

# NAFTA AT YEAR TWELVE

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HEARING  
BEFORE THE  
SUBCOMMITTEE ON INTERNATIONAL TRADE  
OF THE  
COMMITTEE ON FINANCE  
UNITED STATES SENATE  
ONE HUNDRED NINTH CONGRESS  
SECOND SESSION  
—  
SEPTEMBER 11, 2006  
—



Printed for the use of the Committee on Finance

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U.S. GOVERNMENT PRINTING OFFICE

38-636—PDF

WASHINGTON : 2006

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## NAFTA AT YEAR TWELVE

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MONDAY, SEPTEMBER 11, 2006

U.S. SENATE,  
SUBCOMMITTEE ON INTERNATIONAL TRADE,  
COMMITTEE ON FINANCE,  
*Washington, DC.*

The hearing was convened, pursuant to notice, at 2 p.m., in room SD-215, Dirksen Senate Office Building, Hon. Craig Thomas (chairman of the subcommittee) presiding.

Present: Senator Bingaman.

### **OPENING STATEMENT OF HON. CRAIG THOMAS, A U.S. SENATOR FROM WYOMING, CHAIRMAN, SUBCOMMITTEE ON INTERNATIONAL TRADE, COMMITTEE ON FINANCE**

Senator THOMAS. Good afternoon, everyone. I think we will begin. It is a little quiet around here today, but when there are no votes, why, people do not show up very much.

In any event, we are very glad to have this hearing. The hearing is intended to provide an update from USTR on NAFTA, as well as an update on the review that is going on. Customs officials will testify on a variety of border issues that have arisen during the agreement and how the trade between the countries has impacted the global war on terror.

Finally, a panel of witnesses that includes economists, agricultural representatives, and businessmen who have investments along the U.S.-Mexican border has been invited to share their thoughts.

As you all know, in 1993 President Clinton submitted to Congress the most comprehensive trade agreement ever negotiated. Upon the implementation of the North American Free Trade Agreement, it created the largest trading bloc in the world.

Today, the member nations of NAFTA have a population that exceeds 430 million and combined domestic production of nearly \$13 trillion. Canada and Mexico represent the largest export markets for U.S. goods.

Not surprisingly, the same holds true for my home State of Wyoming. Since implementation of NAFTA, exports from our State have tripled, from just under \$49 million to over \$161 million. Exports to Mexico have had similar growth, at slightly more than \$71 million.

Despite the impressive growth, the debate on what impact NAFTA has had on our economy exists. It is estimated that 25 percent of U.S. economic growth in the 1990s was directly related to exports.

Even with substantial growth in U.S. exports in the past, America continues, of course, to have a negative trade balance. The reasons for the negative balance are many, but the bottom line is, we continue to import more than we export.

Today we will hear from a diverse group of witnesses who will share their thoughts of what the impact of NAFTA has been. We will hear from the Customs Service how NAFTA has impacted the operations on the border. We will hear from the private sector on how NAFTA has impacted their operations and what needs to be addressed to make the agreement better and to boost benefits today and in the future.

The world has changed, of course, in the 12 years since NAFTA took effect. Innovation of technology has made the world smaller, political changes have improved and continue to impact the dynamics, and the awakening of China has forever changed the global landscape as well. A good trade agreement is one that is not only fair and provides benefits to certain parties, but also gives flexibility. So we appreciate you being here.

Obviously today is a difficult day for many people. There is no event in recent years that has had a more profound impact than the events of September 11, 2001. Today represents that anniversary, and certainly it has changed our Nation forever. It is important to remember those who were killed and those who still bear the scars of this day. I hope we will keep them in our thoughts as we go forward.

Let me turn to Senator Bingaman.

**OPENING STATEMENT OF HON. JEFF BINGAMAN,  
A U.S. SENATOR FROM NEW MEXICO**

Senator BINGAMAN. Thank you very much, Mr. Chairman. Thanks for having the hearing. As you point out, it is a day of commemoration and remembrance for the whole country, and I do think it is important that we continue to try to do constructive work here in the Congress. I commend you for having the hearing.

Let me just say that the issue of NAFTA and the larger issue of trade relations and globalization is one that I think is extremely important for our economic future and one that we need to understand better here in the Congress. I think this hearing is a good start in trying to help me to understand the issue better, and I appreciate your willingness to do it.

As you know, I had asked that, in addition to the seven witnesses that you have today, that we also hear from the policy director for the AFL-CIO, Ms. Thea Lee, and that was not the decision. But I hope if we are able to have another hearing, as I hope we will, I hope that she will be called as a witness.

I would, as part of today's record, ask that we include the written statement that she submitted to us, if we could do that.

Senator THOMAS. Without objection.

[The prepared statement of Ms. Lee appears in the appendix.]

Senator BINGAMAN. Thank you, Mr. Chairman. I appreciate that. I will have questions for all the witnesses as we get into the testimony. I very much appreciate them coming and giving us their insights as to the impact of NAFTA.

I have long thought that, with regard to trade agreements, we have much more interest in the administration and in the Congress in getting new agreements signed than we do in reviewing our experience under the previous agreements that have been implemented. This is a welcome change in that approach and one that I think we should do more of, and I look forward to this testimony. Thank you very much.

Senator THOMAS. Thank you, Senator.

Now if we could have our first panel, please: Mr. John Melle, Deputy Assistant U.S. Trade Representative for North America, Office of the U.S. Trade Representative in Washington; and Ms. Cathy Saucedo, Director, Special Enforcement, U.S. Customs and Border Protection, Washington, DC. Thank you for being here.

Mr. Melle, if you would like to begin.

**STATEMENT OF JOHN MELLE, DEPUTY ASSISTANT U.S. TRADE REPRESENTATIVE FOR NORTH AMERICA, OFFICE OF THE U.S. TRADE REPRESENTATIVE, WASHINGTON, DC**

Mr. MELLE. Thank you, Mr. Chairman and members of the committee, Senator Bingaman. I have submitted written remarks that I would like to be issued for the record, and will summarize those remarks here.

Senator THOMAS. It will be put in the record.

[The prepared statement of Mr. Melle appears in the appendix.]

Mr. MELLE. Thank you for the opportunity to appear before you today. I am pleased to represent USTR and to provide an overview of NAFTA 12 years after its implementation.

The North American Free Trade Agreement has defined our commercial relationships with Canada and Mexico since 1994. To evaluate this experience, the appropriate place to begin is with trade and investment itself. Total goods trade with Canada and Mexico has more than doubled from pre-NAFTA levels and has grown significantly faster than trade with the rest of the world.

Many of the most impressive NAFTA successes are in agriculture. Canada and Mexico are our top two agricultural markets and continue to grow significantly. Many people are not aware that Mexico is our largest market for a wide range of key farm products, including beef, dairy, swine, rice, and apples. U.S. exports of services to Canada and Mexico have also increased 75 percent since 1993.

On investment, the NAFTA partners are investing more in each others' economies, while the rest of the world is investing more in our economies in North America. This change has been especially important for Mexico. Since 1994, annual Foreign Direct Investment inflows have averaged \$14 billion, compared with less than \$3 billion in the 1980s. Mexico's outward FDI has also increased by about 14-fold since 1990.

Notably, this growth in Canada and Mexico has not come at the expense of U.S. inward investment. Even excluding housing, U.S. business investment has risen by 104 percent since 1993.

How much change has been caused because of NAFTA cannot be measured precisely; however, there are many economic indicators that have grown more rapidly since the agreement was implemented.

For example, U.S. employment has increased by 22.2 million jobs since NAFTA. The average post-NAFTA unemployment rate was 5.1 percent, compared to 7.1 percent during the prior 12 years.

U.S. industrial production rose by 49 percent since NAFTA; for the 12 years before NAFTA the increase was 28 percent. Average U.S. real manufacturing compensation has grown 2.3 percent annually since NAFTA, compared to just 0.4 percent between 1987 and 1993.

In Mexico, we have seen consistent GDP growth since NAFTA, 40 percent overall, and annual real wage increases since 1995. Real GDP in Canada has grown by nearly 50 percent, and Canadian unemployment fell from 11.2 percent in 1993 to 6.7 percent last year.

Turning to some recent successes, let me note some events that have allowed us to resolve trade issues with Canada and Mexico this year. In March, the United States and Mexico signed an agreement to promote bilateral trade in cement, which had been the subject of a great deal of litigation. Similarly, in July the United States and Canada reached a final agreement on resolving our softwood lumber dispute, which has continued for more than 20 years.

Also, in late July the United States and Mexico reached agreement on trade in sweeteners, which puts the two countries on a glide path towards full implementation of NAFTA's sweetener provisions in 2008. Today, this morning, Mexico announced that it is revoking antidumping duties on milled rice as a result of U.S. challenge in the WTO.

Turning to the challenges that NAFTA faces today, there are three circumstances to consider. The first is implementation of remaining NAFTA commitments. All tariffs between the United States and Mexico will be eliminated on January 1, 2008.

While less than 1 percent of our NAFTA trade with Mexico remains subject to tariffs, their removal has raised concerns in some sectors. The NAFTA Trade Ministers have made clear that they are committed to full implementation of NAFTA.

A second set of challenges must take into account global trade. The NAFTA partners have begun by reducing trade barriers with other countries, which means there are smaller margins of preference provided by NAFTA itself. In 1993, for example, the average United States duty on imports was 3.2 percent for the world; by 2005, it had fallen to 1.4 percent.

The United States also faces more competition in our NAFTA markets. Mexico has free trade agreements with 42 countries today, compared with one other country in 1994. Canada has, since NAFTA, concluded three additional FTAs and is negotiating with the Republic of Korea.

A third set of challenges is how best to address security concerns while not creating trade barriers, an issue of which we are all especially aware of today. This issue is the mandate of the trilateral Security and Prosperity Partnership of North America. The SPP builds on NAFTA. We have been using, and will continue to use, both processes to advance common strategic goals in North America.

To conclude, the United States and its NAFTA partners today are not only better customers of one another, but better neighbors,

more committed partners, and more effective colleagues in a wide range of trade-related international initiatives.

Senators, I would be happy to answer any questions you may have at the conclusion of this panel's testimony. Thank you.

Senator THOMAS. Thank you, Mr. Melle.

Ms. Saucedo?

**STATEMENT OF CATHY SAUCEDA, DIRECTOR, SPECIAL ENFORCEMENT, U.S. CUSTOMS AND BORDER PROTECTION, WASHINGTON, DC**

Ms. SAUCEDA. Chairman Thomas and Senator Bingaman, I, too, have presented written testimony for the record.

It is a privilege and an honor to appear before you today to discuss the operational impact and enforcement efforts of the North American Free Trade Agreement by Customs and Border Protection.

I want to begin by expressing my gratitude to Chairman Grassley and Ranking Member Baucus, and the committee, for the interest and support you provide as CBP continues to administer and enforce NAFTA, while facilitating the flow of legitimate trade that is so important to our Nation's economy.

U.S. market-opening initiatives took a significant step forward with the entry into force of the U.S.-Canada Free Trade Agreement in 1989. This FTA greatly liberalized trade between the United States and Canada. It was the first FTA that had specific rules of origin, which provided concrete, non-subjective methods for determining the origin of a good.

In 1994, the US-CFTA was superseded by NAFTA. Implementation of this trilateral FTA with the United States' two largest trading partners not only led to a surge of U.S. exportations, but also resulted in a dramatic increase in importations from Canada and Mexico. Since its implementation in 1994, the administration of NAFTA has improved over the years, although CBP continues to experience operational challenges.

NAFTA was the first FTA to address the concepts of transparency and facilitation within the context of implementation, administration, and enforcement of the agreement. CBP promoted transparency through the creation of a temporary call center manned by CBP NAFTA experts to assist CBP and the trade during the implementation phase of NAFTA.

In the spirit of facilitation, the NAFTA negotiators ensured that the flow of trade was not disrupted or hindered by waiving the requirement of the presentation of a paper document, the Certificate of Origin, as a condition of release of the goods. Canada adopted this same procedure, while Mexico continues to require the presentation of a Certificate of Origin prior to the release of the goods.

CBP continues to refine the application of NAFTA and has introduced increased flexibility regarding the presentation of the Certificate of Origin. Initially, the certificate had to be completed on an official, trilaterally agreed upon form, as directed by NAFTA's Uniform Regulations. However, in July of 2005, CBP began to allow the certificate to be in any format, as long as all of the data elements were present.

The experiences CBP has gained through implementing, administering, and enforcing NAFTA have been overwhelmingly positive, although there have been some challenges posed by the agreement.

The provisions of NAFTA require a properly completed NAFTA Certificate of Origin to be signed by the exporter and in the possession of the importer prior to the claim for preferential treatment.

If these requirements are not met, NAFTA requires that the claim be denied, regardless of whether the good is, in fact, originating per the specific rules. This presents rigorous, paper-intensive requirements for the trading community and requires that claims be denied based solely on a paper document rather than the rules of origin. We have remedied this provision in subsequent trade agreements.

Due to the fact that the exporter is required to complete the Certificate of Origin, NAFTA is termed an “exporter-focused agreement.” Although the importer makes the claim and is the responsible entity for duties and any penalties, if any accrue, the determination as to whether or not a good is originating is made by the exporter who may or may not fully understand the requirements of NAFTA.

CBP does verify the origin of a good for which NAFTA preference is claimed through a verification, which also includes verification visits. However, there are several steps necessary prior to initiating a verification, and these steps can interfere with the ability to accurately gauge the veracity of a party’s preference claim.

CBP must first obtain a Certificate of Origin from the importer. Obtaining this Certificate of Origin does not constitute a verification. The actual verification is of the exporter or producer, who must provide information beyond the certificate to support the preference claim.

A shortfall of NAFTA is that the importer, who is ultimately responsible for the claim, is not an active participant in the verification process. Additionally, although CBP must conduct verifications through the exporter, CBP has no jurisdiction over an entity in a foreign country.

A verification can include a visit to the site of production in Canada or Mexico. This allows for an extension of CBP’s enforcement capabilities; however, NAFTA requires a 30-day notice to the exporter prior to the visit.

There is no flexibility with which to conduct strategic enforcement actions, as the exporter will have been provided at least 30 days’ notice, allowing dishonest exporters and producers to make operational adjustments well in advance of the verification visit. This notice effectively allows these exporters and producers the opportunity to clean up their act.

Although the United States, Canada, and Mexico have trilaterally discussed amending the restricted verification visit procedures to allow for more flexibility, no agreement has been reached to date. The exporter-focused regime presents logistical and administrative burdens to importers, exporters, as well as CBP.

An additional area that presents challenges involves textiles and wearing apparel. The three NAFTA parties still have not agreed upon a verification process for certain textiles receiving preferential treatment. CBP continues to meet trilaterally with the Mexican

and Canadian governments in an ongoing effort to resolve differences and agree upon verification procedures.

NAFTA provides for workgroups among the parties to address these types of challenges and other concerns in the areas of administration, interpretation, and enforcement. These work groups successfully tackled many issues during the first few years; however, the parties have not been able to make significant progress on the remaining trilateral issues.

NAFTA's concrete and transparent obligations for the importer, exporter, and government agencies have taught us a great deal regarding provisions that work well and those that require refinement.

NAFTA serves as a framework for the newer FTAs. The newer FTAs have shifted from an exporter-focused to an importer-focused regime, while at the same time eliminating the Certificate of Origin as a formal document.

I have briefly discussed the operational impact and enforcement efforts of NAFTA that CBP has encountered over the past 12 years. NAFTA has been monumental in the creation of a framework from which new FTAs are being modeled and shaped.

We have gleaned positive and effective provisions that allow for an enforceable and operationally sound agreement and have also streamlined the more complicated concepts. We continue to maintain and administer the largest multilateral agreement that the United States has entered into, while retaining effective enforcement methods.

Thank you for this opportunity to testify. I will be happy to answer any of your questions.

Senator THOMAS. Thank you.

[The prepared statement of Ms. Saucedo appears in the appendix.]

Senator THOMAS. We will have a period of questions now.

Mr. Melle, you mentioned that we removed the duties in all sectors. In April, the Director said that there remains trade subject to duties, but there are concerns in the various sectors.

Now, what is the status of that area where there were not duties?

Mr. MELLE. The major commodities that still have duties are largely our exports to Mexico, which covers corn, dry beans, milk powder, and, of course, we both have duties on sugar.

There has been some concern expressed in Mexico over the elimination of the duties on corn and beans. The Mexico government, the Fox administration, has committed to implementing those obligations. Obviously, those are very large exports from a large number of States in the United States.

In fact, we have a working group meeting with the government of Mexico tomorrow to discuss how to smooth that transition to full and open trade in those commodities.

As I mentioned, we reached an agreement on sweeteners in July that hopefully does put us on a path to full implementation of the sweetener provisions as well.

Senator THOMAS. But you indicated that the duties would all be removed in a certain time. Is that what you said?

Mr. MELLE. Absolutely. January 1, 2008. Yes.

Senator THOMAS. And you are going to be able to overcome the difficulties?

Mr. MELLE. Well, the difficulties may be as much perception as reality. To take corn, for example, which is probably the single largest concern in Mexico, Mexican corn production has continued to increase after NAFTA.

Much of the exports from the United States have gone to their feed, their cattle and poultry industries, where the consumption of those goods is way up. So we think the issue is manageable, yes.

Senator THOMAS. I see.

You mentioned settlement of the softwood lumber thing between Canada and Mexico. One of the interesting parts of that is, apparently, the parties used both NAFTA and WTO rules to come to an agreement. Why is it that rules of both these trade associations can be used to govern this dispute?

Mr. MELLE. The two systems have a different standard of review. I should say I am not an attorney, so I can just give you an informal answer here. But the WTO rule is based on meeting a WTO set of obligations, while the NAFTA review is conducted by companies that are challenging, in this case, the administration and implementation of U.S. laws.

So, from the beginning, there are two different standards. When you have two different standards, you sometimes get two different results out of dispute settlement bodies, which is what happened in some of the lumber cases.

Senator THOMAS. I guess the question is, why would WTO rules be used in NAFTA?

Mr. MELLE. Well, it is the same issue that is being challenged in both, that is, the imposition of dumping and countervailing duties. But again, each result was based on applying a different standard. So it is not that the WTO was telling us what to do under NAFTA. Both sets of panels were telling us what to do with respect to those orders.

Senator THOMAS. I see.

As I said earlier, the purpose of this panel and the purpose of this process is to see if there are things that could better the agreement, that would make it work better, that would be more productive.

You have been monitoring this for a good long time. Do you have thoughts? Do you have areas that have worked well and areas that need attention that you think should be considered?

Mr. MELLE. One of the areas that we are currently working on, as Cathy Saucedo mentioned, is the complicated rules of origin. NAFTA was a comprehensive agreement with our two largest trading partners, so it got an incredible amount of scrutiny by a wide range of business and agricultural sectors, in much more depth than you might expect for a smaller trading partner.

What we have seen over the last 12 years is that trade patterns have changed, that production decisions have changed, and that perhaps in some cases the old rules of origin no longer make sense or facilitate trade.

So we have been making changes to those. We have done three sets of changes so far and hope another set will be implemented

sometime next year. Cathy has talked about continued efforts we need to make at the border.

There is always the potential to reduce the transaction costs and, through both NAFTA and through the Security and Prosperity Partnership, we are getting private sector input and attempting to address some of those concerns.

Senator THOMAS. All right.

Ms. Saucedo, you apparently then have multiple hats. National security has also become an even more important function over the years. Does Customs balance the need between efficiently moving products and security interests?

Ms. SAUCEDA. Certainly. Although I am not an expert on all of these programs, since 9/11 there have been many programs put into place with CBP: the Trusted Partnership programs, and the like. We have established layered approaches to our enforcement efforts so that we do not unnecessarily delay shipments.

Those types of inspection methods, the NII (Non-Intrusive Inspection) equipment and the like, allow us to expedite and facilitate legitimate trade where we can more easily detect those shipments that need further inspection.

Senator THOMAS. When problems arise or bottlenecks occur, do you involve the private sector in identifying solutions?

Ms. SAUCEDA. I personally believe that one of the things that CBP does very well is involve the trade in issues. One of the most significant, of course, is the Trade Act of 2002, when we held multiple hearings with the trade on how to work with the advance information requirements so that the trade is not unnecessarily encumbered, while CBP can still get the information in advance of the arrival of the shipment.

We also have committees within our ACE system called the Trade Support Network (TSN), where we work with the trade on our facilitative approaches through electronic means. We also have other committees with the trade, such as the Commercial Operations Advisory Committee (COAC), where we meet quarterly and discuss issues that involve the trade community and CBP actions in the trade area.

Senator THOMAS. All right. Thank you.

Senator Bingaman?

Senator BINGAMAN. Thank you very much.

Mr. Melle, the Chairman here was asking you about areas in NAFTA that need more work or need some changes. I think that was the thrust of one of his questions.

