0
2008	260.9	335.6	-74.7	151.5	215.9	-64.4	412.4	551.5	-139.1
2009	204.7	224.9	-20.2	129.0	176.5	-47.5	333.7	401.4	-67.7
2010	248.2	276.5	-28.3	164.3	229.7	-65.4	412.5	506.2	-93.7
2011	280.8	316.5	-35.7	197.5	263.1	-65.6	478.3	579.6	-101.3
2012	291.8	324.2	-32.4	216.3	277.7	-61.4	508.1	601.9	-93.8
2013	300.2	332.1	-31.9	226.2	280.5	-54.3	526.4	612.5	-86.1
2014	312.13	346.1	-33.94	240.3	294.2	-53.8	552.5	640.2	-87.8

Source: Compiled by CRS using trade data from the U.S. International Trade Commission's Interactive Tariff and Trade Data Web, at http://dataweb.usitc.gov.

Table A-2. U.S. Private Services Trade with NAFTA Partners

(billions of nominal U.S. dollars)

	Canada			Mexico			Total NAFTA		
Year	Exports	Imports	Services Trade Balance	Exports	Imports	Services Trade Balance	Exports	Imports	Services Trade Balance
1993	17.0	9.1	7.9	10.4	7.4	3.0	27.4	16.5	10.9
1994	17.2	9.9	7.3	11.3	7.9	3.4	28.5	17.8	10.7
1995	17.9	11.0	6.9	8.7	7.9	0.8	26.6	18.9	7.7
1996	19.5	12.4	7.1	9.4	8.9	0.5	28.9	21.3	7.6
1997	20.5	13.7	6.8	10.8	9.9	0.9	31.3	23.6	7.7
1998	19.4	15.0	4.4	11.7	9.8	1.9	31.1	24.8	6.3
1999	22.9	16.6	6.3	14.2	9.7	4.5	37.1	26.3	10.8
2000	24.8	18.2	6.6	15.8	11.2	4.6	40.6	29.4	11.2
2001	24.7	17.8	6.9	16.7	10.9	5.8	41.4	28.7	12.7
2002	25.2	18.4	6.8	17.9	12.3	5.6	43.1	30.7	12.4
2003	27.6	20.0	7.6	18.5	12.5	6.0	46.1	32.5	13.6
2004	29.5	21.2	8.3	19.5	13.9	5.6	49.0	35.1	13.9
2005	32.8	22.6	10.2	22.5	14.4	8.1	55.3	37.0	18.3
2006	37.9	23.9	14.0	23.8	14.9	8.9	61.7	38.8	22.9
2007	42.7	25.7	17.0	25.0	15.3	9.7	67.7	41.0	26.7
2008	45.4	26.0	19.4	26.2	15.9	10.3	71.6	41.9	29.7
2009	43.5	23.7	19.8	22.9	14.0	8.9	66.4	37.7	28.7
2010	53.1	27.4	25.7	24.6	14.0	10.6	77.7	41.4	36.3
2011	58.3	30.5	27.8	26.4	14.7	11.7	84.7	45.2	39.5
2012	61.5	30.8	30.7	28.2	15.5	12.7	89.7	46.3	43.4
2013	63.3	30.5	32.8	29.9	17.8	12.1	93.2	48.3	44.9

Source: Compiled by CRS using data from the Bureau of Economic Analysis online database at http://www.bea.gov.

Table A-3. U.S. Trade with NAFTA Partners by Major Product Category: 2014

(billions of nominal U.S. dollars)

NAFTA Partner	U.S. Exports: Leading Items (NAIC 4-digit level)	U.S. Exports: Value	U.S. Imports: Leading Items (NAIC 4-digit level)	U.S. Imports: Value
Canada	Motor vehicles	26.9	Oil and gas	96.1
	Motor vehicle parts	26.0	Motor vehicles	44.2
	Oil and gas	16.8	Petroleum and coal products	15.8
	Petroleum and coal products	15.1	Motor vehicle parts	14.6
	Agriculture and construction machinery	11.2	Nonferrous metal and processing	10.5
	All Other	216.1	All Other	164.9
	Total exports to Canada	312.1	Total imports from Canada	346.1
Mexico	Motor vehicle parts	21.5	Motor vehicles	46.4
	Petroleum and coal products	19.1	Motor vehicle parts	40.1
	Computer equipment	16.0	Oil and gas	27.8
	Semiconductors and other electronic components	13.5	Computer equipment	14.3
	Basic chemicals	10.1	Audio and video equipment	14.2
	All other	160.1	All other	151.4
	Total Exports to Mexico	240.3	Total Imports from Mexico	294.2

Source: Compiled by CRS using trade data from the U.S. International Trade Commission's Interactive Tariff and Trade Data Web, at http://dataweb.usitc.gov.

Notes: The North American Industrial Classification System (NAICS) is the standard used by federal statistical agencies in classifying business establishments for the purpose of collecting, analyzing, and publishing statistical data related to the U.S. business economy.