The testimony that we have put in the record by the policy director for the AFL-CIO, Ms. Lee, says at one point, "The NAFTA labor side agreement has utterly failed to protect labor's rights. None of the 34 cases filed under the side agreement has progressed beyond the initial stage of cooperative consultations."

I would be interested in your reaction to that statement, whether you think it is true, whether you think there is a logical explanation, or whether we need to make some changes.

I have here a chart that is entitled "The Dispute Settlement Procedure for the North American Agreement on Labor Cooperation." I believe this sets out the procedure that is followed when there is concern about labor rights under that side agreement.

According to the way I understand her statement, there are four stages in this. We are still in the first stage with regard to each of the 34 complaints that have been raised in the 14 years that this agreement has been in place.

Do you have a reaction or any knowledge about this?

Mr. MELLE. Well, I am aware of those cases, Senator. I would like to respond more extensively for the record later. I think the one point I would make here is, I think the first question is, how do you measure success?

I think we take the view that the dialogue, the openness, the scrutiny that the NAFTA labor agreement has provided is, in and of itself, a success and you do not necessarily have to score each particular complaint or petition and see how far it gets in the process to get results that are useful and desirable.

Senator BINGAMAN. So your thought is that the fact that none of these has gone beyond the first of the four stages is not a sign that the system is not working.

Mr. MELLE. Correct.

Senator BINGAMAN. Well, I would be interested in any kind of elaboration you could give me with regard to these 34 complaints. It strikes me that there is something deficient in the system, the procedures that we have set up, if there is no way to move these cases along and resolve them one way or another.

[The information appears in the appendix on p. 54.]

Senator BINGAMAN. Let me ask about another issue. I have complained about this, even at hearings before this committee, before. We have been trying for the last couple of years now to reopen the Mexican border to imports of live breeding bulls and dairy heifers from the United States.

As I understand it, so far in 2006 we have imported 780,000 live Mexican cattle, and they have not imported a single live animal from the United States. Mexico is now imposing 28 separate requirements on live cattle to be imported from the United States.

I guess my question is, if we cannot get any movement on this, why do we not impose those same 28 requirements on Mexican cattle coming into this country?

Mr. MELLE. Senator, every time you ask a USTR official about cattle trade with Mexico that question comes to me, so I am quite familiar with your interest. I know you, indeed, are very interested in this and are very much results-oriented.

I can report that we have succeeded in having breeding bulls enter Mexico, but we have not yet obtained any agreement over dairy heifers.

Senator BINGAMAN. So breeding bulls are now permitted to enter Mexico?

Mr. MELLE. That is my understanding.

Senator BINGAMAN. Because that is contrary to what I have been told.

Mr. MELLE. Let me verify that for you, Senator. But my understanding is, they have been allowed for several months.

Senator BINGAMAN. Oh, really? All right. That is new information. I thought they were continuing to block that.

Mr. MELLE. On dairy heifers, I do not have success to report yet. I know our veterinarians are working at USDA and with our Mexi-

can counterparts very intensively. But again, since you are results-oriented, I do not have an outcome yet, but hope that they are quite close.

Senator BINGAMAN. All right.

Let me ask about one Customs-related issue that, Ms. Saucedo, you would be the right person to respond to. This also is a fairly parochial question related to my State. We have a port of entry between the United States and Mexico at Santa Teresa.

Several companies have complained that the rate of truck inspection at Santa Teresa is significantly higher than the rate of trucks inspected at ports of entry in the neighboring State of Texas.

First, I guess I would ask whether you can confirm that, and if you can, is there a reason to think that there are more illicit goods being carried from Mexico to the United States through the Santa Teresa port of entry than through ports of entry in Texas?

Ms. SAUCEDA. Sir, off the top of my head I do not know the answer, but we will get a response back to you.

Senator BINGAMAN. I would appreciate that. That would be very useful.

Those were the questions I had of this panel, Mr. Chairman. Thank you.

Senator THOMAS. Thank you.

Just one more question for both of you, I guess. I understand NAFTA partners are undertaking a complete review of NAFTA which identifies more ambitious disciplines than contained in other free trade agreements. What do you think will be the result of this review, either of you or both of you?

Mr. MELLE. Well, let me start. We expect to have a meeting with our counterparts at a Vice Ministerial level in the next couple of months—as you know, there have been some management changes at USTR since we undertook our review—where we will be discussing it with our partners.

I think, generally, we are looking at issues of trade facilitation, of simplification of NAFTA, and, as I mentioned, continued effort to make sure all the NAFTA obligations are implemented on time.

Senator THOMAS. Do you have any comment?

Ms. SAUCEDA. The only comment I would like to make is that CBP would be very pleased to participate with USTR in this review to better facilitate under NAFTA.

Senator THOMAS. All right. Nothing very specific?

Ms. SAUCEDA. No, sir.

Senator THOMAS. Just one final comment. During the negotiations, we entered into a side letter on sugar. I will not go into detail, but apparently that process is flawed. I have never been able to get a copy of the letter, and Mexico denies being bound by it. Do we still use side letters in trade negotiation?

Mr. MELLE. I believe the literal answer to that would be yes, but I also think we do a much better job of it than we did in this one particular instance.

Senator THOMAS. All right.

Anything further, Senator?

Senator BINGAMAN. No.

Senator THOMAS. Well, thank you very much. We appreciate it, and look forward to working with you.

Let us go on then to our next panel, which includes Mr. Jim Magagna, executive vice president of the Wyoming Stock Growers Association. I am being a little localized, but I want to particularly thank Mr. Magagna for being here from Wyoming. I appreciate that.

The rest of the panel consists of Mr. Craig Lang, president of the Iowa Farm Bureau Federation; Mr. Jerry Pacheco, executive director, International Business Accelerator in New Mexico; Sandra Polaski, senior associate and director, trade, equity, and development project, Carnegie Endowment for International Peace; and Dr. Sidney Weintraub, chair in political economy, Center for Strategic and International Studies. I thank all of you for being here.

You will have about 5 minutes, please. You will see it on your equipment there. Your full statements will be put into the record. We appreciate it very much.

Mr. Magagna, would you like to begin?

**STATEMENT OF JIM MAGAGNA, EXECUTIVE VICE PRESIDENT,  
WYOMING STOCK GROWERS ASSOCIATION, CHEYENNE, WY**

Mr. MAGAGNA. Thank you, Mr. Chairman. I appreciate the opportunity to be here with you today. It is also a pleasure to sit here with Senator Bingaman, I would like to say, just a few years after we sat in the halls of Stanford Law School together.

Mr. Chairman, for the record, I am the executive vice president of the Wyoming Stock Growers Association. For some 134 years, we have represented the cattle industry in the State of Wyoming. I am also personally a lifelong sheep rancher, and the former president of the American Sheep Industry Association.

I would like to focus this afternoon primarily on two areas with regard to NAFTA. The first is the evolving dichotomy with which the three nations look at this trade agreement in terms of the cattle industry.

I might preface this by saying that my remarks will tend to focus on the situation that existed prior to the outbreak of BSE in Canadian cattle, since that has significantly distorted some of those relationships.

Second, I will focus on the way that the sanitary and phytosanitary regulations have been dealt with under NAFTA.

By way of a general opening comment, I want to acknowledge that NAFTA has certainly resulted in a tremendous increase in the movement of beef and live cattle products among the three nations.

The evidence is far less clear, however, that any benefit has occurred from that, particularly to the cow/calf sector of the cattle industry that I represent. And certainly in Wyoming, most of our producers would share my judgment that we have not seen any measurable direct benefit.

But to give you a better background, with Mexico in particular, prior to NAFTA, total beef movement from the United States to Mexico, net, was about \$200 million a year.

Last year, in spite of even the partial restrictions of BSE, there was some \$893 million, and for the first 6 months of this year, \$564 million. So, certainly there is a tremendous amount of beef product moving into Mexico.

But I caution, that has to be measured against the large number of Mexican feeder cattle moving into the southwestern States of the United States; so, to a great degree, we are turning product around.

A comparison. For the first 10 years of NAFTA across the three nations, at least one economic analysis that has been done that I have referred to several times in my written testimony, would indicate that, as a result of NAFTA, there has been a reduction in U.S.-fed cattle prices of approximately 82 cents per hundred-weight, and a reduction in feeder cattle prices of approximately 77 cents per hundred-weight. So, again, when it is all added up, the benefits are not quite that clear.

With regard to my first point, in the industry we view Mexico and Canada as, clearly, our partners in the beef business, but also as our competitors in the beef business.

We recognize that certain segments of our industry, particularly the packer/processor segment, benefit by promoting the concept of a North American beef industry. On the production side of the industry, particularly the cow/calf sector, we feel that that characterization is inaccurate, and perhaps even harmful.

There are clear differences in production, in regulatory practices that our producers are faced with, in terms of environmental concerns, in terms of labor laws, that distinguish our industry very clearly from the industry of our two partners, particularly from that of Mexico.

So while perhaps it does not call for changes in NAFTA, we are asking you, the members of this committee, to encourage a change in the way that this administration looks at NAFTA in terms of defining the beef industry. We are clearly three distinct industries that have much to be gained from cooperation from trade amongst ourselves, but we are not a North American beef industry.

Turning to the issue of sanitary and phytosanitary provisions contained in NAFTA, NAFTA provides significant language about how these issues are to be addressed, protecting the rights of individual Nations to establish those standards that they need, not necessarily binding them to international standards.

It was our hope when NAFTA was originally approved that it would provide a process for effectively, efficiently, and timely dealing with differences and with concerns in terms of sanitary and phytosanitary, or animal health, in particular, regulations among the countries.

The best example I can provide to you, Mr. Chairman, is Canada, where, since prior to the adoption of NAFTA, the U.S. has worked hard to achieve a relaxation of Canadian standards with regard to blue tongue and anaplasmosis on the movement of live cattle into Canada from, particularly, our mid-level States—not the very northern tier States, but the mid-level States—to move those standards more into compliance with international standards.

All appearances are that NAFTA was totally ineffective in providing us a tool for getting there. Just this year, Canada has announced those relaxations. It would be my conjecture that that was driven far more by the BSE situation and their desire to restore their trade relationship in beef with the United States than it was by anything contained in NAFTA itself.

Turning to Mexico, particularly commenting at this point on the sheep industry, we have seen Mexico repeatedly close its borders for a period of time to the importation of live-slaughter sheep and to various sheep meats from the U.S., each time citing various health and food safety concerns to justify such actions.

Again, if NAFTA is truly to provide for free and open trade between our Nations, among our Nations, then we feel that it should address these issues. Not that they will not arise, but that it should provide an efficient mechanism for dealing with them so that they do not, as I believe to be the case with Mexico, allow them to be used as trade barriers in an effort to protect the domestic industry. We need to move toward a harmonization of these sanitary and phytosanitary standards.

By contrast to the comments I have made about Canada and Mexico, the U.S. seems to have taken a much more liberal approach to respecting these.

We would urge, Mr. Chairman, that USTR and this committee look at some change to Chapter 7 of NAFTA in an effort to ensure that these sanitary and phytosanitary issues are addressed.

In closing, Mr. Chairman, I would simply point out that we do believe that the U.S. cattle industry has a bright future based on our ability to maintain our preference in our domestic markets and to aggressively participate in international markets, including those of Canada and Mexico.

But in order to achieve these goals, we ask your assistance in providing our trade negotiators with direction to ensure increased access to export markets on terms that are no more restrictive than those that we grant to other nations.

In closing, Mr. Chairman, I again want to thank you for the opportunity to testify today, and I will stand ready to address questions from you and Senator Bingaman as this panel moves forward. Thank you.

Senator THOMAS. Thank you, Mr. Magagna.

[The prepared statement of Mr. Magagna appears in the appendix.]

Senator THOMAS. Mr. Lang?

**STATEMENT OF CRAIG LANG, PRESIDENT, IOWA FARM  
BUREAU FEDERATION, WEST DES MOINES, IA**

Mr. LANG. Thank you, Mr. Chairman and Senator Bingaman. I also remember the events of 5 years ago, and believe me, as I got on the plane today, I did think about that. But the good news is, I believe it is safer to travel today than it was 5 years ago. So, I appreciate your remarks.

My name is Craig Lang. I am a fifth-generation farmer from Brooklyn, IA. My family and I farm a little over 1,000 acres of corn and soybeans, and we also have pasture. We milk nearly 500 dairy cows.

I am the president of the Iowa Farm Bureau, and I also serve on the American Farm Bureau Federation Board of Directors and the Trade Advisory Committee for the American Farm Bureau Board. I want to thank you for this opportunity to speak to you about the North American Free Trade Agreement.

NAFTA has been good for much of American agriculture, and for Iowa agriculture, in particular. Thanks to NAFTA, Canada and Mexico now buy a third of U.S. agricultural exports and also supply a third of our agricultural imports.

Japan used to be our top export market for the American farm products, but now Canada is number one and Mexico is number two, followed by Japan.

Because of NAFTA, the United States is now the number-one export market for both Canada and Mexico, and I believe this is good. Compared to 1993, the year before the NAFTA treaty went into effect, the dollar value of the 2005 U.S. agricultural exports to Canada has doubled. With our two-way trade agreement with Canada in 2005, both exports and imports are up nearly 130 percent since NAFTA.

Our history with Mexico is even more impressive. Compared to 1993, last year's farm exports to Mexico have increased by 160 percent, and the two-way trade is up 180 percent. It is clear that NAFTA has dramatically increased agricultural trade with our neighbors by lowering tariffs and eliminating other trade barriers, both of which are important ingredients in a true market integration.

Since NAFTA, Mexico has become a priority market for American grain. Soybeans, corn, and sorghum are some of our major exports to Mexico, where they are used in livestock feed. Mexico is also a promising market for corn gluten meal and distillers' dried grains, the corn ethanol co-products fed to our livestock. With the build-up in ethanol plants today, you know how important that extra market is.

Income and population growth in Mexico mean more demand for protein, so the Mexicans are buying both livestock feed for their own industry and finished meat and dairy products from the U.S. We in Iowa are especially grateful for Mexican purchases of U.S. beef. Since the Japanese market closed to U.S. beef in 2003, Mexico is now our number-one export market for beef.

A couple of years ago, the Iowa Farm Bureau put up \$50,000 with the U.S. Meat Export Federation Board and put a project together in dining areas in Mexico, and we immediately had fans of high cuts of meat from the Midwest.

The Mexican consumer preference also provides valuable markets for meat products in low demand here, such as turkey dark meat for processing into turkey ham, beef tripe, or menundo, and pork intestines for sausage casings. Now, menundo is a beef tripe, which is a stomach stew, and is very popular in Mexico, but I cannot tell you that I have ever had it.

What food products do we import from Mexico? Consumer goods and warm climate labor-intensive crops for which Mexico has a comparative advantage. Everybody knows about Corona beer and Tequila, peppers and tomatoes, avocados and mangoes. American consumers benefit from lower prices and more year-round variety in fruits and vegetables because of NAFTA. Both countries we trade in have a large diversification of trade. Our agriculture trade is diversified in Canada, with processed foods, lumber, and paper products as some of our top exports.

Most of our agricultural exports to Canada are consumer-ready, high-value food products. Iowa's top 10 merchandise exports from Mexico are mostly farm commodities. In Iowa, we sell manufactured goods to Canada, like tractors and front-end loaders, refrigerators and washing machines, and processed steel.

The only agricultural product in Iowa's top 10 exports to Canada is soybean meal for the livestock feed. But U.S. grain is also going to Canada in the form of those processed foods, and Canada is buying U.S. corn for livestock feed, ethanol production, and corn syrup production.

Iowa is the number-one State in pork production, thanks, in part, to Canada. Only about half of the hogs marketed in Iowa are born in Iowa. Iowa farmers buy baby feeder pigs from other States to fatten on Iowa corn and soybeans.

Our largest single source of feeder pigs is Canada. Iowa imported almost three million Canadian piglets last year, and believe me, our growers of pork believe Canadian pigs are the best.

Our beef industry is even more integrated with Canada and Mexico, thanks to NAFTA. Last year, American cattlemen imported about 1.25 million feeder cattle from Mexico and about 240,000 feeder cattle from Canada. U.S. packing plants also imported 320,000 slaughter cattle from Canada.

When the border closed on BSE, our slaughtering facilities—or harvest facilities as we like to call them—were seriously in jeopardy because they had to close down on one shift, and you cannot do that very long in the processing industry.

With these numbers of cattle crossing the borders, we have evolved into an integrated North America cattle industry that benefits ranchers, meat processors, and consumers in all three countries. Over the past 12 years, the forecasted benefits of NAFTA have come true.

Nobody can deny that the overall effect of NAFTA has been overwhelmingly positive. Our closest neighbors are American agriculture's best export customers. There is no doubt that NAFTA has helped American farmers expand export markets and increase American farm income.

Thank you. I will answer any questions later.

Senator THOMAS. Thank you very much.

[The prepared statement of Mr. Lang appears in the appendix.]

Senator THOMAS. Mr. Pacheco?

**STATEMENT OF JERRY PACHECO, EXECUTIVE DIRECTOR, INTERNATIONAL BUSINESS ACCELERATOR, SANTA TERESA, NM**

Mr. PACHECO. Thank you, Mr. Chairman and members of the committee. Thank you for inviting me here today to discuss NAFTA from a private sector standpoint on the border.

For the record, let me state that I have lived and worked in Mexico for the past 16 years in both the public and private sectors. My main focus during this time has been assisting both large and small companies wishing to explore the trade opportunities in Mexico.

Currently, I manage the International Business Accelerator, a nonprofit international trade counseling center that is part of the New Mexico Small Business Development Center network.

The Accelerator helps businesses take their products and services to the global market. We have offices in Santa Teresa, NM, where we have an inordinate amount of inspections, as the Senator said, and we also have an office in Chihuahua City, which is about 240 miles south of El Paso, TX. The El Paso/Juarez/southern New Mexico border complex is the largest industrial base on the entire U.S.-Mexico border.

Now, from a large company standpoint, NAFTA has facilitated the entry, which was previously difficult or at times impossible, into the Mexican market. I have seen this firsthand. My old real estate development group recruited to our three industrial parks in Santa Teresa approximately 35 companies for which we built more than 2 million square feet of industrial space.

Approximately 1,500 direct jobs, and three to four times as many indirect jobs were created by these companies in southern New Mexico, which is one of the poorest regions in all of the U.S. Almost every single one of those companies is tied into either the Mexican maquila industry or some type of Mexican industry.

American companies account for the largest portion of Mexico's imports, and NAFTA has facilitated this flow of goods and services south. Now, from the standpoint of smaller companies, the biggest effect that I believe NAFTA has had is creating an interest in exploring business in Mexico that previously did not exist.

In the pre-NAFTA period, it was extremely difficult to generate any Mexican export successes because smaller companies simply did not have the resources to overcome all of the barriers that the Mexican market presented. Today, our trade counseling center is inundated with smaller companies hungry to explore opportunities south of the border.

In my experience, the removal of tariffs from a Customs schedule is clear and understandable. What are hard to eradicate, and continue to pose a serious threat to the fulfillment of NAFTA, are the non-tariff barriers or the bottlenecks, and these can take the form of congestion at the ports of entry, confusion over proper documents needed to cross merchandise across borders, uncertainty over work visa permits, and inconsistent cargo inspections, among others.

I will discuss a couple of these, briefly. Total two-way trade between the U.S. and our NAFTA partners has increased by more than 100 percent, despite the fact that Mexican commercial trucks coming to deliver merchandise in the U.S. market cannot go further than a thin border commercial zone north of the U.S.-Mexico border.

Truck drivers and their cabs, if they are coming from Mexico, have to cross into the United States, unhitch their trailers with their cargo, and have an American truck and driver deliver the merchandise to its final destination in the U.S. A similar situation exists for U.S. trucks going south. This extra process adds time and costs to the logistic chain, which are then passed on to the consumer.

Of course, we do not want to endanger U.S. citizens with unsafe trucks on our roads. I live in the Border Commercial Zone. I have

a wife, Loretta, and son, Joseph, who are driving side by side with the Mexican trucks on a daily basis, and I certainly do not want to see them put in harm's way. But the restricted trucking area there really adds a bottleneck that impedes the free flow of trade.

A positive development in terms of the expediting of cargo, while at the same time addressing security, is the Fast and Secure Trade program, or the FAST, that is managed between the private sector and the Bureau of Customs Protection, under the aegis of the Customs Trade Partnership Against Terrorism.

In this program, qualified manufacturers, distributors, and logistics firms commit to securing shipments against terrorist activities and contraband from the time the product is made to the time that it crosses the border and is delivered.

Companies participating in this program are then allowed to use the special FAST crossing lane for expedited crossings. This program holds a lot of promise for combatting illegal activities and congestion at the ports of entry.

Now, NAFTA created a special temporary work visa for Canadian and Mexican citizens wishing to work in the U.S. called the TN visa. From 1996 to 2005, almost 700,000 TN visas were issued for Canadians. This averages more than the current total annual 65,000 cap on the H1B visa.

During this same period of time, Mexican workers were issued about 20,000 TNs, which averages less than 2,000 per year. Many employers do not want to go through the paper-heavy, time-consuming bureaucratic process of sponsoring a Mexican employee or trying to qualify them per a list of acceptable TN professions.

I, myself, have gone through the TN process to sponsor an employee who works in our program, and by the time we had finished the application, we had created a book about the size of "War and Peace," and it was not a very pleasant experience. I can see why many U.S. employers or many U.S. companies that need Mexican work within the company do not want to go through that process.

Now, if we realistically want to create a North American free trade bloc so that we can remain competitive against other regions of the world, can we realistically expect to do this without some type of viable work visa program?

Now, the retraining of workers negatively affected by NAFTA has been a rocky road, at best. Many workers or companies do not know that training funds are available, and, if companies are aware of this assistance, it can be hard for them to prove that an agreement such as NAFTA has negatively affected their welfare.

At the time that NAFTA was implemented, the U.S. Department of Commerce started charging for its services that previously were provided for free. Many smaller companies cannot afford or are not willing to pay for these services.

The potential for this organization to increase its impact on the small business sector is great, but more along the lines of how it operated before. Commerce has been one of my favorite agencies to use when we help businesses, but it has become less user-friendly.

Now, 15 years after having become involved in supporting NAFTA, I still believe that the agreement has brought more positive than negative effects to the U.S., especially in terms of increased exports and the creation of export-based jobs.

Every day I work on the U.S.-Mexico border assisting U.S. companies to break into the Mexican market. We have had export successes in Mexico with clients involving telecommunication systems, high technology products, and automotive accessories.

Without NAFTA, the majority of our clients would not have been able to expand the markets or create the new jobs that currently exist in my State due to this agreement. From 1993 to 2005, the State of New Mexico's exports to Mexico more than quadrupled. Similar results have occurred in an overwhelming number of U.S. States.

Now, by no means is NAFTA perfect; many issues need to be addressed. However, we can learn from the positives and negatives of NAFTA in order to better structure future U.S. trade agreements to create new opportunities for U.S. companies and new jobs for Americans.

Thank you very much for allowing me to testify in front of this committee. I would be happy to take any questions you may have on my remarks.

Senator THOMAS. Thank you very much.

[The prepared statement of Mr. Pacheco appears in the appendix.]

Senator THOMAS. Ms. Polaski?

**STATEMENT OF SANDRA POLASKI, SENIOR ASSOCIATE AND DIRECTOR, TRADE, EQUITY, AND DEVELOPMENT PROJECT, CARNEGIE ENDOWMENT FOR INTERNATIONAL PEACE, WASHINGTON, DC**

Ms. POLASKI. Thank you, Mr. Chairman, and thank you, Senator Bingaman, for this opportunity to comment on the performance of NAFTA at 12. I, too, have submitted more extensive written testimony for the record.

My name is Sandra Polaski, and I am a senior associate at the Carnegie Endowment for International Peace, where I direct policy work on trade and development. Previously, I had the privilege of serving both Secretary Colin Powell and Secretary Madeleine Albright as the Senior Representative for International Labor Affairs at the State Department where, among other responsibilities, I did negotiate labor issues in trade agreements.

Prior to that, I was the Director of Research for the NAFTA Labor Secretariat, the intergovernmental organization that administers the NAFTA labor side agreement.

As the brief biography suggests, my analysis of trade agreements tends to include particular emphasis on the employment and related effects of trade agreements. In the case of NAFTA, it is very instructive to look at the agreement's employment consequences, because that is one of the most important channels through which NAFTA has affected the United States.

I am speaking not about the direct effects on employment and income within the United States, because frankly NAFTA's effects on these have been small given the enormous difference in the size and comparative advantages of the two countries. My written remarks go more extensively into the experience of the U.S. under NAFTA, and employment, again, is very small.

But, rather, it is the employment and income effects of NAFTA in Mexico that I think are key to understanding several related current policy challenges that now confront the United States, and Congress in particular.

In Mexico, NAFTA was a key contributing factor to a series of changes that have had deep and important consequences affecting migration patterns, overall economic growth in Mexico, and, indeed, political stability.

I would like to mention only the highlights of my written testimony on these points. NAFTA has produced disappointing results for job growth in Mexico. Data limitations and the difficulty of isolating NAFTA effects from other causes preclude an exact tally, as with other measures of NAFTA, as my fellow speakers have mentioned, but it is clear that, overall, the jobs created in the manufacturing sector in Mexico have not kept pace with the jobs lost in the agricultural sector in Mexico.

There has been a decline in non-maquila manufacturing employment in Mexico since NAFTA took effect in 1994. Employment in the non-maquila manufacturing sector stood at 1.4 million in January of 1994, sharply declined during the peso crisis, recovered briefly, but then began declining again, and has declined over the last 5 years, so that in June of this year there were about 130,000 fewer manufacturing jobs in Mexico outside of the maquilas than when NAFTA took effect.

The pattern in the maquiladoras themselves has been more positive, as maquiladora assembly plants added about 800,000 jobs between NAFTA's enactment in 1994 and the sector's peak employment, which occurred in 2001. However, they have been shedding jobs since then. Currently, they employ about 700,000 more workers than they did before NAFTA.

Adding the results together for the maquila and non-maquila manufacturing sectors in Mexico, we can see that, overall, about half a million jobs were gained in Mexican manufacturing between January of 1994 and June of 2006, the most recent statistics available.

By contrast, Mexican agriculture has been a net loser in trade with the United States. Although we have heard statistics on the two-way flow of trade between Mexico and the U.S., indeed, Mexico has had a negative trade balance with the U.S. in agriculture persistently since NAFTA was adopted, except for the peso crisis year of 1995, when Mexicans could not afford imports.

Employment in the agricultural sector in Mexico has declined sharply. U.S. corn exports, in particular, have been implicated, in that they have depressed corn prices and agricultural employment in Mexico.

It is a fair conclusion to say that the rural poor in Mexico have borne the brunt of adjustment to NAFTA in that country. Agricultural employment in Mexico stood at about 8.1 million in the years before NAFTA came into force in the early 1990s. It actually increased slightly during the peso crisis, when many unemployed workers returned to the agricultural sector and agricultural production. However, ever since the peso stabilized, employment in the sector has been on a steady downward trend, currently about 6 mil-

lion jobs in the first quarter of 2006, in other words, a loss of over 2 million jobs compared to the pre-NAFTA levels.

Not all that reduction could be attributed to NAFTA, of course, but other forces that influenced agricultural trade in Mexico, such as the devaluation of the peso, pushed in the opposite direction in favor of exports. So we have to assume that the lowering of trade barriers was an important factor in that continued decline in agricultural employment more than offsetting the growth in manufacturing employment.

The experience of Mexico, unfortunately, confirms the prediction of trade theory, that there will be both winners and losers from trade. The losers, however, may be as numerous—or in some cases more numerous—than the winners, especially in the short to medium term, and in Mexico, clearly, more farmers lost from NAFTA than gained from the NAFTA-induced changes.

Looking at another related measure very quickly, real wages for many Mexican workers today are lower than when NAFTA took effect. When I did the study of NAFTA at 10, 2 years ago, that was true overwhelmingly for workers in Mexico.

There has been some slight recovery, but still there is a stunning setback in wages in Mexico over the past 12 years. Mexican wages are diverging from, rather than converging toward, U.S. wages.

This overall performance of Mexican labor markets would be a concern to us, and certainly a concern to the members of your committee in general, looking at the economic performance of a near neighbor, but they are particularly important because of the impact that they have had on the pattern of Mexican migration to the U.S.

Migration is always a function of both push and pull factors, as the migration economists like to identify: the push outward of a sending country which cannot satisfy the employment and income needs of all of its population, and the pull into the receiving country which may have more job opportunities than its workforce can satisfy.

But the fact is, Mexican migration to the U.S. surged during the 1990s when the U.S. economy was going very strong and unemployment was at record post-war lows, and it surged even greater in the years after 2001 when the U.S. was in the recession and when unemployment levels were rising in the U.S. Clearly, the push factor out of Mexico is the strongest economic factor which can account for the pattern of migration that we have seen.

The policy consequences of this surge in migration are well known to this committee, and I will not rehearse them now, but I hope that this analysis helps to trace the sources of the migration push because, in part, that source is NAFTA, not in full but in part, and I think it suggests some of the ways that our implementation of NAFTA can be improved going forward.

This leads to a particular challenge that this committee will confront next year. As many have mentioned, there are still a few remaining tariffs that govern trade between the U.S. and Mexico, and these are on the most sensitive agricultural products traded between the countries, most importantly, from the perspective of Mexico, white corn and beans.

There is no doubt that this further liberalization of agricultural trade on January 1, 2008 will add new and very high impact

stresses in the countryside in Mexico. These stresses have implications for migration to the U.S. and for political stability in Mexico.

When earlier rounds of tariff reductions were implemented in the course of the NAFTA schedule, we saw blocking of highways, we saw massive demonstrations by Mexican farmers. More recently, we have seen demonstrations in the context of political frustration, and some of that frustration, again, can be traced to the countryside in Mexico which has not fared well in recent times.

These issues should be addressed with the greatest seriousness. There will certainly be a need for much more trade adjustment assistance for small-scale farmers within Mexico by the Mexican government, but there may also be a need for the U.S. to consider flexibility in the timetable for implementation of the tariff phase-out on white corn and beans.

I would argue that the U.S. Government should also consider development assistance targeted specifically at the Mexican countryside, particularly those regions of Mexico, mainly the south and some of the central regions, that have felt negative impacts from NAFTA in their agricultural sector but have felt few positive effects in other sectors.

This would be an investment in good neighborliness, but also one of the more effective instruments in addressing future sources of migration. It would also contribute to the political stability of one of our closest neighbors and allies.

In addition to these policy considerations, let me make one final point. As more free trade agreements have been negotiated and the World Trade Organization membership grows, the advantages that Mexico gained as the first developing country to have a free trade agreement with the United States are progressively eroded.

The accession of China, for example, to the WTO has meant mounting competition for Mexico's manufactured exports, particularly in labor-intensive sectors such as apparel and electronics.

The U.S. free trade agreement with Central America will add a sizeable pool of low-wage labor to the available regional labor force, further undermining Mexico's remaining advantages.

It is not in the United States' strategic interests to demonstrate that free trade agreements between the U.S. and developing countries do not produce clear advantages for our developing country trading partner. This is one more reason why the U.S., and this committee, should take a leadership role to ensure that NAFTA's negative impacts on Mexico are assuaged, to the extent that we can help the Mexican government do that.

Thank you. I would be happy to take questions.

Senator THOMAS. Thank you, Ms. Polaski.

[The prepared statement of Ms. Polaski appears in the appendix.]

Senator THOMAS. Dr. Weintraub?

**STATEMENT OF DR. SIDNEY WEINTRAUB, WILLIAM E. SIMON  
CHAIR IN POLITICAL ECONOMY, CENTER FOR STRATEGIC  
AND INTERNATIONAL STUDIES, WASHINGTON, DC**

Dr. WEINTRAUB. What I really want to do is make several points that have to do with NAFTA and with the context in Mexico and in the United States under which NAFTA has operated.

One of the main points I am going to make is that it is over-simplistic to say that a lot of things occurred in Mexico after NAFTA and, therefore, NAFTA was at fault. There is a tendency to do that. It is a well-known economic fallacy that whatever comes later was caused by whatever came before, and it just ain't so, as I am going to say.

You have already been given a lot of data on the growth in trade between the two countries. Mexico's exports have grown considerably more than our exports to Mexico have grown. We have a trade deficit with Mexico. We have a trade deficit with Canada. As an aside, we have a trade deficit with just about everybody in the world, so it is hard to just single out those two.

The idea that the net export growth—I mean, exports as compared with import growth—of Mexico was the problem in job creation in Mexico just defies common sense. The trade growth has been significant. I think there are other reasons.

I am going to get into some of them, and I will do it fairly quickly. Mexico has some deep structural problems that have not been addressed. I will get to the agricultural area in a few moments, but I will first look at some others.

Tax collections are low in Mexico. They are normally about 10 or 11 percent of GDP; we are 18 percent of GDP, not counting what we collect in the States. In order to meet its budgetary needs, Mexico makes up about 6 percent of its GDP by taking money away from PEMEX, the national oil company. That compounds PEMEX's problems of exploration and production.

Indeed, the Mexican energy situation is quite bad, and PEMEX has had no new serious finds in a good many years. At the moment, Mexico has about 10 years of proven reserves at current usage rates. PEMEX's budget has been helped recently by high prices, but that is not a full solution.

Mexico's educational structure at the primary and secondary levels is inadequate. The labor system is quite inflexible. I can go into the details, but this creates an awful lot of problems in Mexico.

People do not want to hire full-time workers because of the benefits they have to pay when they dismiss these workers. So because of the incentives built into the system, employers hire part-time workers, and about 40 percent of the total labor force is informal.

Mexico does have laws to promote competition, but in point of fact there are many, many public and nonpublic monopolies and oligopolies in Mexico. Government procurement is not always straightforward.

I have listed a bunch of things that are really, really quite serious: an inadequate fiscal system, robbing PEMEX of enough money for exploration, a weak educational system, an inflexible labor system, a system of justice that needs improvement. These are structural issues.

Alongside those, NAFTA is small potatoes. To blame NAFTA for what these issues cause pushes way beyond what NAFTA was intended to do. The one strong feature of Mexican policy in recent years, and it has been quite strong, is the financial sector.

Mexico has a strong financial sector. Government paper is investment-grade. Money flows into Mexico. Investment in Mexico is substantial. The new president, who takes office on December 1, thus

inherits deep, deep problems—and I will come back to these—that will have to be faced, but a strong financial situation.

One of the deeper weaknesses of Mexico which has not been mentioned here by others is that it may be one of the most unequal societies in the world, it and Brazil. It is now a divided country, with 35 percent voting for center left, and 35 percent center right. The victory for the center right candidate was just declared.

I just came back from Mexico City, and the Reforma and all of the main streets are still covered by tents. There are not many people in them, but they are still covered by tents.

I agree with one thing that was just said by Sandra Polaski. I think the United States should take a leaf out of European Union practice and provide more aid, not for the agricultural sector itself, I do not agree with that, but for provincial rural centers where manufacturing can take place so that workers, when they have no jobs, do not necessarily come to the United States.

Let me deal a bit with the agricultural picture. I see it quite differently from the way you have just heard. I will give you one or two numbers first. One indicator is that the rural sector of Mexico is about 23, 24 percent of the population. But this sector contributes about 6 to 7 percent of the GDP of Mexico. Translate that into the real world; it means that the people living in rural areas are quite poor and there are few opportunities for them.

The idea, when NAFTA was negotiated, was that a lot of people in agricultural areas would get jobs in the cities or in the urban centers. That proved to be wrong.

If people are living in rural areas where there is no future for them, I find quite cruel the idea of keeping them there. The Mexican negotiators felt that way as well. Unfortunately, economic growth since NAFTA has not been great, and I gave you some of the reasons for this earlier in my discussion.

Let me add a note on corn. You have already heard, the tariffs disappear in 2008. Mexicans have not really prepared for that. Many Mexicans have said they would like to renegotiate the agricultural provisions of NAFTA. I do not think they really want to do that.

I think if you take the packaged agricultural goods, Mexico's agricultural trade with the United States is probably in surplus, if you include processed products. Mexico has had a big boost in exports of fruits, vegetables, and other high-priced products. These products come from a different region than where the subsistence corn is grown.

What I believe is that, rather than renegotiate NAFTA, the Mexicans may have a case for corn, and we may negotiate some kind of agreement. Yes, we still do have side agreements, Senator, from time to time in NAFTA.

But an agreed side agreement—the sugar one was not mutually agreed to, by the way—should be possible in order to help out the corn people. It is only white corn, it is not all corn. It is only one variety of beans, not all beans. I think agreements could be worked out.

I do not want to get into what I think have been some of the political benefits of NAFTA. I think they have been great. Mexico is not an anti-American country any more. U.S. and Mexican busi-

nessmen cooperate with each other. You have just heard from some of the agricultural people, and they cooperate with each other. Government officials do, the environmentalists do the same. There is a world of difference from what existed in 1990 to what exists today in the relations with the two countries.

Now, one final note on Canada. The big issue in Canada when the free trade agreement with the United States was negotiated and went into effect in 1989—after, I think you will all remember, a difficult election in 1988—was the issue of sovereignty in a free trade agreement with the United States.

The Conservatives won. The free trade agreement with Canada went into effect. Nobody hears much any more about sovereignty in connection with free trade agreements in Canada.

In other words, I do not know all of the operations of NAFTA, but what I think NAFTA has done is to bring into the open the shortcomings of basic economic and structural policies in Mexico—not macro-economic policy, but structural policy—that need correction. If that is not done, none of the other solutions we have talked about will matter.

Thank you.

[The prepared statement of Dr. Weintraub appears in the appendix.]

Senator THOMAS. Thank you. Thanks to all of you. We will have a couple of short questions, and then we will see if we can get short answers and be on our way here, soon.

Mr. Magagna, you mentioned the situation in your written testimony, the difference in how beef trade with Canada has impacted the producers in the United States. What do you think can be done there?

Mr. MAGAGNA. Well, Mr. Chairman, I think that certainly some of that, perhaps I should say, corrected itself, but not through the right process, but unfortunately through the continuance of BSE in the Canadian cattle herd. But I think that that is a process that, again, can be corrected if we have good processes in place to deal with the disputes that arise. I spoke earlier of the failure of a process under NAFTA to address the sanitary and phytosanitary measures.

If I might take a moment to address one other, I think, outstanding example of this. This is actually with Mexico. In April of 2000, Mexico imposed a wide array of antidumping tariffs on a variety of U.S. beef products going into that country.

The U.S. called for a review under Chapter 19 of NAFTA. It took, first, 9 months for the review panel to even be appointed. It then took them 4 years to issue a decision. The tariffs have been imposed for 5 years. Under the processes allowed by NAFTA, they continued to the end of that 5th year.

The Mexican director of the economy at that point accepted a request from the cattle feeding industry in Mexico for a review of the sunset provision and, in a decision just issued 2 months ago, has reimposed virtually all of those same antidumping tariffs for another 5 years. So, clearly the process has failed us there.

It has failed us in two ways. One is that we are now facing a variety of tariffs on beef products into Mexico. You might naturally

say, well, then how have we been able to export such large volumes into Mexico?

Well, one or two companies in the U.S. have been able to effectively argue that they were not guilty of dumping, and therefore the market is open to them. Meanwhile, the remainder of the processing and distribution companies in the U.S. are facing tariffs anywhere from 3 cents a pound to 85 cents a pound.

So not only do we have antidumping tariffs being used as barriers to protect the Mexican cattle industry, but we have a distortion here within our own domestic system that is already a very concentrated system in the processing sector where basically two processors have full access to the Mexican market and the rest of our processes face stiff tariffs in going into that market. So, those are the types of things that I think need to be corrected in NAFTA.

Senator THOMAS. All right. Thank you.

Mr. Lang, you mentioned the value of exports has doubled, and so on, yet critics continue to claim that NAFTA has been devastating to agriculture. Why do you think that is the case?

Mr. LANG. Well, I do not know why they continue to say that. But I honestly believe in an integrated market system where all three countries can work together. I will give you an example of one that just recently presented itself to us at the Iowa Farm Bureau, where the pork producers from Canada were in Iowa, and they would like to put together an I-35—that is the Interstate 35—corridor for hog production.

They would like to farrow the piglets in Canada. They would like to ship them through Minnesota and Iowa, where we grow the corn, so that we can take advantage of the resources that we have in soil, appropriate weather, and rain, and they can utilize the resources they have with a certain amount of security on disease and things like that in a less populated area of Canada.

I have seen the results of a true integration of markets and the value that it brings to those subsistence farmers that both individuals to my left referred to, that in some cases the technology in agriculture allows us to move ahead, and the best result for those individuals is to seek employment somewhere else.

That employment somewhere else certainly has to be encouraged. It has to be supported in some fashion. But for Iowa growers, certainly growing the amount of corn that we do, and now with ethanol and the byproducts from ethanol, we need markets for that, and both countries provide that.

Senator THOMAS. All right. Thank you.

Senator, I will stop there. Do you have a question?

Senator BINGAMAN. Thank you very much, Mr. Chairman.

Thank you all for your testimony. Let me start by asking Ms. Polaski if she has any knowledge or view as to the issue that I had raised before with the first panel related to the NAFTA labor side agreement, this argument that Ms. Lee from the AFL-CIO has made that the labor side agreement “utterly failed to protect workers’ rights,” and she cites the 34 cases that have been filed under the side agreement that have gone nowhere. At least, that was her general characterization.

Do you have any knowledge of that or any view on that issue?