Table A-4. U.S. Foreign Direct Investment Positions with Canada and Mexico

(1993-2012 historical cost basis [millions of U.S. dollars])

Year	Canadian FDI in the U.S.	U.S. FDI in Canada	Mexican FDI in the U.S.	U.S. FDI in Mexico
1993	40,373	69,922	1,244	15,221
1994	41,219	74,221	2,069	16,968
1995	45,618	83,498	1,850	16,873
1996	54,836	89,592	1,641	19,351
1997	65,175	96,626	3,100	24,050
1998	72,696	98,200	2,055	26,657
1999	90,559	119,590	1,999	37,151
2000	114,309	132,472	7,462	39,352
2001	92,420	152,601	6,645	52,544
2002	92,529	166,473	7,829	56,303
2003	95,707	187,953	9,022	56,851
2004	125,276	214,931	7,592	63,384
2005	165,667	231,836	3,595	73,687
2006	165,281	205,134	5,310	82,965
2007	201,924	250,642	8,478	91,046
2008	168,746	246,483	8,420	87,443
2009	188,943	274,807	11,111	84,047
2010	192,463	295,206	10,970	85,751
2011	205,225	330,041	12,500	85,599
2012	217,800	346,080	14,458	98,377
2013	237,921	368,297	17,610	101,454

Source: Compiled by CRS using data from the Bureau of Economic Analysis online database at http://www.bea.gov.

Appendix B. Mexico's Protectionist Trade Policies Prior to NAFTA

Summary of Mexico's Protectionist Policies Prior to NAFTA

For decades prior to NAFTA Mexico relied on import substitution policies, restrictions on foreign investment, and a controlled exchange rate to help foster domestic growth and to protect itself from a perceived risk of foreign domination.

State-Owned Enterprises (SOEs). Mexico had a strong state presence prior to NAFTA. During the late 1950s and 1960s, the number of state-owned enterprises in Mexico almost doubled from 144 to 272. By 1982, the number of SOES had increased to 1,155. Mexico's economic reforms and divestiture of the state owned sector that occurred during the period of 1983 to 1993 decreased the number of SOEs to 258. By the end of 2003, the number of SOEs dropped to 210.

Import Licenses. Mexico had import license requirements on most, if not all, Mexican imports. The government began to phase these out in the mid-1980s. By the time NAFTA negotiations started, import licenses were required on only 230 products of the nearly 12,000 items in the Mexican tariff schedule. In agricultural goods, 60% of U.S. exports to Mexico required import licenses or faced other nontariff barriers. There was also a lack of transparency of procedures through which exporters to Mexico could apply for the proper license, certificate, or test.

Foreign Investment Restrictions. Mexico's restrictive Law to Promote Mexican Investment and Regulate Foreign Investment was in effect at the time of NAFTA negotiations, though Mexico had started liberalizing some restrictions in the mid-1980s. In 1991, 37% of Mexican economic activity was not open to 100% foreign investment ownership.

Auto Industry Import Substitution Policy (Auto Decrees). Mexico had a restrictive import substitution policy that began in the 1960s through a series of Mexican Auto Decrees in which the government sought to supply the entire Mexican market through domestically produced automotive goods. The decrees established import tariffs as high as 25% on automotive goods and had high restrictions on foreign auto production in Mexico. The decrees prohibited imports of finished vehicles; imposed high domestic-content requirements on foreign manufacturers producing cars in Mexico; issued export requirements in which a certain amount of exports was required for every dollar of imports. The government issued the final decree in 1989, after joining the GATT, liberalizing rules on the industry but not entirely eliminating them. Auto manufacturers were still required to have a certain percentage of domestic content in their products and meet export requirements, both of which were considered huge impediments to the industry. Even after joining the GATT, Mexico had tariffs of 20% or more on imports of automobiles and auto parts.

Restrictions in Agriculture. In the period after the 1910 revolution and until the 1980s, Mexico had a land distribution system in which land was redistributed from wealthy land owners and managed by the government. This *ejido* system, formed under Mexico's Agrarian Law, changed in the 1980s when the government began to implement agricultural and trade policy reform measures. Changes included the privatization of the *ejido* system in order to stimulate competition. Mexico's unilateral reform measures included eliminating state enterprises related to agriculture and removing staple price supports and subsidies. Mexico also had a government agency known as CONASUPO which intervened in the agriculture sector. The agency bought staples from farmers at guaranteed prices and processed the products or sold them at low prices to processors and consumers. Many of Mexico's domestic reforms in agriculture coincided with NAFTA negotiations, beginning in 1991, and continued beyond the implementation of NAFTA in 1994. The unilateral reforms in the agricultural sector make it difficult to separate those effects from the effects of NAFTA. By 1999, CONASUPO had been abolished.

Sources: United States International Trade Commission (USITC), *The Likely Impact on the United States of a Free Trade Agreement with Mexico,* Publication 2353, February 1991.Gary Clyde Hufbauer and Jeffrey J. Schott, Institute for International Economics, *NAFTA Revisited,* October 2005. Alberto Chong and Florencio López-de-Silanes, *Privatization in Mexico,* Inter-American Development Bank, Working Paper #513, August 2004.

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