Ms. POLASKI. Senator, I do have some knowledge. When I was the Research Director at the NAFTA Labor Secretariat I was responsible for both legal and economic research, and so we followed the cases very, very closely. It is true that none of the cases have gone beyond the consultation stage, which you might call the fact-finding or job-owning stage.

In a few cases, I think that fact finding, including some public hearings that were held in the early years of NAFTA by the U.S. Department of Labor on complaints, did have some positive impact. It had the sunshine effect of calling attention to problems in Mexico, which are rife in their industrial relations system. It is quite a distorted system.

The unions, in many cases, used to be affiliated with the governing party, which is no longer the governing party, but there are these sorts of distortions in the system. As a result, many Mexican workers do not really have recourse to improve their grievances at work or their conditions at work.

The sunshine of these hearings, I think, was positive, but in many cases the problems were so serious, including very serious health and safety problems, minimum wage problems, lack of enforcement of domestic laws, discrimination against women workers for pregnancy, et cetera, that they really should have been carried further to an attempt at adjudication.

There is a very finely calibrated series of steps in the labor side agreement where you do not have to go all the way to dispute settlement right away, you can go through fact finding, you can go through an expert committee that can give advice.

That has not been utilized by any of the three countries, and I think that that has really been a missed opportunity, because there are these tensions around employment issues, around labor issues.

We have machinery in the side agreement that could be used to not only uncover problems, but to try to resolve them. It is a shame, really, that none of the cases has gone farther.

Senator BINGAMAN. Jerry, let me ask you a question about the maquiladora program. I remember a period a few years ago where there was a substantial decline in the number of people employed in maquiladora plants. That was my recollection.

And the general consensus was that a lot of the work that had been going on in maquila plants was now going to shift to China, was now shifting to China, and this was not going to be a future opportunity for job creation in Mexico.

I would be interested in your view as to what the future holds with regard to the maquiladora industry. Is this something that can continue to be competitive with manufacturing operations elsewhere? Is it something that is on the decline? What is your view on that?

Mr. PACHECO. Well, previous to 9/11, we saw a softening of the maquila industry which had not really occurred to that extent before in all of its history since 1965.

The maquila industry, at certain points, was growing up to 20 percent a year. After 9/11, that went down to 1 percent, 2 percent. It is now back up to about 5 percent growth a year, which is not 20 percent any more, but it is still a pretty healthy growth.

Now, it was a fallacy for people to say, well, the sky is falling, the maquila industry is going away. When you have the industrial base that Mexico has with the maquila industry, and for the greater part of the last 15, 20 years it has been its greatest source of export revenues—now with PEMEX and the oil prices pretty high that has switched a little bit—the maquila industry is there, and it is going to stay there. The firms that moved to China were the ones that probably should have gone to China. They were the very labor-intensive operations where Mexico, in its industrial base, is not very competitive any more.

You saw a lot of assembly operations that require very low automation go to China. The firms in the maquila industry that stayed are the ones that are moving big, bulky products, like Electrolux. Electrolux just put a big plant in Juarez, Mexico. They built 1.2 million square feet of space. They are producing I do not know how many thousands of refrigerators a day there in Juarez. But big, bulky products.

Products that are sensitive with intellectual property do not want to go to China because they are still very unsure of whether their patents, trademarks, what have you, the intellectual property, will be protected in China. Lastly, the third group of companies that I see staying and keeping the maquila industry strong are those companies that have a very tight supply chain.

When you are waiting on a 3-month lead time to get your product from China, and they are actually finishing it on the ship coming over here to try to shore up the lead time, and Mexico is our neighbor and we trade with Mexico and you can do dock-to-dock, you have suppliers in El Paso and Santa Teresa literally taking a trailer to their Mexican buyers, leaving the trailer there for a period of a half day or a day, bringing the trailer back and, thus, decreasing the cost in terms of warehousing, it is that tight supply chain that is keeping a lot of the maquila industry there and very competitive.

Senator BINGAMAN. Let me ask one general question here before I quit. This is one I will maybe direct to Dr. Weintraub and Ms. Polaski, and any of the rest of you who want to comment.

There was an interesting article on Friday in the *Financial Times* by Joe Stiglitz, who used to work around here in Washington. He had what I thought was a thought-provoking set of statements in there.

He says, “Full economic integration implies the equalization of unskilled wages throughout the world. Although this has not yet happened, the downward pressure on those at the bottom is evident. Unfettered globalization actually has the potential to make many people in advanced industrial countries worse off, even if economic growth increases.”

Do you agree with that, Dr. Weintraub, or do you think Joe Stiglitz has been in the academic world too long? What is your view?

Dr. WEINTRAUB. Well, I have been in the academic world a long time, too. In part, I agree with it. In part, I disagree with it. If there were a one-price rule around the world, if goods were traded very, very widely, or if people moved across borders very widely, that would happen exactly as he said.

But it is not happening. Goods do not move that efficiently across borders and a lot of people move, but it is not complete. In other words, while I think his tendency is right, I do not think, in the real world, it is going to happen quite that way.

Senator BINGAMAN. All right.

Dr. WEINTRAUB. Although I am one of those who thinks that the great increase in immigration of low-wage people has lowered somewhat the wages, not necessarily of everybody at the bottom, of the Americans at the bottom, and somewhat of the previous immigrants who came here. I think they have been adversely affected by immigration. I would complicate what he said, is what I am saying.

Senator BINGAMAN. All right.

Ms. Polaski, did you have a view?

Ms. POLASKI. I think even the theoretical models, going way back to David Ricardo, would show how trade can be good for both trading partners. Certainly I think no one here would dispute that trade, indeed, is good and can be good for trading partners around the world. Still, we will have winners and losers. If you look at the classical models, they do not have capital mobility.

They do not have investment flowing from one country to another. It is assumed that labor and capital stay in their own country and you only trade the goods, and therefore you will not necessarily have this downward pressure.

However, with investment flowing quite readily across borders, I think that we are seeing—and I do not think there really are any serious economists, any serious labor market scholars who do not see—that unskilled labor is under pressure everywhere in the world. I mean, we can look at the pressures in our own country. You can see it on other developing countries.

To the extent that China can produce goods for lower prices, their competitors in other developing countries put downward pressure on wages. So, I think we have to acknowledge that.

That is not to say we should not trade, but it is to say that we are going to need, at our own national level and at the international level, complementary policies that can help the people who would otherwise be losers from trade turn themselves into winners.

That was the sort of policy toward Mexico I was advocating that we consider when we come to the final phase-out of the tariffs on the crops that the very poor in Mexico produce.

Senator BINGAMAN. Good. Anybody else want to comment on it? [No response.] Thank you all very much. I appreciate you being here.

Thank you, Mr. Chairman.

Senator THOMAS. All right. Thank you.

Just one very quick question, if you can have a quick answer, Dr. Weintraub. You have studied this thing pretty closely. What has been the biggest disappointment to you in terms of putting NAFTA into use?

Dr. WEINTRAUB. Well, it has not been NAFTA, as such. I sort of agree with what several of the other panelists said. NAFTA has worked the way it was supposed to work, at least as far as increasing trade and increasing investments in Mexico. Not perfectly. There are shortcomings. There are big shortcomings.

I guess my main disappointment is with the Mexican policies where there are great disparities between the north and the south, long before NAFTA ever existed. There was great poverty in southern Mexico long before NAFTA.

My greatest disappointment is that the Mexicans did not deal with that issue in any effective way. We did not deal with that issue in any effective way. We provided no real help, for a lot of reasons which I can understand.

Because NAFTA benefitted most the areas in the northern part of Mexico where the trade takes place, the disparities have worsened, and it is now a deep issue for the incoming president.

Senator THOMAS. Sure. That is more of a problem for Mexico, I presume.

Dr. WEINTRAUB. Well, it is a problem for Mexico, and then they come up here and you have to deal with them.

Senator THOMAS. All right. Got you.

Mr. Magagna, you mentioned you might have something you wanted to bring attention to.

Mr. MAGAGNA. Mr. Chairman, that was basically the issue of the processes for dealing with antidumping that I raised partly in response to your earlier question.

Senator THOMAS. All right. Very good.

Your written statements will be included in the record. If members who are not here have additional questions, they might give them to you, and written responses will be required.

So, thank you very much. I hope we will all keep in mind that the purpose of this hearing, and the purpose of the consideration we are giving, is to find ways to help NAFTA boost the benefits that come from the agreement that we have. It is being reviewed now, of course. I think the input that you have had, hopefully, will be helpful.

So, we thank you very much for being here. Thank you for your input.

The committee is adjourned.

[Whereupon, at 3:42 p.m., the hearing was concluded.]

# **A P P E N D I X**

## **ADDITIONAL MATERIAL SUBMITTED FOR THE RECORD**

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**Submitted Testimony of Thea M. Lee  
Policy Director  
American Federation of Labor and Congress of Industrial Organizations  
Subcommittee on Trade  
of the United States Senate Committee on Finance on  
“NAFTA at Year Twelve”**

The North American Free Trade Agreement (NAFTA) was sold to the American public and American workers as a market-opening agreement that would create high-paying export-related jobs here in the United States, bring prosperity to Mexico, and spur economic growth and political stability throughout North America. The outcome has been quite different.

While it is true that trade and investment flows between the three North American countries have grown rapidly since NAFTA was implemented in 1994, on measures of much more importance to the average North American citizen, NAFTA has been a dismal failure. Workers in all three NAFTA countries have seen their wages fall or stagnate (failing to keep pace with productivity increases), as job insecurity and inequality have grown. At the same time, NAFTA rules have disadvantaged North American family farmers, many small businesses, consumers, and the environment relative to multinational corporate interests.

Rather than encouraging sustainable and equitable growth, NAFTA has contributed to the loss of jobs and incomes of workers, while enriching the very few. NAFTA's main outcome has been to strengthen the clout and bargaining power of multinational corporations, to limit the scope of governments to regulate in the public interest, and to force workers into more direct competition with each other, while assuring them fewer rights and protections. The increased capital mobility afforded by NAFTA has hurt workers, the environment, and communities in all three NAFTA countries.

### **Loss of American Jobs**

Advocates of NAFTA promised better access to a market of 90 million consumers on our southern border and prosperity for Mexico, yielding a “win-win” outcome. Yet more than twelve years after NAFTA went into effect, our combined trade deficit with Mexico and Canada has ballooned from \$9 billion to \$127 billion. The Labor Department has certified that well over half a million U.S. workers lost their jobs due to NAFTA (through 2002, when the NAFTA-TAA program was merged with other trade-displacement

programs), while the Economic Policy Institute estimates that the ballooning NAFTA trade deficit contributed to the loss of more than one million jobs and job opportunities.

Even workers who have kept their jobs have seen wages, benefits, and bargaining power eroded under NAFTA. Professor Kate Bronfenbrenner at Cornell University found that since NAFTA was put in place, employers have increasingly used the threat of shifting production to stifle union organizing drives or to block first contracts.

### **Benefits for Mexico?**

One of the main advantages of NAFTA was supposed to be that it would alleviate poverty and low wages in Mexico, helping bring the U.S. and Mexico closer together. However, on this front also, it has fallen short. Real wages in Mexico are actually lower today than before NAFTA was put in place, and the number of people in poverty grew from 62 million to 69 million (through 2003)<sup>1</sup>. The number of people crossing the border illegally is estimated to have doubled, contrary to predictions of NAFTA boosters, including then-President Salinas.

Furthermore, Mexico now faces difficult transitions in its farm sector, as the last round of NAFTA's agricultural tariffs are phased out. And the rapid maquiladora employment growth of the 1990s is fading fast, as multinational corporations shift more production to China and other low-wage locations, where workers' rights are severely repressed. These are the logical consequences of a free trade agreement that relied solely on lowering trade barriers and protecting corporate interests, but failed to build an adequate social dimension.

### **The NAFTA Model**

NAFTA undermines our laws by allowing corporations to sue governments and challenge statutes protecting the environment, public health and consumers. In some cases, corporations have even collected compensation from governments for lost profits or other damages. Legislators and ordinary citizens have no effective voice in the dispute resolution process, even though it is the laws they have voted for that are under attack.

NAFTA restricts the ability of governments to regulate services delivered across borders and by foreign investors. Under NAFTA, we have had to open the border to Mexican trucks even though we cannot ensure that each of these trucks meets our health and safety standards. Public services have been threatened as well – a case against Canada's postal service under NAFTA is still under way, and has disturbing implications for our governments' ability to regulate and support other essential public services.

NAFTA doesn't allow governments in Canada, Mexico and the U.S. to include local preferences or workers' rights criteria in making purchasing decisions. In fact, when

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<sup>1</sup> John J. Audley, Demetrios G. Papademetriou, Sandra Polaski, and Scott Vaughan, "NAFTA's Promise and Reality," CEIP, 2004.

President Clinton issued an executive order banning the federal procurement of goods made with the worst forms of child labor in 1999, he had to exclude Canada and Mexico from the order, because banning goods made by child slave labor would have violated NAFTA's government procurement provisions.

Finally, the NAFTA labor side agreement has utterly failed to protect workers' rights. None of the 34 cases filed under the side agreement has progressed beyond the initial stage of cooperative consultations, and no labor rights violators have faced any penalties under the accord. No government has paid a penny in fines, and no trade sanctions have been imposed (or even threatened). A UCLA study of the labor side agreement found that its inherent weaknesses, and a lack of political will among the parties to implement it aggressively, may doom the accord to "oblivion."<sup>2</sup>

#### NAFTA "Plus"?

On March 23, 2005, in Waco, Texas, the presidents of the United States, Mexico and Canada launched a new initiative, the Security and Prosperity Partnership for North America (SPP), to "increase security and enhance prosperity ...through greater cooperation and information sharing." While the twin goals of greater security and prosperity are ones we support, we have deep reservations about the processes set out to reach them in this instance. It appears that important decisions related to deepening economic integration among our three nations, and the well-being of our citizens, are being made by government and business elites, while civil society and Congress are sidelined.

In 2005, each nation established "Prosperity Working Groups" to consider and carry out proposals on a number of issues, including: manufactured goods and sectoral and regional competitiveness; movement of goods; energy; environment; e-commerce and information communications technologies; financial services; business facilitation; food and agriculture; transportation; and health. These working groups are supposed to consult with "stakeholders" in undertaking their activities. However, it appears that for the U.S. working groups, consultation outside of business circles has been minimal at best. The working group on manufactured goods, for example, is contemplating the integration of the auto and steel sectors of North America. There is little indication to date, however, that unions in these sectors will have any substantial input as to how such integration should be deepened.

Further evidence of the corporate domination of this process was the formation of the North American Competitiveness Council (NACC) in March 2006. The NACC was formed to discuss ways to enhance competitiveness through further elimination of regulations and other barriers to trade. The non-governmental representatives invited to participate in this council include Campbell Soup Co., Chevron, Ford, FedEx, General Electric, General Motors, Kansas City Southern Industries, Lockheed Martin Corp.,

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<sup>2</sup> Linda Delp, Marisol Arriaga, Guadalupe Palma, Haydee Urita, and Abel Valenzuela, "NAFTA's Labor Side Agreement: Fading into Oblivion?" University of California at Los Angeles, March 2004.

Merck, Mittal Steel USA, New York Life, United Parcel Service, Wal-Mart and Whirlpool.

In order for the SPP to be mutually beneficial to average citizens in North America, civil society must have the ability to participate meaningfully in these discussions. Simply submitting comments through the SPP website is not enough. Before the SPP process goes further, the task forces and councils advising our government must be expanded beyond business circles.

### **NAFTA in the Context of Broader U.S. Trade Policy**

One often-cited argument for NAFTA was that it would improve U.S. competitiveness with the rest of the world. However, since NAFTA was put in place, our overall trade deficit has also ballooned, from \$75 billion in 1993 to \$726 billion in 2005. The current account deficit hit a dangerously high 6 percent of GDP at the end of 2005, slowing any possibility of strong economic recovery and undermining the potential for future job growth. The high import propensity of the U.S. economy means that even as economic recovery gets under way, a large proportion of every dollar spent by consumers goes to purchase imports, undermining the economy's ability to generate good jobs at home.

These figures are very real to working Americans who are losing family-supporting jobs and benefits as manufacturing and even service jobs are lost overseas.

This year's trade figures reveal other startling weaknesses in the U.S. economy, even in those areas which have traditionally been considered U.S. strongholds, like services and advanced technology products. The trade surplus in services has fallen from \$92 billion in 1997 to \$56 billion in 2005. In advanced technology products, similarly, the U.S. surplus of \$4.5 billion in 2001 had turned into a whopping deficit of \$44 billion by 2005, most of that with China. The long-time U.S. trade surplus in agriculture has pretty much evaporated, including in products that compete with U.S. goods. These trends call into question the conventional wisdom that the United States enjoys a permanent and growing comparative advantage in the export of services, high-technology goods, and agriculture.

In general, the experience of our unions and our members with past trade agreements has led us to question critically the extravagant claims often made on their behalf. While these agreements are inevitably touted as market-opening agreements that will significantly expand U.S. export opportunities (and therefore create export-related U.S. jobs), the impact has more often been to facilitate the shift of U.S. investment offshore. In fact, the agreements' far-reaching protections for foreign investors directly facilitate the shift of investment, and such shifts can fairly be considered an integral goal of these so-called "trade" agreements. Much, although not all, of this investment has gone into production for export back to the United States, boosting U.S. imports and displacing rather than creating U.S. jobs.

The net impact has been a negative swing in our trade balance with most of the countries with which we have negotiated free trade agreements. While we understand that many other factors influence bilateral trade balances (including most notably growth trends and exchange rate movements), it is nonetheless striking that most of our FTAs have yielded worsening trade balances. Moreover, our overall trade balance has continued to deteriorate rapidly, even as we pursue an aggressive FTA strategy.

If the goal of these so-called “free trade” agreements is truly to improve U.S. competitiveness and open foreign markets to American exports (and not to reward and encourage companies that shift more jobs overseas), it is pretty clear the strategy is not working. Before Congress approves new bilateral free trade agreements based on the outdated NAFTA model, it is imperative that we take some time to figure out how and why the current policy has failed.

#### **Free Trade or Fair Trade?**

The AFL-CIO believes that increased international trade and investment can yield broad and substantial benefits, both to American working families, and to our brothers and sisters around the world – if done right. Trade agreements must include enforceable protections for core workers’ rights and must preserve our ability to use our domestic trade laws effectively. They must protect our government’s ability to regulate in the public interest, to use procurement dollars to promote economic development and other legitimate social goals, and to provide high quality public services. Finally, it is essential that workers, their unions, and other civil society organizations be able to participate meaningfully in our government’s trade policy process, on an equal footing with corporate interests.

NAFTA is a model that has utterly failed to deliver the promised benefits to ordinary citizens in any of the three North American countries. Yet our government is in the process of negotiating new trade agreements with dozens of countries, using NAFTA as a template.

The success or failure of any future trade and investment agreements will hinge on governments’ willingness and ability to negotiate agreements that appropriately address all of the social, economic, and political dimensions of trade and investment, not just those of concern to corporations. Unfortunately, NAFTA is precisely the wrong starting point.



U.S. SENATE COMMITTEE ON

# Finance

SENATOR CHUCK GRASSLEY, OF IOWA - CHAIRMAN

<http://finance.senate.gov>

Submitted for the Record  
 Statement of Senator Chuck Grassley  
 International Trade Subcommittee of the Finance Committee  
 Hearing on "NAFTA at Year Twelve"  
 Monday, September 11, 2006

I'd like to begin by thanking today's witnesses for appearing at this hearing. The topic of the hearing, "NAFTA at Year Twelve," is important, and the Finance Committee will benefit from your testimony. I'd like to extend a special greeting to Craig Lang, a dairy farmer from Brooklyn, Iowa, and President of the Iowa Farm Bureau, who is testifying today.

The North American Free Trade Agreement (NAFTA) entered into force on January 1, 1994. I voted in 1993 for the bill implementing this agreement because I was confident that NAFTA would provide significant benefits for the United States. I know today, more than twelve years after the implementation of NAFTA, that my vote was the right one.

NAFTA resulted in the creation of the world's largest free trade area. The lowering of barriers to trade between the United States, Mexico, and Canada, contributed to the combined 2005 gross domestic product (GDP) of the NAFTA countries of \$14.3 trillion, approximately one-third of the world's GDP. Between 1993 and 2005, total trade between the NAFTA countries grew 172 percent, and during those same years, U.S. exports to Mexico increased by 189 percent and to Canada by 111 percent. The 48 percent growth in the U.S. economy between 1993 and 2005 can be attributed, in part, to NAFTA. The level of U.S. unemployment has fallen since the implementation of NAFTA, from an average of 7 percent from 1982-1993 to 5 percent from 1994-2005, and the United States has added 22.6 million jobs since 1993.

Our NAFTA partners, Mexico and Canada, are now the largest export market for 46 of the 50 states, including my state of Iowa. In fact, 49 percent of Iowa's total merchandise exports – both manufactured and agricultural products – went to Mexico and Canada in 2005. Iowa's merchandise exports for 2005 to Mexico and Canada were \$2.4 billion above their level for 1993, an increase of about 224 percent.

As a senator from Iowa, I'm especially interested in the impact of NAFTA on U.S. agriculture. NAFTA has been, overall, very positive for U.S. farmers. Between 1992 and 2005, while U.S. agricultural exports to the world grew by 46 percent, U.S. agricultural exports to Mexico and Canada increased by an even greater 128 percent. Some 32 percent of all U.S. agricultural exports went to these two countries in 2005, up from 21 percent in 1993. Under NAFTA, U.S. agricultural exports to Canada have doubled, from \$5.3 billion in 1993 to \$10.6 billion in 2005, and have more than doubled to Mexico, from \$3.6 billion in 1993 to \$9.4 billion in 2005.

The major Iowa agricultural commodities of corn, soybeans, pork, and beef – which are also top farm products of other states – have benefited significantly from NAFTA. Between 1993 and 2005, U.S. exports of each of these products to Mexico more than doubled, and Mexico is now the largest export market for U.S. beef and the second-largest market for U.S. pork, corn, and soybeans. U.S. exports of corn to Canada more than doubled between 1993 and 2005, and soybean exports to Canada have increased by 50 percent. While U.S. beef exports to Canada dropped by over 50 percent

during that same time period, U.S. exports to Canada of another meat – pork – have grown twelve-fold. In addition, while U.S. market share in the Canadian beef market is down, Mexico became the largest export market for U.S. beef in 2004.

While the United States has benefited overall from the NAFTA, that doesn't mean that U.S. trade relations with our NAFTA partners haven't been without problems. For example, Mexico imposed a 20 percent tax on soft drinks containing high fructose corn syrup (HFCS) on January 1, 2002. This tax was designed to block exports to Mexico of U.S. produced HFCS and U.S. corn designated for processing at Mexican HFCS plants. I worked to help make sure that the United States challenged this tax through the dispute settlement process of the World Trade Organization (WTO), and the WTO determined last year that this tax indeed violated Mexico's WTO commitments. Fortunately, the United States and Mexico reached an agreement two months ago by which Mexico will eliminate its discriminatory tax. I'd like to thank one of today's witnesses, John Melle, Deputy Assistant U.S. Trade Representative for North America, for his work in seeing that this HFCS agreement was reached. In the coming months, I'll monitor steps taken to implement this agreement.

Although I hope the HFCS dispute is now behind us, some disputes between the United States and its NAFTA partners remain, and others will undoubtedly arise. Regardless, NAFTA has been, overall, a great success for the United States.

It's important to point out that our NAFTA partners have also benefited from this agreement. While both Canada and Mexico have gained from NAFTA, I'd like to focus on Mexico, given that some critics contend that NAFTA has been of little value to that country. According to the Mexico's Ministry of the Economy, Mexico's GDP has increased by 43 percent over the past ten years. Mexico added over 590,000 jobs in 2005, and it looks like the number of jobs created in 2006 could reach 900,000. Economic growth and job growth in Mexico can be attributed, in part, to NAFTA-induced increases in foreign direct investment (FDI) in Mexico. FDI in Mexico averaged \$2.1 billion from 1986 to 1993, reached almost \$18 billion in 2005, and could hit \$20 billion in 2006.

By locking in economic reforms, NAFTA has helped to bring economic stability to Mexico. Mexican families have benefited by the near disappearance of inflation, which was at just 3.3 percent in 2005, a marked drop from pre-NAFTA inflation of, for example, 159 percent in 1987. Likewise, Mexican consumers – who faced annual interest rates of 96 percent in 1987 – saw interest rates of just 9.2 percent last year.

With regard to Mexican agriculture, Mexico's agricultural exports to the United States have increased by \$5.6 billion over the past twelve years, compared with U.S. agricultural exports to Mexico increasing by \$5.7 billion during that same time period, which demonstrates that the growth in agricultural trade between the United States and Mexico has been quite balanced under NAFTA. I'd also like to note that while some critics of NAFTA claim that U.S. exports have devastated Mexican corn production, this isn't the case. Production of corn in Mexico has remained remarkably stable since NAFTA was implemented – Mexico produced 19 million metric tons of corn in 1993/94 compared to 22 million metric tons in 2004/2005. U.S. corn exports have supplemented Mexican corn production and go largely to Mexico's growing livestock industries.

Finally, the benefits of NAFTA to Mexico are more than economic. I'm convinced that there's a link between NAFTA and Mexico's significant movement to democracy following 1993. After all, free markets tend to lead to free elections.

It's clear, some twelve years after its implementation, that NAFTA has been a success for the United States, Mexico, and Canada. This agreement will continue to benefit the United States and its NAFTA partners in the coming years.

**Statement to the United States Senate Committee on Finance  
“NAFTA at Year Twelve”  
September 11, 2006**

**Craig Lang  
President  
Iowa Farm Bureau Federation**

Good afternoon. My name is Craig Lang. I'm a fifth generation farmer from Brooklyn, Iowa. My family and I farm a thousand acres of corn, soybeans, and pasture, and milk 400 head of dairy cows. I'm the president of the Iowa Farm Bureau and I also serve on the American Farm Bureau Federation board of directors and trade advisory committee. Thank you for the opportunity to speak with you about the North American Free Trade Agreement.

NAFTA has been good for most of American agriculture, and for Iowa agriculture in particular. Thanks to NAFTA, Canada and Mexico now buy a third of U.S. agricultural exports, and also supply a third of our ag imports. Japan used to be the top export market for American farm products, but now Canada is number one and Mexico is number two, followed by Japan at number three. And the United States is now the number one export market for both Canada and Mexico, as well.

Compared to 1993, the year before the NAFTA treaty went into effect, the dollar value of 2005 U.S. agricultural exports to Canada has doubled. Our two-way ag trade with Canada in 2005, both exports and imports, was up 130 percent since NAFTA. Our history with Mexico is even more impressive. Compared to 1993, last year's farm exports to Mexico had increased by 160 percent, and two-way trade was up 180 percent. It's clear that NAFTA has dramatically increased ag trade with our neighbors, by lowering tariffs and eliminating other trade barriers.

Since NAFTA, Mexico has become an important market for American grain. Soybeans, corn, and sorghum are some of our major exports to Mexico, where they are used for livestock feed. Mexico is also a promising market for corn gluten meal and distillers dried grains, the corn ethanol co-products fed to livestock. Income and population growth in Mexico means more demand for protein, so the Mexicans are buying both livestock feed for their own industry and finished meat and dairy products from the U.S. We're especially grateful for Mexican purchases of U.S. beef – since the Japanese market closed to U.S. beef in 2003, Mexico is now our number one export market for beef. And Mexican consumer preference also provides valuable markets for meat products in low demand here, such as turkey dark meat for processing into turkey “ham”, beef tripe for menudo, and pork intestines for sausage casings.

And what food products do we import from Mexico? Consumer goods and warm-climate or labor-intensive crops for which Mexico has a comparative advantage – beer and tequila, peppers and tomatoes, avocados and mangos. We American consumers benefit from lower prices and more year-round variety in fruit and vegetables because of NAFTA.

Our agricultural trade with Canada is more diversified, with processed foods and lumber and paper products as some of our top exports. Most of our ag exports to Canada are consumer-

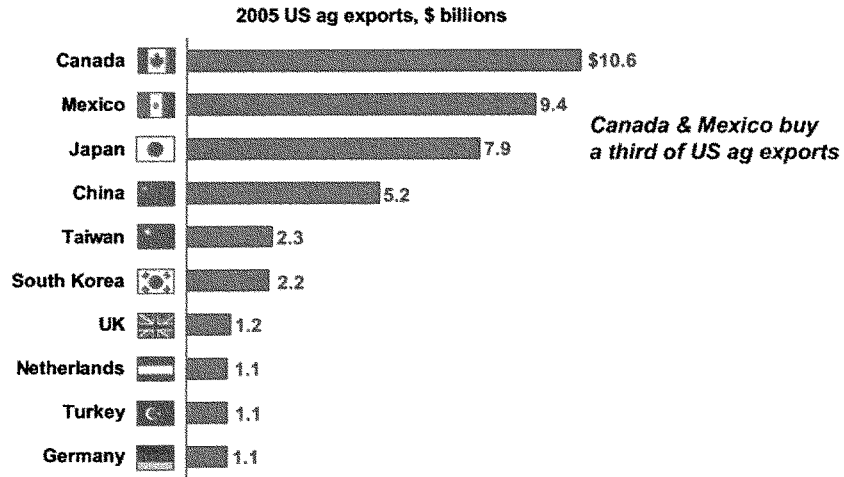
ready, high-value food products. Iowa's top ten merchandise exports to Mexico are mostly farm commodities, but my state sells mostly manufactured goods to Canada: tractors and front-end loaders, refrigerators and washing machines, processed steel. The only ag product in Iowa's top ten direct exports to Canada is soybean meal for livestock feed. But U.S. grain is also going to Canada in the form of those processed foods, and Canada is buying U.S. corn for livestock feed, ethanol production, and corn syrup production.

Iowa is the number one state in pork production, thanks in part to Canada. Only about half the hogs marketed in Iowa are born in Iowa. Iowa farmers buy baby feeder pigs from other states to fatten on Iowa corn and soybeans. (Did I mention Iowa is also number one in corn and soybean production?) But our largest single source of feeder pigs is Canada. Iowa imported almost three million Canadian piglets last year.

Our beef industry is even more integrated with Canada and Mexico, thanks to NAFTA. Last year, American cattlemen imported about one and a quarter million feeder cattle from Mexico, and about 240,000 feeder cattle from Canada. U.S. packing plants also imported almost 320,000 slaughter cattle from Canada. With these numbers of cattle crossing the borders, we have evolved into an integrated North American cattle industry that benefits ranchers, meat processors, and consumers in all three countries.

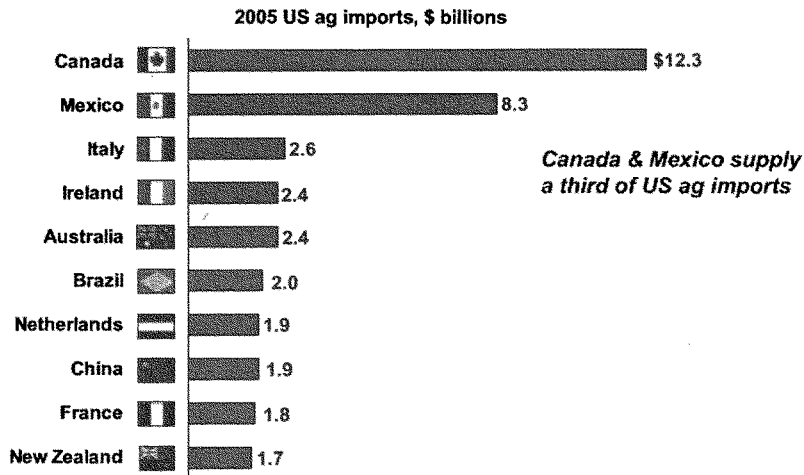
Over the past twelve years, the forecasted benefits of NAFTA have come true. Nobody can deny that the overall effect of NAFTA has been overwhelmingly positive. Our closest neighbors are American agriculture's best export customers. There is no doubt that NAFTA has helped American farmers expand export markets, and increase American farm income.

## Top ten US ag export markets



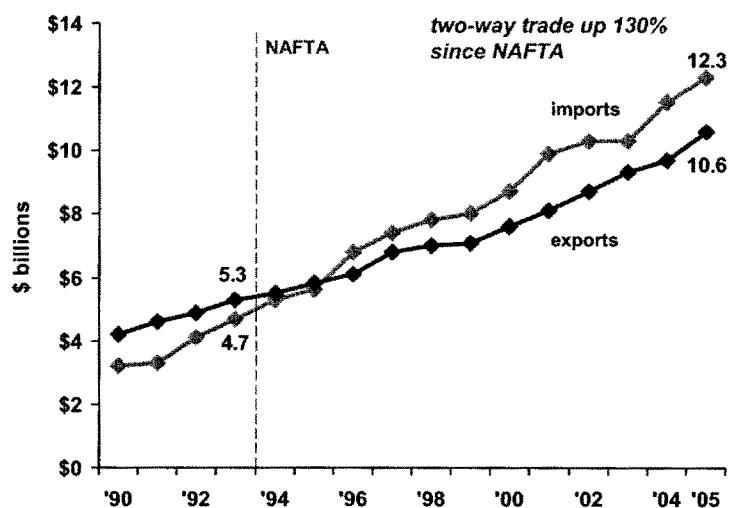
source: US Census Bureau, Foreign Trade Statistics (FATUS export aggregations) last accessed 8/06

## Top ten US ag import suppliers



source: US Census Bureau, Foreign Trade Statistics (FATUS import aggregations) last accessed 8/06

## US agricultural trade with Canada



source: US Census Bureau, Foreign Trade Statistics (FATUS aggregations), last accessed 8/06

## US ag exports to Canada, 2005

1. Misc. processed foods \$ 574 million
2. Sawn/chipped wood 529
3. Bread, pastry 455
4. Rough logs 439
5. Petfood, livestock feed 431
6. Kraft paper 398
7. Orange, fruit juices 336
8. Lettuce 296
9. Chocolate 292
10. Fresh vegetables 286

source: US Census Bureau, Foreign Trade Statistics, last accessed 8/06

## US ag imports from Canada, 2005

1. Sawn/chipped wood	\$ 6.9 billion
2. Newsprint	3.0
3. Particle board	2.8
4. Wood pulp	2.0
5. Doors/windows/trusses	1.7
6. Beef	1.2
7. Cookies, pastry	886 million
8. Crab & lobster	867
9. Pork	745
10. Chocolate	699

source: US Census Bureau, Foreign Trade Statistics, last accessed 8/06

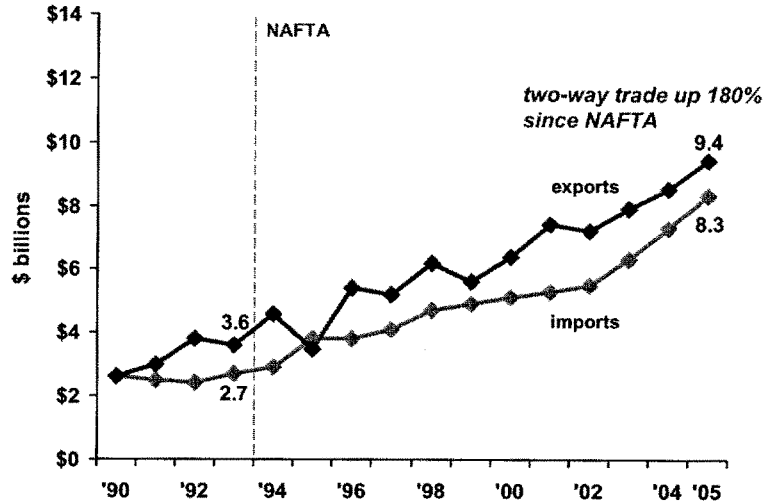
## Iowa merchandise exports to Canada, 2005

1. Tractors	\$ 158 million
2. Refrigerators	84
3. Front-end loaders	78
4. Washing machines	75
5. Rolled steel plate	69
6. Soybean meal	59
7. Rolled non-alloy steel	51
8. Chair parts	49
9. Backhoes, trenchers	49
10. Steel tubing	47

*(May not include Iowa ag products processed in or shipped via other states.)*

source: US Census Bureau, Foreign Trade Statistics, last accessed 8/06

## US agricultural trade with Mexico



source: US Census Bureau, Foreign Trade Statistics (FATUS aggregations), last accessed 8/06

## US ag exports to Mexico, 2005

1. Soybeans	\$ 855 million
2. Corn	690
3. Beef	534
4. Wheat	461
5. Turkey, chicken	410
6. Cotton	389
7. Processed foods	376
8. Cracked corn	324
9. Grain sorghum	313
10. Beef tripe, pig intestines	304

source: US Census Bureau, Foreign Trade Statistics, last accessed 8/06

## US ag imports from Mexico, 2005

1. Beer	\$1.341 billion
2. Peppers, vegetables	914 million
3. Tomatoes	781
4. Live feeder cattle	516
5. Tequila	488
6. Avocados, mangos	348
7. Shrimp	326
8. Grapes	303
9. Candy	300
10. Cookies	256

source: US Census Bureau, Foreign Trade Statistics, last accessed 8/06

## Iowa merchandise exports to Mexico, 2005

1. Corn	\$ 186 million
2. Cracked corn	108
3. Soybeans	96
4. Soy flour	58
5. Soybean meal	44
6. Refrigerator parts	24
7. Denim fabric	24
8. Corn gluten meal	22
9. Misc. steel articles	15
10. Pork intestines	15

*(May not include Iowa ag products processed in or shipped via other states.)*

source: US Census Bureau, Foreign Trade Statistics, last accessed 8/06

TESTIMONY  
OF  
JAMES H. MAGAGNA  
EXECUTIVE VICE PRESIDENT  
WYOMING STOCK GROWERS ASSOCIATION

SENATE FINANCE COMMITTEE  
SUBCOMMITTEE ON INTERNATIONAL TRADE

“NAFTA AT YEAR TWELVE”

WASHINGTON, DC  
September 11, 2006

Mr. Chairman, members of the Subcommittee. I am Jim Magagna, Executive Vice President of the Wyoming Stock Growers Association (WSGA), the 134 year old voice of the Wyoming cattle industry. I am also a life-long sheep producer and former president of the American Sheep Industry Association. I appreciate the opportunity to appear before you today to share our perspectives on “NAFTA at Year Twelve”.

My remarks this afternoon will focus on two areas that affect the livestock industry. The first of these is the evolving dichotomy with which the three nations have come to redefine the beef industry under NAFTA. Then I will focus on weaknesses in NAFTA in assuring that sanitary and phytosanitary measures are not employed as trade barriers. Beef and cattle trade between the U.S. and its NAFTA partners has been highly distorted by the outbreak of BSE in Canadian cattle and the subsequent detection of BSE in a Canadian born animal in Washington State. Unless indicated otherwise, my remarks will focus on the impacts of NAFTA prior to this distortion.

By way of background, I want to emphasize that NAFTA has provided both challenges and opportunities to livestock producers. In some northern tier states, cow/calf producers have seen increased competition for feeder cattle coming from Canadian feedlots. Southern state cattle feeders have benefited from the availability of Mexican feeder cattle to keep their lots operating nearer capacity. Wyoming has not seen any identifiable benefit from either of these opportunities.

Trade data confirms that there has been a significant increase in U.S. export of beef, in particular high value cuts, to Mexico, as a result of the reduction and removal of tariffs under NAFTA. At the same time, the supply of USDA graded beef available for both

export and domestic consumption has been significantly increased by the ease with which Mexican feeder cattle and Canadian fed cattle can be imported into our market. While several segments of the beef industry have benefited from this combination of NAFTA – enhanced market adjustments, we find no evidence that the U.S. cow/calf producer has been one of those beneficiaries.

A comparison of beef and live cattle imports/exports between the U. S and its NAFTA partners for the first ten years of NAFTA compared to the previous ten year period reveals that the combined country effects of NAFTA trade were a reduction in U.S. fed cattle prices of \$.82 cwt for fed cattle or \$330 million dollars of fed cattle revenue. U.S net beef imports (imports less exports) from Canada increased by 128% while net imports from Mexico, a much smaller market, decreased by 192%. Most directly affecting northern tier states cow/calf producers has been the impact of increased Canadian trade in fed and feeder cattle--\$1.35cwt and \$.77 respectively. This has cost the U.S industry \$980 million. It is important to recognize that this increase occurred even though U.S./Canadian cattle trade was already liberalized under terms of the Canadian Free Trade Agreement prior to NAFTA. (Source: “Post NAFTA and the U. S. Beef Market”, John Marsh, Professor, Department of Agricultural Economics and Economics, Montana State University, Bozeman).

I will address my first point on redefining the beef industry. NAFTA sought to remove agricultural trade barriers and phase out tariffs among the three signatory nations. It did not, at least in the explicit language of the agreement, call for a total integration of the respective industries of each nation that constitute the agricultural sector. U.S. cattle producers view their counterparts in Canada and Mexico as both partners and competitors. We have much to gain through strong communication, shared information and a cooperative approach in addressing disease, food safety and production issues. At the same time we must remain realistic in recognizing that we are marketplace competitors all the way from the seedstock industry to the consumer.

We recognize that certain segments of the beef industry are benefited by promoting the concept of a “North American Beef Industry”. The cow/calf segment is not one of these. For this reason, the Wyoming Stock Growers Association has been vocal in its objection to federal government references to the North American Beef Industry. We are particularly concerned with the apparent prevalence of this view in the USDA under the current administration.

Meanwhile, it has been our observation that Mexico has been vigilant in recognizing and supporting the independence of its significantly smaller and more fragile cattle industry. Canada has adeptly played their cards on integration vs. independence as they have worked their way through the current BSE crisis.

WSGA believes that critical factors that independently affect the beef industry in each nation make the concept of a single industry unrealistic, impractical and harmful. These include differences among the three nations in regulatory burdens (environmental

controls, animal welfare requirements, labor laws, etc.), economic policy and political philosophy.

Our expressed concern with the perspective of North American Beef Industry does not call for specific revisions to the NAFTA agreement. However, it does beg for specific direction to those who represent the U.S in discussion of possible changes to NAFTA as well as to those responsible for U.S. agricultural policy. We urge this subcommittee to play a leading role in providing that direction.

I will now turn my attention to the issue of the application of sanitary and phytosanitary provisions contained in NAFTA. Article 712 (1) provides that , " *Each Party may, in accordance with this Section, adopt, maintain or apply any sanitary or phytosanitary measure necessary for the protection of human, animal or plant life or health in its territory, including a measure more stringent than an international standard, guideline or recommendation.*" Article 715 requires that such measures be based on scientific principles and appropriate risk assessment.

Perhaps recognizing the temptations that would exist, a subsequent provision in Article 15 entitled "Disguised Provisions" warns, *No Party may adopt, maintain or apply any sanitary or phytosanitary measure with a view to, or with the effect of, creating a disguised restriction on trade between the Parties.* WSGA believes that in fact sanitary and phytosanitary measures have been used by our NAFTA partners in a manner that constitutes trade restrictions.

We have repeatedly seen the government of Mexico close its borders for a period of time to the importation of sheep and to import of specific variety meats from the U.S. Animal health and food safety concerns have been presented as justification for such actions. While we do not challenge the sovereign authority of a NAFTA nation to take any such actions, we do not believe that these actions have been fully supported by sound science or acceptable risk analysis.

NAFTA should move member nations toward a harmonization of sanitary and phytosanitary standards. Over the first eleven years of NAFTA we did not achieve this goal in our relationship with Canada. Repeated efforts by the U.S. cattle industry to achieve removal of scientifically unjustified restrictions on the import of U.S. cattle based on bluetongue and anaplasmosis restrictions were unsuccessful. These restrictions could not be defended based on sound science or a defensible risk analysis. They have finally been relaxed this year. It is apparent to us that this relaxation was undertaken to encourage a more favorable U.S. industry response toward further opening of the border to imports of Canadian live cattle, not in an effort to comply with NAFTA's provisions.

We acknowledge that, since the discovery of BSE in Canadian cattle, some within the U.S. cattle industry have sought to utilize animal health and food safety concerns as an economic tool to achieve trade restrictions on the import of Canadian beef and/or live cattle into the U.S. While their motives may be subject to challenge, there should be little doubt that the restrictions that have been imposed are compliant with the terms of

NAFTA cited above. Given the ongoing discovery of BSE infected animals in Canada, WSGA believes that the U.S has been lenient in the exercise of its rights under Chapter Seven of NAFTA.

In response to the above concerns, WSGA urges that the USTR seek amendments to Chapter 7 of NAFTA that will identify more precisely the criteria that would authorize a member country to impose sanitary or pytosanitary standards that are more restrictive than those established by recognize international standards organizations. The role of the Committee on Sanitary and Phytosanitary Measures should be strengthened in overseeing and responding to the activities of the parties in this area.

I would also call to the Committee's attention the extent to which other nations have utilized animal health and food safety issues as trade barriers. The continued response of numerous nations, most notably Japan and south Korea, to the discovery of a Canadian-born BSE infected cow in the U.S. and the subsequent discovery of a single U.S.-born infected animal have been based on neither international guidelines nor defensible science and risk analysis. WSGA urges the USTR to ensure that future trade agreements contain strict enforceable criteria for the determination of justifiable sanitary and phytosanitary import restrictions. Most importantly, these agreements should require the harmonization of such standards.

Mr. Chairman, the U.S. cattle industry has a bright future based on our ability to remain the supplier of choice to domestic beef consumers and strong continued growth in our exports. To achieve these goals we are committed to producing a quality product in an environmentally sustainable manner. We ask your assistance in assuring that U.S. trade negotiators provide us with increased access to export markets on terms that are no more restrictive than those that we grant to other nations.

Again, thank you for the opportunity to testify today. I will be pleased to address any questions the committee members may have.

As prepared for delivery

**Statement of  
John M. Melle  
Deputy Assistant U.S. Trade Representative  
For North America  
before the  
Committee on Finance  
of the  
United States Senate  
September 11, 2006**

Mr. Chairman, Members of the Committee:

Thank you for the opportunity to appear before the Committee today. I am pleased to represent the Office of the United States Trade Representative and provide an overview of our trade and investment relationship with our NAFTA partners, Canada and Mexico.

The North American Free Trade Agreement (NAFTA) has defined our commercial relationship with Canada and Mexico since its entry into force on January 1, 1994. The NAFTA is a comprehensive trade agreement, covering trade in goods, services and investment, as well as government procurement, intellectual property rights, standards, and dispute settlement. Twelve years after implementation of the NAFTA began, essentially all of the agreement's transitional implementation periods are now complete with the exception of a handful of tariffs that fall to zero on January 1, 2008.

In evaluating the impact of the NAFTA on both the United States and its partners, the appropriate place to start is with trade and investment flows.

- For goods, our total trade (imports plus exports) with Canada and Mexico has more than doubled from pre-NAFTA levels. Growth in trade with our NAFTA partners exceeds growth with the world as a whole. Mexico has passed Japan to become our second largest trading partner and export market, trailing only Canada.
- There has also been a qualitative transformation in goods trade; in the 1980s, 80 percent of Mexico's exports were oil and raw materials. Today, value-added manufactured goods account for 90 percent of Mexico's exports, an indicator that Mexico has joined the United States and Canada as part of a continent-wide market of producers and consumers.
- Much of the recent concern about NAFTA is with agriculture. In fact, growth in agricultural trade has paralleled growth in total trade since 1994. U.S. agricultural exports to Canada and Mexico have grown by 98 percent since 1994, nearly matching the 101 percent total growth in U.S. total exports to those countries over the same period. Canada and Mexico are our top two agricultural export markets.
- Many of the most impressive export successes for the United States are also agricultural. Mexico is our largest market for a wide range of products – beef, dairy, swine, rice,

turkey, apples, soymeal, sorghum, and dry beans among them. Our share of Mexico's imports is above 90 percent, due in part to the preferential access we have under the NAFTA for five of these seven products. In 2005, Mexico was also our second largest market for corn, port, poultry meats, soybeans, wheat, and pears.

- NAFTA has solidified Canada's position as our largest trading partner. More trade crosses the Ambassador Bridge between Detroit and Windsor than moves between Spain and France.<sup>1</sup>
- U.S. exports of services to Canada and Mexico have grown by 75 percent since 1993. In 2004, the last year for which we have complete data, the United States exported \$47.7 billion in private commercial services to our NAFTA partners, and maintained a trade surplus of \$14.2 billion.

As a result of the NAFTA and the earlier bilateral free trade agreement, the phase-out of tariffs between the United States and Canada was completed on January 1, 1998, except for tariff-rate quotas which Canada maintains on certain supply-managed agricultural products. Nearly all of the NAFTA tariff cuts with Mexico have been implemented, except for the handful of remaining items whose tariffs will be eliminated in 2008. Since 1994, the average U.S. duty on Mexican goods has fallen to about 0.1 percent in 2005. Mexico's duties on U.S. goods are even smaller -- 0.003%.

By establishing a framework to promote a secure and predictable environment, investment in each of the NAFTA countries have grown. The NAFTA partners are investing more in each others' economies, and the rest of the world is also investing more in our economies.

- This change is especially important for Mexico. Since 1994, annual Foreign Direct Investment (FDI) inflows have averaged \$15 billion, compared to less than \$3 billion in the 1980s. Mexico's outward FDI flows have increased fourteen-fold since 1990, and it is now one of the largest developing country overseas investors.
- The United States accounts for approximately two-thirds of total foreign direct investment in Canada. U.S. investment is concentrated in the manufacturing, finance, and mining sectors.
- Investment growth in Canada and Mexico has not come at U.S. expense. Even excluding housing, U.S. business investment has risen by 104% since 1993, compared to a 37% rise between 1981 and 1993.

How much the NAFTA affected the changing trends in goods and services trade and investment cannot be measured precisely. This is especially true when looking at broader measures of economic performance since the NAFTA entered into force. However, there are a wide range of economic indicators that have grown more rapidly since the NAFTA was implemented.

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<sup>1</sup> Derived from GAO report 02-595R, page 1 and the CIA World Factbook.

- For the United States, job creation, industrial production, real compensation for manufacturing workers, business productivity and investment have all increased by higher rates in the period since 1993 compared with prior years.
  - U.S. employment rose from 112.2 million in December 1993 to 134.4 million in December 2005, an increase of 22.2 million jobs, or nearly 20 percent. The average unemployment rate was 5.1 percent in the period 1994-2005, compared to 7.1 percent during the period 1982-1993.
  - U.S. industrial production – 78 percent of which is manufacturing – rose by 49 percent between 1993 and 2005, exceeding the 28 percent increase achieved between 1981 and 1993.
  - Growth in real compensation for manufacturing workers improved dramatically. Average real compensation grew at an average annual rate of 2.3 percent from 1993 to 2005, compared to just 0.4 percent annually between 1987 (earliest data available) and 1993.
- U.S. business sector productivity rose by 2.6 percent year between 1993 and 2005, or by a total of 36.2 percent over the full period. Between 1981 and 1993 the annual rate of productivity growth was 1.8 percent, or 24.3 percent over the full 12 year period.
- Mexico has seen consistent GDP growth - 40 percent since 1993 - and annual real wage growth since 1995. This has been accompanied by much lower interest rates and rapid development of consumer finance services, such as home mortgages that have created a boom in consumer lending and home purchases.
- Real GDP in Canada grew from C\$773.5 (1997 Canadian dollars) in 1993 to C\$1,157.7 in 2005, an increase of nearly 50 percent. Real Canadian GDP per capita surged by 33 percent over the same period. Canadian unemployment fell from 11.2 percent in 1993 to 6.7 percent last year.<sup>2</sup>

#### **NAFTA's Ability to Respond to Changes**

The NAFTA remains a vibrant agreement, one that has been able to respond to changes in production methods and sourcing arrangements. For example, the NAFTA establishes schedules for the elimination of tariffs, but the agreement also allows the Parties to accelerate the elimination of tariffs. Since the entry into force in 1994, the NAFTA partners have accelerated the elimination of tariffs four times, in 1997, 1998, 2000 and 2001. The total value of trilateral trade covered by these four rounds of tariff cuts is approximately \$28 billion.

Over time, manufacturers often change the way they design and build products. They choose new suppliers, change the materials used in the production of a good, or improve their products by using new parts. Since 2002, the NAFTA partners have worked to update the NAFTA rules

<sup>2</sup> See "Economic Indicators," on the website of the Department of Foreign Affairs and International Trade, [http://www.international.gc.ca/eet/pdf/economic\\_indicators-en.pdf](http://www.international.gc.ca/eet/pdf/economic_indicators-en.pdf)

of origin, the regulations that specify which goods are eligible for preferential treatment under the agreement. These changes have allowed U.S. companies to export their products duty-free to our NAFTA partners, saving thousands, sometimes millions of dollars in duties. The NAFTA partners have implemented three sets of changes to the rules of origin, in 2002, 2004 and 2006. The total value of trade covered by these changes exceeds \$39 billion. We are working to implement a fourth set of changes in 2007.

#### **Recent Successes**

In 2006, the United States has resolved a number of our thorniest trade issues with Canada and Mexico.

- In January, the United States and Mexico signed a bilateral agreement on trade in tequila, which will ensure that U.S. bottlers can continue to import tequila in bulk form. The agreement imposes no obligations on the United States beyond current practice.
- In March, the United States and Mexico signed an agreement to promote bilateral trade in cement. The agreement will allow for additional supply of cement at a time of strong domestic demand following the devastation of Hurricanes Katrina and Rita. The agreement also ends all NAFTA and WTO litigation on cement from Mexico, which had stretched back 16 years.
- In July, the United States and Canada reached final agreement on softwood lumber, a dispute that has dogged trade relations for 20 years.
- In August, the United States and Mexico reached an agreement on trade in sweeteners, which puts the two countries on a glide path towards full implementation of the NAFTA sugar provisions in 2008. Mexico agreed to remove its beverage tax and duties on drinks sweetened with high fructose corn syrup and other non-sugar sweeteners, and the United States agreed to an increase in the amount of duty-free sugar that Mexico is allowed to export to the United States. Mexico is providing duty-free access for an equivalent volume of high fructose corn syrup (HFCS).

#### **Current Challenges**

To address the challenges the NAFTA framework faces today and in the future, there are three circumstances to consider.

The first is implementation of the remaining NAFTA commitments by January 1, 2008.

As I mentioned earlier, all tariff cuts between the United States and Canada have already been implemented, and the remaining tariffs between the United States and Mexico will be eliminated on January 1, 2008. While less than one percent of our NAFTA trade with Mexico remains subject to duties, final removal of these duties has raised concerns in some sectors. As the three NAFTA trade ministers made clear at their annual oversight meetings in Mexico this past March, they are committed to full implementation of the NAFTA and will not consider any reduction to our NAFTA obligations.

A second set of challenges must take into account the changes in global trade since the NAFTA entered into force. Simply put, each of the NAFTA partners have been reducing trade barriers with other countries, meaning the margins of preference provided by the NAFTA are shrinking.

- In 1993, for example, the average United States duty on imports from all countries in was 3.2 percent. By 2005, it had fallen to 1.4 percent. Mexico still has a larger margin of preferential access today than it did before NAFTA implementation began, but it has begun to fall.
- The United States also faces more competition in the Mexican and Canadian markets: Mexico has free trade agreements with 42 other countries today, compared with one (Chile) in 1994. Canada has concluded three additional FTAs since 1994, and is currently engaged in negotiations with the Republic of Korea.
- And, of course, all three countries face the challenge of increased competition with economies such as China and India.

A third set of challenges is how to best address today's security concerns while not creating trade barriers. This is the fundamental challenge of the Security and Prosperity Partnership of North America, a trilateral initiative launched in March 2005. The SPP seeks to enhance the security, prosperity, and quality of life for the citizens of all three countries while respecting the sovereignty and unique cultural and legal heritage of each country. The SPP builds on and complements the NAFTA, and we can use both processes to advance common strategic North American goals. For example, under both the NAFTA and the SPP, USTR is soliciting proposals from U.S. industries to liberalize and simplify NAFTA Rules of Origin, making it easier to use the benefits of the duty-free access that the NAFTA provides.

To conclude, with the NAFTA firmly in place, the United States and its NAFTA partners have not only become better customers for each other but better neighbors, more committed partners, and effective colleagues in a wide range of trade-related international organizations.

I am pleased to answer any question you may have.

**Senate Finance NAFTA Hearing  
September 11, 2006**

Additional comments from John Melle in response to questions from Senator Bingaman:

**Labor Petitions**

Senator Bingaman stated that for the thirty-four submissions filed under the North American Agreement on Labor Cooperation (NAALC) since the NAFTA entered into force, none have advanced beyond the "first stage."

Labor rights' matters under the NAALC can be addressed at several levels. The NAALC called for each country to establish a National Administrative Office (NAO) to serve as a point of contact between the countries on labor matters. The NAOs' responsibilities include to receive and review public submissions and to consult on labor law matters. As of October 19, 2006, the three NAOs have received 35 public submissions, which were subject to review and NAO-level consultations. Specifically, for the 35 submissions received, 21 were accepted for review, 9 were rejected, 4 were withdrawn, and 1 remains pending. Of those reviewed, public hearings were held regarding 16 submissions. For 15 submissions, the next step in the process, Ministerial-level consultations between the governments, took place.

Ministerial Consultations have led to intensive dialogue between the governments, and, in several cases, the entering into of Implementation Agreements or Joint Declarations between the Ministers of Labor. Under these Agreements and Declarations, the governments have reaffirmed their commitments under the NAALC, issued public pronouncements concerning the application of labor law, agreed to undertake training, outreach, and education efforts to improve labor law enforcement, and committed to bilateral and multilateral cooperative programs to address enforcement shortcomings. Seven of the eight U.S. requests for Ministerial Consultations have resulted in such Agreements or Declarations and one remains pending.

Subsequent steps in the NAALC process, a report from an Evaluation Committee of Experts and, for submissions concerning occupational health or safety, child labor, and minimum wage, formation of an arbitral panel, have not been reached to date. Thus far, the three governments have felt sufficiently satisfied with the outcome of Ministerial Consultations so as not to warrant taking further steps under the NAALC processes.

Additional Background

Thirty-five submissions have been filed under the North American Agreement on Labor Cooperation (NAALC). Twenty-one were filed with the U.S. NAO of which 19 involved allegations against Mexico and two against Canada. Nine were filed with the Mexican NAO and involved allegations against the United States. Five submissions have been filed in Canada, three raising allegations against Mexico and two raising allegations against the United States.

Sixteen of the twenty-one submissions filed with the U.S. NAO involved issues of freedom of association and eight of them also involved issues of the right to bargain collectively. Two submissions concerned the use of child labor, one raised issues of pregnancy-based gender discrimination; three concerned the right to strike; five concerned minimum employment standards; and seven raised issues of occupational safety and health.

Of the submissions filed to date with the U.S. NAO, four were withdrawn by the submitters before hearings were held or the review process completed. Hearings were held on ten. Eight of the U.S. submissions have gone to ministerial-level consultations. The U.S. NAO declined to accept six submissions for review. Five Mexican NAO submissions resulted in ministerial consultations. Two Canadian NAO submissions resulted in ministerial consultations with Mexico. Canada declined to accept three submissions.

Trilateral Summary:

Total number of submissions: 35  
Submissions that a country declined to accept: 9  
Submissions withdrawn before the process was completed: 4  
Submissions that resulted in public hearings: 16  
Submissions that resulted in ministerial consultations: 15

**Cattle Exports to Mexico**

Senator Bingaman noted that Mexico had not imported a single live animal from the United States so far in 2006. Melle responded that breeding bulls had been entering Mexico for several months and promised verification of that fact, and an update on dairy heifers.

Additional information:

On May 8, USDA (APHIS) sent its official acceptance of Mexican requirements for the shipment of U.S. dairy breeder cattle into Mexico. A small number of dairy breeding cattle have been exported following the agreement.

Following the Senate Finance hearing, on September 20, 2006 USDA received word that SAGARPA has accepted USDA's proposal for the importation of U.S. dairy heifers. Under the proposal, animals will be inspected at the farm of origin by APHIS federally accredited veterinarians, and Mexican approved veterinarians will conduct inspections at U.S. pens in Texas, New Mexico and Arizona. The understanding was effective on October 4, and USDA began endorsing health certificates. We understand shipments of U.S. dairy cattle to Mexico will start later this month, many via St. Teresa, New Mexico.

**TESTIMONY  
JERRY PACHECO  
EXECUTIVE DIRECTOR  
INTERNATIONAL BUSINESS ACCELERATOR**

Mr. Chairman and members of the committee:

It is an honor and privilege for me to be asked to provide you with some of the personal insight that I have gained pertaining to the North American Free Trade Agreement (NAFTA) throughout the years working with both U.S. and Mexican companies along the U.S.-Mexico border. I especially want to thank New Mexico Senator Jeff Bingaman for his support and cooperation throughout these past years on trade-related matters.

As an American, I have lived and worked in Mexico for the past 16 years in both the public and private sectors. During this time, I have been a state government official directing the State of New Mexico's Mexico City Trade Office (1991 to 1994). In this capacity, I was responsible for assisting New Mexican companies wishing to break into the Mexican market, with the goal of increasing my state's exports to Mexico. During this period of time as part of a group of expatriates working in Mexico, I also lobbied in favor of NAFTA.

Subsequently, I have worked as an international banker, with a focus on Mexico; a private consultant working on behalf of Mexican and American firms wishing to explore their market in either the U.S. or Mexico; part of a real estate development group that built more than 2 million square feet in three industrial parks surrounding the Santa Teresa Port of Entry – in this capacity, I was responsible for recruiting companies supplying Mexico's maquiladora (twin plant industry) and/or importing finished goods from Mexico and distributing them throughout the world; a professor of international business and marketing for institutions of higher education in both the U.S. and Mexico; and a journalist with a syndicated international trade column, "*Business Across Borders*," that appears in the southwestern U.S. and northern Mexico.

Currently, I manage the International Business Accelerator, a non-profit import/export international trade counseling center that is part of the New Mexico Small Business Development Network. The Accelerator helps New Mexican businesses take their product/service to the global market. We have offices in Santa Teresa, New Mexico (on the western edge of El Paso Texas) and in Chihuahua City, Chihuahua, Mexico (approximately 230 miles south of the border). The El Paso/Juarez/southern New Mexico border complex is the largest industrial base on the entire US-Mexico border.

I would like to briefly examine NAFTA from the standpoint of both large U.S. industrial concerns and smaller companies in the context of trade with Mexico, since this has been my focus throughout the years. From a large company standpoint, NAFTA facilitated the entry, which was previously difficult or at times impossible, into the Mexican market. It's true that previous to the 1994 implementation of NAFTA, U.S. firms such as Ford,

General Motors and Citibank had been actively doing business in Mexico. With the advent of the maquiladora program in 1965, it became more and more common to see U.S. firms producing in Mexico. However, this did not necessarily mean that these firms could sell their products into Mexico nor break into restricted Mexican markets.

NAFTA attempted to lower tariff and non-tariff trade barriers between the three NAFTA partners with the objective of creating a North American Free Trade Block. According to the U.S. Department of Commerce International Trade Administration, U.S. exports to Mexico during the first 10 years of NAFTA rose by 106%. From 1994 to 2002, Mexican foreign direct investment in the U.S. grew by 280%, as compared to growth of 185% by non-NAFTA countries during this period of time.

I have seen first-hand the effect that NAFTA has had in providing accessibility to large U.S. firms wishing to export their products to Mexico. My old real estate development group recruited to our three industrial parks in Santa Teresa approximately 35 companies for which we built more than 2 million square feet of industrial space. Almost all of these firms are supplying manufacturers or distributors in Mexico. Approximately 1,500 direct jobs and possibly three to four times this many indirect jobs were created by these companies in southern New Mexico, one of the poorest regions in all of the U.S. American companies account for the largest portion of Mexico's imports, and NAFTA has facilitated this flow of goods and services south.

From the standpoint of the smaller companies (manufacturers, distributors and service providers) the biggest effect that I believe NAFTA has had is creating an interest in exploring business in Mexico that previously did not exist. In other words, NAFTA encouraged smaller businesses to look at Mexico as a viable market where they could explore new commercial opportunities. Having worked assisting smaller companies in the pre-NAFTA period, it was extremely difficult to generate any export successes, due to the previously closed economy that Mexico presented to foreign companies. Smaller companies simply did not have the resources to overcome all of the barriers that the Mexican market presented. Today, my non-profit trade counseling center is inundated with requests from smaller New Mexican companies hungry to explore opportunities south of the border; and by Mexican companies exploring joint venture opportunities with U.S. counterparts.

For both large and small U.S. companies, NAFTA has lowered the tariff barriers that made doing business in Mexico infeasible. In my experience, the removal of tariffs from a customs schedule is clear and understandable. What is hard to eradicate and continues to pose a serious threat to the fulfillment of NAFTA is the continuing presence of what are referred to as non-tariff barriers. At the border, we commonly refer to these as bottlenecks. These can take the form of congestion at the ports of entry, confusion over proper documents needed to cross merchandise across borders, uncertainty over work visa permits, and inconsistent cargo inspections among others.

According to the U.S. Department of Commerce, total two-way trade between the U.S. and our NAFTA partners grew by 111% between 1993 and 2003. This occurred despite

the fact that Mexican commercial trucks coming to deliver merchandise in the U.S. market cannot go further than a thin border commercial zone north of the U.S. border. Truck drivers and their cabs have to cross into the U.S., unhitch their trailers with their cargo, and have an American driver and cab deliver the merchandise to its final destination in the U.S. A similar situation exists for American drivers attempting to deliver their merchandise to destinations in Mexico. This extra process adds time and costs to the logistics chain, which results in extra costs to the manufacturers/distributors. These costs are then passed on to the consumer. Of course we want safe Mexican trucks on our highway - we don't want to endanger U.S. citizens with unsafe trucks on our roads. I can say this with certainty because I live within the border commercial zone. My wife Loretta and son Joseph are on the freeways side-by-side with Mexican trucks on a daily basis, and I certainly don't want them put in harm's way. However, restricted trucking continues to remain a bottleneck that impedes the free flow of trade.

A particularly positive development in terms of the expediting of cargo, while at the same time addressing security, is the Fast and Secure Trade (FAST) program that is managed between the private sector and the Bureau of Customs Protection, under the aegis of the Customs-Trade Partnership Against Terrorism. In this program, qualified manufacturers, distributors and logistics firms commit to securing shipments against terrorist activities and contraband from the time the product is made to the time it is delivered. Participating companies and their employees undergo background checks, and appropriate monitoring procedures are used to secure the shipments. Trucks participating in this program are then allowed to use a special FAST crossing lane for expedited crossings. This program is becoming more and more popular along the border, and holds a lot of promise for combating illegal activities and congestion at the ports of entry.

Another bottleneck relates to work visas. If trade has increased more than 100% among the NAFTA partners, shouldn't we expect businesspeople in the three countries to require more mobility to travel and work throughout North America? NAFTA created a special temporary work visa for Canadian and Mexican citizens wishing to work in the U.S. called the TN visa. At face value, this was supposed to allow qualified Canadians and Mexicans to work in the U.S. After twelve years, the TN visa program appears to have worked for Canadians. According to the Department of Homeland Security's Office of Immigration Statistics, from 1996 to 2005 almost 700,000 TN visas were issued for Canadians to work in the U.S. This averages more than the current total annual 65,000 cap on H-1B visas

During this same period of time, Mexican workers were issued about 20,000 TNs, an average of fewer than 2,000 per year. Many employers don't want to go through the paper-heavy, time-consuming bureaucratic process of sponsoring a Mexican employee. By and large, TN applicants are required to have specific skills according to the list of acceptable TN professions. Many of the Mexicans who don't qualify for any of these categories still wish to come to the U.S. to work in unskilled and labor-intensive positions. In general, the TN visa is not structured to accommodate these workers, and therefore, many enter the U.S. illegally and live on the lam, working for American companies that desperately need labor.

I myself have gone through the TN process to sponsor a trade specialist employee for my firm, who assists me in providing consulting services for our clientele. By the time we had finished the application process, we had created a book the size to rival *War and Peace*. This was not a pleasant experience. In my opinion, and hindsight is 20-20, this is one of the perplexing aspects of NAFTA – if we realistically want to create a North American Free Trade block so that we can remain competitive against other regions of the world, can we realistically expect to do this without some type of viable work visa program?

The retraining of workers negatively affected by NAFTA has been a rocky road at best. Many workers or companies do not know that retraining funds are available, and if companies are aware of this assistance, it can be hard for them to prove that a multilateral agreement such as NAFTA has negatively affected their welfare. Oftentimes, companies simply close shop and the employees are thrown out on the street to collect unemployment benefits without realizing that they are entitled to retraining funds. In my experience, this issue has impacted both small and large U.S. businesses.

At precisely the time that NAFTA was implemented, the U.S. Department of Commerce (DOC) was put on tighter reins in terms of assisting businesses. It went to a cost-recovery system of providing its services. In other words, it started charging for services that previously were provided for free. DOC trade specialists are now required to be oriented to the sale of services, and are rated on total revenues generated. Many smaller companies wishing to explore their markets that previously could approach the DOC cannot afford or are not willing to pay for these services. If we believe that increasing U.S. exports and exploring global opportunities for smaller U.S. businesses is a good thing, why was the DOC reoriented the way it was? The DOC remains one of my favorite resources to assist companies exploring their international markets. However, I don't believe that it is as user friendly as before. The potential for this organization to increase its impact on the small business sector is great, but more along the lines of how it operated before.

Fifteen years after having become involved in supporting NAFTA, and 12 years of having worked during the course of the implemented agreement, I still believe that the agreement has brought more positive than negative results to the U.S., especially in terms of increased exports and the creation of export-based jobs. Everyday, I work in the trenches on the U.S.-Mexico border assisting U.S. companies wishing to sell their products and services in Mexico. We have had export successes to Mexico with clients involved in telecommunications systems, high-technology products, and automotive accessories. Without NAFTA, the majority of our clients would not have been able to expand their markets or create the new jobs that currently exist in my state due to this agreement. From 1993 (the year before NAFTA was implemented) to 2005, the state of New Mexico's exports to Mexico more than quadrupled. Similar results have occurred in an overwhelming number of U.S. states.

By no means is NAFTA perfect – many issues need to be addressed. However, we can learn from the positives and negatives of NAFTA in order to better structure future U.S. trade agreements with the objective of creating new opportunities for U.S. companies and new jobs for Americans.

TESTIMONY SUBMITTED TO THE SENATE SUBCOMMITTEE ON INTERNATIONAL TRADE  
OF THE COMMITTEE ON FINANCE

**THE EMPLOYMENT CONSEQUENCES OF NAFTA**

BY  
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**SEPTEMBER 11, 2006**

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*Main Findings*

- Employment is the main source of household income for a large majority of the population in all the countries of North America. Therefore, one of the most basic measures of a trade agreement's impact on the well-being of real people is the number of jobs gained or lost as a result of the agreement and the quality of those jobs. NAFTA's most significant impact on employment has been felt in Mexico.
- NAFTA has produced a disappointingly small net gain in jobs in Mexico. Data limitations preclude an exact tally, but it is clear that jobs created in export manufacturing have barely kept pace with jobs lost in agriculture due to imports. There has also been a decline in domestic manufacturing employment, related in part to import competition and perhaps also to the substitution of foreign inputs in assembly operations.
- Mexican agriculture has been a net loser in trade with the United States, and employment in the sector has declined sharply. U.S. exports of subsidized crops such as corn have depressed agricultural prices in Mexico. The rural poor have borne the brunt of adjustment to NAFTA and have been forced to adapt without adequate government support.
- Productivity has increased in Mexico over the last decade. NAFTA likely played a significant role, because Mexico cut tariffs deeply and was exposed to greater

competition. The desirable growth in productivity may have had the unwanted side effect of reducing the rate of job growth, since fewer new jobs were created as workers already on payrolls produced more.

- Real wages for many Mexicans today are lower than when NAFTA took effect. The stunning setback in wages is mainly attributable to the peso crisis of 1994-1995. However, during the NAFTA period, productivity growth has not translated into wage growth, as it did in earlier periods in Mexico. Mexican wages are also diverging from, rather than converging with, U.S. wages.
- Income inequality has been on the rise in Mexico since NAFTA took effect, reversing a brief declining trend in the early 1990s. Compared to the period before NAFTA, the top 10 percent of households have increased their share of national income, while the other 90 percent have lost income share or seen no change. Regional inequality within Mexico has also increased, reversing a long-term trend toward convergence in regional incomes.
- The experience of Mexico confirms the prediction of trade theory, that there will be winners and losers from trade. The losers may be as numerous as, or even more numerous than, the winners, especially in the short-to-medium term. In Mexico, more farmers lost than gained from NAFTA-induced changes.
- In the United States, NAFTA has likely had either a neutral or very small net positive effect on employment.
- Because the net impact of NAFTA on overall employment in the United States is small, the impact on wages is also likely to be minor at the national level. But a widening gap between the wages of skilled and unskilled workers is partly attributable to trade, and NAFTA probably accounts for a small portion of the observed growth in wage disparity within the United States.
- There has been a decoupling of productivity growth from wage growth in the United States over recent decades. Increased trade and outsourcing of employment has led to a weakening of US workers' bargaining power and NAFTA is one factor, among many, causing that effect.
- In Canada, NAFTA's predecessor, the Canadian US Free Trade Agreement, led first to a significant net decrease in jobs in traded sectors, followed by a slow recovery of employment to pre-CUFTA levels after ten years, then a modest continued increase in subsequent years.

### *The Employment Consequences of NAFTA*

Employment is the main source of household income for a large majority of the population in all the countries of North America. Therefore, one of the most basic measures of a trade agreement's impact on the well-being of real people is the number of jobs gained or lost as a result of the agreement and the quality of those jobs. A second important and closely related measure is the effect of trade liberalization on productivity, or how much workers actually produce in any given work session. If productivity rises, workers can be paid more without driving up inflation or cutting into business profits. Thus, rising wages can be sustained over the long term. Rising productivity that leads to higher wages will expand domestic consumer demand, stimulating further production of goods and services and creating a virtuous circle of growth. A third set of economic issues that must be addressed in measuring the impact of trade on average citizens is how the gains from trade are distributed. There are winners and losers from trade, and it is impossible to assess the effect of trade on societies without knowing which groups gained, which lost, and to what degree they were affected.

Beyond these economic effects of trade on real people, there is also an important political reason to study the employment impact of trade. Political leaders often promote trade in general, and particular trade agreements such as the North American Free Trade Agreement (NAFTA), as job creators. In the United States, for example, then-president Bill Clinton predicted that NAFTA would create 200,000 U.S. jobs in its first two years of existence.<sup>1</sup> Today, President George W. Bush promotes trade pacts on the same basis, promising that they will "generate high-wage jobs for American workers."<sup>2</sup> When trade pacts are sold to the public and to legislators on the basis of their potential to create jobs and raise wages, it is important to revisit those promises, once time has elapsed and data have accumulated, to determine actual results. Such retrospective studies can then be used to guide future trade policy.

As with other effects of NAFTA, it is not a simple or straightforward proposition to tally the impact of the agreement on jobs, wages, and incomes. Still, there are several aspects of NAFTA's effects that can now be estimated with some confidence. In my testimony, I review the impact of NAFTA on jobs, wages, and household income in each of the countries of North America, but focus primarily on Mexico, because the impact of NAFTA on employment has been much greater there than in Canada or the United States.

### *Employment in Mexico*

Mexico has an abundance of labor. Very high population growth rates through the mid-1970s translated into a demographic bulge in the workforce in the 1990s and this century, as people born during the earlier high-growth years matured and began looking for work. In addition, during the 1980s and 1990s women joined the workforce at increasing rates, in part because of the decline in the reproductive rate, but also out of the need to support household incomes during recurrent economic crises. Overall, the Mexican labor force grew from 33.7 million immediately before NAFTA to 43.4 million in 2004, meaning that Mexico needed almost a million jobs a year simply to absorb the growth in labor supply.<sup>3</sup>

Economic theory suggests that opening to trade will increase the demand for labor in a labor-abundant country and therefore will increase the number of jobs, the wages paid, or both. Clearly, that would be a desirable effect for a country with a large and growing workforce such as Mexico. However, in practice, the effect of a trade pact like NAFTA depends on many factors, including which tariffs were reduced or eliminated by each country, in what sequence and at what pace. The following discussion focuses on tariff changes between Mexico and the United States, because trade between Mexico and Canada is a very small part of Mexico's total trade.<sup>4</sup>

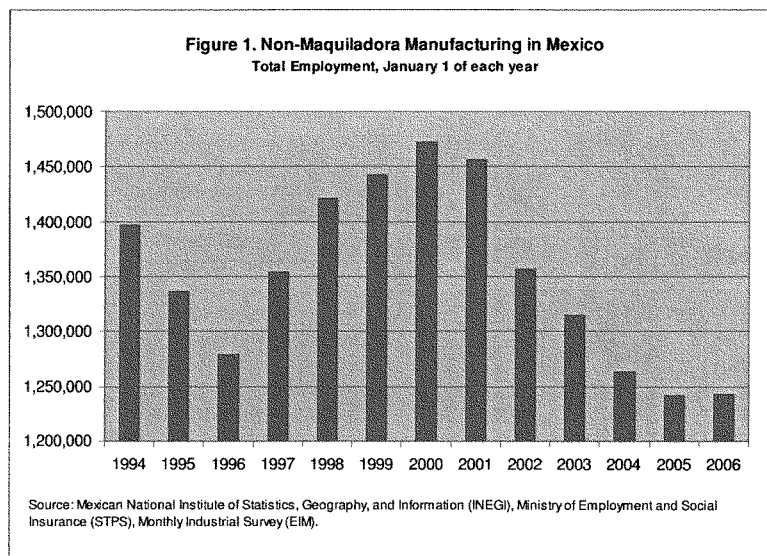
Under NAFTA, the United States cut tariffs on most Mexican manufactured goods, with the largest cuts on textiles and apparel, followed by more modest but still significant reductions on footwear, chemicals, miscellaneous manufactures, and transportation equipment. The United States also cut agricultural tariffs and increased quotas, although one of Mexico's main agricultural products, sugar, continues to be restricted through tariffs and quotas. Other Mexican crops face seasonal restrictions that are scheduled to end by 2008. Meanwhile, Mexico cut tariffs dramatically on both agricultural and livestock products and virtually all manufactured goods from the United States. Some tariffs will be maintained on sensitive agricultural products such as maize and beans until 2008, but in practice the Mexican government has already allowed substantial above-quota tariff-free imports of corn.

The pattern of trade between the two countries changed in a number of ways as a result of these cuts. From Mexico's standpoint, the cumulative changes resulted in a shift from a net trade deficit with the United States before NAFTA to a substantial net trade surplus in 2002. The overall net surplus masks a growing deficit in agricultural trade with the United States that is more than offset by a surplus in manufactured exports from Mexico. Trade in services shows a small deficit for Mexico.

#### Manufacturing Employment

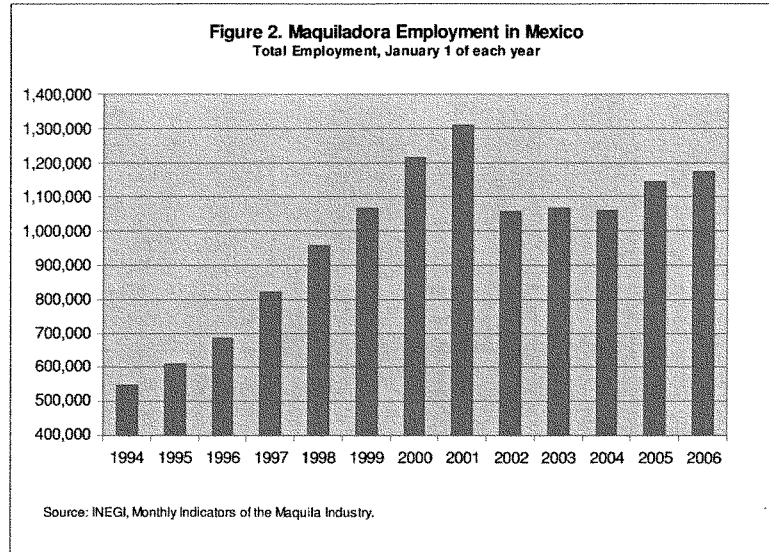
Translating these changes in trade patterns into employment impacts is not easy, but approximate numbers of jobs can be determined with reasonable certainty. With respect to manufacturing, the task is complicated by data availability. The Mexican government tracks manufacturing employment through two separate data series. One survey covers medium-size and large manufacturing establishments that account for about 80 percent of industrial production, but excludes the maquiladora sector.<sup>5</sup> A separate survey covers maquiladoras, which are export assembly plants.

Overall employment in non-maquiladora manufacturing in Mexico is lower in 2006 than it was in 1994, except in microenterprises, which are mainly in the informal sector.<sup>6</sup> Employment in the non-maquiladora manufacturing sector stood at about 1.4 million in January 1994, declined sharply during the peso crisis, and then began a recovery that produced an additional 91,000 jobs at its peak in May 2000 before declining again over the past six years. In June 2006 there were 1.26 million jobs in non-maquiladora manufacturing, about 130,000 fewer than when NAFTA took effect (see Figure 1).



The decline since 2000 has been caused in part by the U.S. recession and weak recovery, as well as by global changes such as the rise of competitive exports from China.

The maquiladora program was created by Mexico and the United States in 1965 to allow tariff-free and tax-free imports of materials and components into Mexico for assembly and re-export to the United States. It is concentrated in the auto parts, electronics, and apparel sectors. The growth in maquiladora jobs is not primarily attributable to NAFTA, since the program predates that pact, but NAFTA did provide significant tariff cuts on apparel and as a result stimulated that subsector of the maquiladoras. Maquiladora assembly plants added about 800,000 jobs between NAFTA's enactment in January 1994 and the sector's peak employment in early 2001. They then shed about 125,000 jobs through January 2006. Currently, maquiladoras employ about 700,000 more workers than they did before NAFTA (see Figure 2).



Maquiladora plants produce almost entirely for export, so employment in that sector can be attributed largely to trade (although not exclusively to the terms of NAFTA). By contrast, the data on non-maquiladora manufacturing employment blend production for export with production for domestic markets; therefore, it is difficult to determine the proportion of employment attributable to exports. One study suggests that the share of non-maquiladora manufacturing employment associated with exports increased by roughly 500,000 jobs between 1994 and 1999, and then declined.<sup>7</sup> Of those jobs, some 450,000 were based on exports to the United States.

Only part of the growth in both maquiladora and non-maquiladora export employment can be attributed to NAFTA. The peso devaluation of 1994-1995 gave a very significant boost to all Mexican exports, as the dollar bought more than twice the value of Mexican goods after the devaluation. A study by the U.S. International Trade Commission (USITC) found that the peso devaluation of 1994-1995 had a larger impact on the growth of Mexican exports of manufactured goods to the United States than all NAFTA-related tariff changes combined.<sup>8</sup> If one uses the USITC's findings on the relative impact of various factors on changes in Mexican exports to the United States, NAFTA tariff cuts likely explain about one-quarter of the total growth in export manufacturing jobs (maquiladora and non-maquiladora), or the addition of about 250,000 jobs, while the peso devaluation, lower transport costs, and other factors account for the rest.<sup>9</sup>

The overall reality during the NAFTA years has been one of strong growth in the volume of manufactured exports but very disappointing growth in manufacturing employment. This unwelcome divergence between manufacturing output and employment growth emerged in

Mexico in the mid-1980s but appears to have widened since enactment of NAFTA.<sup>10</sup> A number of explanations for this outcome have been advanced. One obvious explanation is productivity growth, which reduces the amount of job creation for any given level of exports. While productivity did increase in Mexican manufacturing over most of the twelve years since NAFTA took effect, productivity gains alone do not account for the very slow growth in manufacturing employment.

Another factor that likely explains part of the phenomenon is that export manufacturing in Mexico is increasingly based on a production model in which component parts are imported, then processed or assembled, then re-exported. In this model, the spillover effect of such operations on the broader economy is very limited, because only a narrow range of processing or assembly operations benefit the labor market. Vertical integration, including creation of businesses that supply parts and materials, has not occurred, limiting the multiplier effect of any growth in exports. This pattern is quite clear in the maquiladora sector, in which 97 percent of components are imported and only 3 percent are produced locally in Mexico. But the non-maquiladora export sector shows similar patterns. The intra-firm production carried out by multinational firms operating in Mexico in sectors such as the auto and electronics industries depends heavily on imported inputs. It seems probable that Mexican manufacturers that previously supplied inputs to large manufacturing firms have lost a significant share of input production to foreign suppliers, and thus account for part of the weakness in manufacturing employment.<sup>11</sup>

Another important factor limiting manufacturing employment growth is that some Mexican manufactures have been displaced directly by imports. The limited employment growth that has occurred in manufacturing for the domestic market has been mainly in very small firms and in the informal sector, with low pay and usually without benefits.

The export manufacturing model in Mexico has also failed to generate much growth in jobs at the high-skills end of the spectrum, in areas such as research, engineering, design, and accounting. One study of the skills component of manufacturing jobs in Mexico found that in 2000, the proportion of skilled labor in the manufacturing sector was only 9.9 percent.<sup>12</sup> The skilled labor component in manufacturing was actually less than the average share of skilled labor in the overall economy, 13.9 percent.

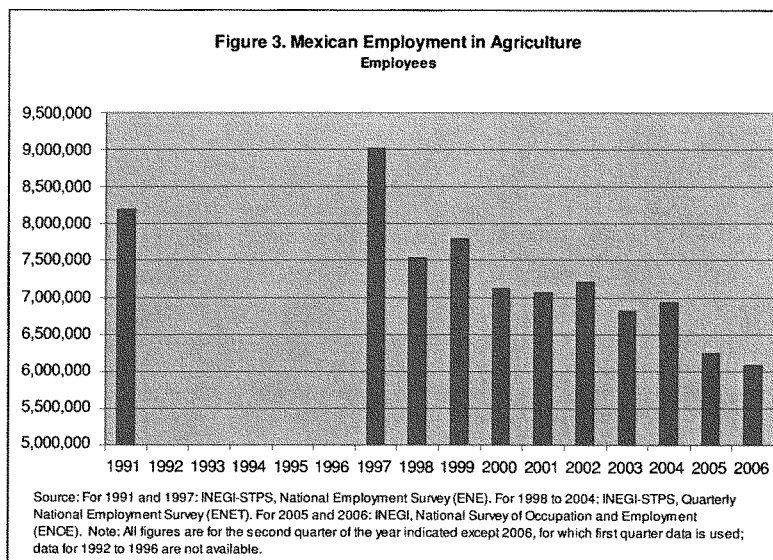
The limited job creation under the manufacturing model currently prevalent in Mexico is of particular concern when put in the context of other changes that are likely to affect future employment growth in the sector. Mexico enjoyed the advantage of being the first low-wage country to strike a free-trade agreement with the United States and Canada. However, as more free-trade agreements are negotiated, unilateral preference programs are expanded, and World Trade Organization (WTO) membership grows, the first-mover advantage is progressively diluted. The accession of China to the WTO, in particular, has meant mounting competition for Mexico's manufactured exports, particularly in labor-intensive sectors such as apparel and electronics. In 2003, China displaced Mexico as the second-largest exporter to the United States (after Japan). It is no accident that Mexico was the last WTO member to agree to the terms for China's accession to the trading organization. The proliferation of free-trade agreements by the United States and Canada also means that the value of Mexico's market access advantages will erode as other low-wage countries gain similar access. For example, the US free trade agreement

with Central America adds a sizable pool of lower-wage labor to the available regional labor supply, undermining Mexico's current advantage.

#### Agricultural Employment

As noted above, Mexico has had a net trade deficit in agricultural goods with the United States every year since NAFTA took effect, except the peso crisis year of 1995, when the huge devaluation of the peso made most dollar-denominated products too expensive for Mexicans. The agricultural trade deficit existed before NAFTA, but it grew after enactment of the trade pact and was larger in 2002 than in any previous year. Tariffs on the most sensitive crops in both the United States and Mexico have yet to be eliminated, and so the nature of bilateral agricultural trade will continue to evolve. However, the pattern to date challenges the conventional wisdom that agricultural liberalization is good for the developing country in a trade relationship with a developed economy. The one bright spot for Mexico, an increase in exports of fruits and vegetables, has not kept pace with Mexican imports of U.S. grains and oilseeds. This may be due in part to greater efficiency among U.S. producers, but it is also partly due to U.S. subsidies. By one estimate, U.S. corn was sold in Mexico from 1999 through 2001 at prices 30 percent or more below the cost of production.<sup>13</sup>

The increasing trade deficit has translated into job losses in agriculture. Agricultural employment in Mexico stood at about 8.1 million in the early 1990s just before NAFTA came into force. It actually increased slightly in the aftermath of the peso crisis, when widespread unemployment led some workers back to the farm. Employment in the sector then began a downward trend, with about 6 million employed in the first quarter of 2006, a loss of over 2 million jobs compared to the pre-NAFTA levels.<sup>14</sup> While not all of that reduction can be attributed to NAFTA, other forces that affected trade, such as the sharp devaluation of the peso during 1994-1995, pushed in the opposite direction, toward greater growth of Mexican exports over imports. In fact, 1995 was the one post-NAFTA year in which Mexico had a surplus in its agricultural trade with the United States, and agricultural employment did improve modestly for a few years thereafter. However, once the peso stabilized, the agricultural trade balance again turned against Mexico and agricultural employment resumed its decline. During this period, Mexico was also liberalizing trade with other partners, so the entire impact cannot be ascribed to NAFTA. But the WTO has determined that Mexico reduced its agricultural tariffs much more for the United States than for other trading partners.<sup>15</sup> Thus, agricultural trade liberalization linked to NAFTA is the single most significant factor in the loss of agricultural jobs in Mexico (see Figure 3).



The release of 2 million workers from the agricultural sector more than offset the 700,000 jobs gained in the export-manufacturing sector in the twelve years since NAFTA took effect. As already noted, it is impossible to establish precisely what proportion of the gain in export manufacturing jobs and the loss in agricultural jobs between 1994 and 2006 was directly attributable to NAFTA. However, it is clear that the trade pact has not produced a strong gain in overall employment and, indeed, might have produced a net loss of jobs for Mexico. The long-term effects are still uncertain, as most manufacturing tariffs have now been eliminated, while the most sensitive agricultural tariffs have yet to come down.

#### Service Sector Employment

NAFTA has had little direct effect on employment in the Mexican service sector, because most services are not traded and those that are, such as financial and telecommunications services, are not very labor intensive. Mexico has had a small trade deficit in services with the United States, so any impact on employment is likely to be negative, although not large.

Nevertheless, the service sector is key to an overall understanding of the Mexican employment situation, because it is here that most Mexicans find employment. It is also the epicenter of the growth in the so-called informal sector. The share of total employment found in the service sector increased from 51 percent immediately before NAFTA took effect to 60 percent by June

of 2006. Most of this growth was due to absorption of labor from the agricultural sector, which decreased from 25.7 percent of employment in 1993 to 14.3 percent by June of 2006.<sup>16</sup>

Negative impacts on subsistence farmers, caused in part by increased agricultural imports from the United States, meant that rural households had to struggle to maintain adequate income levels. Due to sluggish employment growth in manufacturing, as well as the limited skills of many agricultural workers, employment was found (or created) mainly in low-pay, low-productivity jobs in the service sector such as domestic work, street vending, and personal services and repairs. Much of this was in the informal sector, which comprises self-employment, employment in microenterprises, and other forms of employment that do not provide benefits such as health care and pensions.<sup>17</sup> Overall, the informal sector grew during most of the 1990s, with employment in informal jobs approaching 50 percent of all employment in Mexico in 1995 and 1996, following the peso crisis and the subsequent economic contraction. After economic growth resumed in the late 1990s, the informal sector shrank somewhat, but still accounts for about 46 percent of Mexican jobs.<sup>18</sup> This reservoir of low-wage, low-productivity workers shows no sign of being absorbed by Mexico's export sector in the foreseeable future.

#### *Wages and Productivity in Mexico*

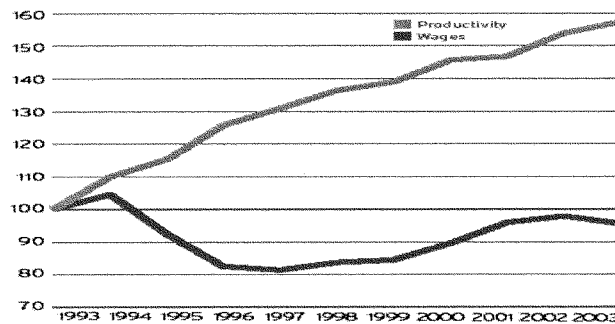
Real wages for many Mexicans are lower today than when NAFTA took effect. This stunning setback in wages cannot be attributed primarily to NAFTA, however. Most of the decrease in real wages observed over the last twenty years can be traced to two periods of sharp wage declines. The first was during the debt crisis of the early 1980s, when a devaluation of the peso and contractionary policies designed to achieve macroeconomic stability and meet the terms demanded by international holders of Mexico's debt led to a sharp drop in wages. The second decline occurred as a result of the peso crisis of 1994-1995. When the peso was sharply devalued in each crisis, the cost of imported goods and the rate of inflation both shot up, while wages were constrained by the government's monetary and wage-setting policies. Wages gradually recovered after each of those macroeconomic shocks. However, they did not grow enough in either recovery period to return to previous levels. This pattern is true of both traded and nontraded sectors of the economy, as well as for employees of small, medium, and large firms.<sup>19</sup>

While NAFTA is not the cause of the two major setbacks in Mexican wages, it is striking that a free-trade agreement that dramatically increased exports and foreign direct investment has not done more to increase wages and living standards for average Mexican workers--or even for workers in most export firms--relative to pre-NAFTA levels. Trade theory suggests that a country with an abundance of low-skill labor (such as Mexico) that opens to trade will experience increasing returns (wages) to its low-skilled workers. However, wages for most production workers in both maquiladora and non-maquiladora manufacturing are still below pre-NAFTA levels. Some analysts have suggested that, for a variety of reasons, trade increased the demand for highly skilled labor in Mexico relative to the demand for less skilled workers.<sup>20</sup> But even for highly educated workers in the manufacturing sector (such as professional, technical, and administrative staff), real wages in the late 1990s were below those in 1993, with the only exceptions occurring in a few regions along the U.S. border.<sup>21</sup> This same pattern holds for other sectors of the economy. Workers with university degrees and even postgraduate study received

lower real wages in 2000 than in 1993.<sup>22</sup> The disappointing wage performance has occurred despite the fact that Mexican workers' productivity has increased since NAFTA took effect (see Figure 4).

Increasing productivity is a necessary condition for sustainable increases in wages, since over time an economy can only afford to consume what it produces. But increased productivity is not sufficient to guarantee wage increases. Wage outcomes will depend in part on supply and demand in labor markets, and in part on the quality (and any bias) of institutions that have been established to determine how the gains from productivity are distributed. At present, labor market supply continues to exceed demand in most categories of labor in Mexico, contributing at least a partial explanation for poor wage results. In addition, the increasing integration of global production as a result of liberalized trade and improved protections for foreign investors has meant that, for many categories of unskilled and semi-skilled labor, competition is found not only in national labor markets but also internationally, as firms make production and sourcing decisions based in part on labor costs in various countries. The accession of China and other low-wage countries to the WTO has increased the supply of labor that firms can tap while still being guaranteed access for their output to the world's rich markets, including the United States and Canada. Differences in tariffs and transportation costs may not offset larger differences in unit labor costs. (Unit labor costs reflect the combination of wages and productivity).

**Figure 4: Manufacturing Productivity and Real Wages in Mexico**  
Index: 1993=100



Source: INEGI/STPS, Monthly Industrial Survey (EIM), Economic Information Bank (BIE), Indicadores Económicos de Coyuntura  
Notes: Productivity and wage data cover both production and non-production workers. The maquiladora sector is not included in this data series. Wages include salaries, bonuses, and benefits. Data for 1993–2002 are annual averages; 2003 is January–September average.

While labor market supply and demand and footloose global production undoubtedly contribute to the decoupling of wages from productivity seen in Mexico, it is also the case that Mexican institutions have been biased against wage increases. For example, it has been government policy

to hold down the minimum wage over most of the last two decades. This has been done both to increase global competitiveness of Mexican labor and exports and to meet structural adjustment goals. The minimum wage determines many other wages in Mexico, which are set as multiples of the minimum, and so the impact is felt beyond the lowest-paid jobs. Further, unionization and collective bargaining, among the main institutional mechanisms for determining how gains from productivity increases will be distributed between employers and workers, have been repressed in Mexico through weak labor laws. In the maquiladoras, for example, it is a widespread practice for employers to conclude “protection contracts” with corrupt or non-existent trade unions. Since Mexican labor law allows only one union to hold a contract in a workplace, these contracts preclude efforts by workers or more legitimate unions to bargain for wage increases. There have been numerous substantiated allegations of Mexican labor authorities allowing employers to collude with non-representative unions to avoid vigorous collective bargaining.<sup>23</sup>

### *Inequality and Poverty in Mexico*

Gauging the effects of trade on real people requires an assessment of trade’s impact on inequality and poverty, because the gains and losses from trade are not distributed evenly. Inequality in Mexico is high, as it is in much of Latin America. This is a cause for concern because it undermines social stability and political cohesion. Furthermore, societies with highly unequal economies have been shown to reduce poverty less effectively and at slower rates than more equal societies.<sup>24</sup> Some studies have also shown that overall growth is reduced over the long term by highly unequal income distributions, thus constraining the incomes of all.<sup>25</sup>

Income inequality had been declining in Mexico for several decades up to the early 1980s, but it reversed course after the debt crisis of 1982 and the resulting macroeconomic contraction and structural reforms. Inequality then increased for most of the following decade, but began to abate again in the early 1990s, the years immediately before NAFTA. However, since 1994 inequality has again been on the rise. Compared to the period before NAFTA, the top 10 percent of households have increased their share of national income, while the other 90 percent have lost income share or seen no change.<sup>26</sup>

Income inequality in Mexico has a geographic dimension as well. Historically, Mexico’s southern states have been poorer, while the regions around the capital and along the U.S. border have been relatively more prosperous. From 1940 to 1980, targeted government policies led to an increasing convergence in per capita income among regions. However, following the macroeconomic crisis of the 1980s, the long trend toward convergence in regional incomes first stopped and then reversed, with regional inequality widening again in the 1990s.<sup>27</sup>

The share of people living in extreme poverty in Mexico has followed a similar pattern, shrinking dramatically during the 1960s and 1970s (from 61 percent to 30 percent) and then increasing after the 1982 debt crisis. Like economic inequality, the incidence of poverty increased through the remainder of the 1980s (reaching 41 percent by 1989) and then began to decline somewhat in the early 1990s, with the extreme poverty rate at 31 percent when NAFTA took effect. Poverty surged again during the peso crisis of 1994-1995, to over 40 percent. Since

then, it has again declined, but at 31 percent the proportion of Mexicans living in poverty is still slightly higher than the level seen in the late 1970s.<sup>28</sup>

### *Employment in the United States*

The impacts of NAFTA on the United States' economy and employment are significantly less than on Mexico or Canada, for several reasons. The U.S. economy is much larger than that of either of its neighbors; it is less dependent on trade because of its huge (and wealthy) domestic market; and only one-third of its total trade is with its NAFTA partners. Further, U.S. tariffs were substantially lower than those of Mexico and Canada before NAFTA (and its predecessor, CUFTA), and its tariff reductions were proportionately much smaller than the tariff cuts made by those countries. Since NAFTA has had a much smaller overall impact on the U.S. economy, its impact on jobs and wages in the United States is also much less than in Mexico and Canada.

The actual impact of NAFTA on U.S. employment has been sharply disputed by proponents and critics of the agreement. Widely diverging estimates have been produced. Some proponents of NAFTA have approached the task by estimating the number of manufacturing jobs supported by a given level of exports and then multiplying the growth in exports to Canada and Mexico by that figure to arrive at job gains. Critics, on the other hand, have applied the multiplier formula to the overall trade deficit, (reflecting the greater increase of imports over exports). Advocates of NAFTA resist using the multiplier formula to identify jobs lost due to imports, since it is not certain that all imported goods substitute for U.S. goods that would have been produced in the absence of trade.<sup>29</sup> However, it is clear that NAFTA, like all trade agreements, has produced both winners and losers, and so estimates that focus only on jobs created and not those destroyed offer no insight into the agreement's net employment effects. A further limitation of this methodology is that it does not distinguish between changes in trade due to NAFTA and changes caused by other trade agreements, such as that creating the WTO, and does not take into account the impact of exchange rate fluctuations on trade. Due to these limitations, the estimates of the employment impact of NAFTA based on the multiplier approach, by both proponents and opponents, are unpersuasive.

The USITC recently developed a model to measure the impact of NAFTA and four other trade agreements on the U.S. economy which represents an advance over earlier studies.<sup>30</sup> The USITC model estimates that the combined effects of NAFTA and CUFTA had a positive impact on total compensation to U.S. workers of approximately \$10 billion in 2001, compared to a scenario without the two agreements.<sup>31</sup> The model assumes that there is no net gain or loss of jobs due to NAFTA. This assumption is based on trade theory, which suggests that in full-employment economies, job composition will shift but there will be no net change in total employment. Labor market adjustment will occur by means of rising wages in the sectors that benefit from trade. However, the model can be used to estimate the order of magnitude of job gains or losses by changing the assumption about how labor markets adjust to changes in trade. If one assumes instead that wages are rigid and that the full adjustment occurs through increases in the number of jobs rather than increases in wages, the USITC model would produce a maximum net gain of 270,000 jobs. From 1994 until 2001, the US labor market could be considered at full employment. Under that condition, it is likely that gains from trade have translated into higher

wages rather than additional jobs. On the other hand, with U.S. unemployment rising in the recession of 2001 and for some time thereafter, it is reasonable to assume that some of the NAFTA/CUFTA impact would be seen in increased employment rather than higher wages. The combination of labor market conditions suggests that the overall impact of NAFTA on U.S. employment lies somewhere between a net gain of 270,000 jobs and zero net change.

An important limitation of the USITC model, which it shares with other methodologies, is that it does not capture the effect of investment decisions to relocate production from the United States to Mexico or Canada. To the extent that those decisions are based purely on market access (tariff and nontariff) considerations, the USITC model will capture them. But NAFTA also included important protections for U.S. investors that had not existed before the agreement, and those investor benefits may also affect decisions on where to produce. Further research and modeling work is needed to assess these effects.

Whether the *net* impact of NAFTA on employment is a small net positive (as the USITC model suggests) or neutral or weakly negative (as further elaboration, including research on investment impacts, might show), it is known that about a half-million U.S. workers lost jobs as a result of the agreement. While these lost jobs were likely offset by other jobs gained, the impact on losers is an economic and political concern. A useful source of information on NAFTA's impact on job loss can be found in data compiled under the NAFTA Trade Adjustment Assistance (NAFTA-TAA) program. This U.S. government program provided additional benefits for workers affected by NAFTA beyond those included in a general U.S. trade adjustment assistance program from 1994 through 2002. (Thereafter benefits were combined in a single trade adjustment assistance program.) During that time, about 500,000 workers were certified as having lost employment due to NAFTA. A detailed analysis of NAFTA-TAA data showed that about half of the job losses were due to production shifts to Mexico.<sup>32</sup> The apparel industry produced the greatest number of NAFTA-TAA certified job losers, about 28 percent of those eligible under the program, followed by electronics (13 percent), automobiles and parts (7 percent), and fabricated metals (6 percent). Other industries accounted for 5 percent or less of those certified eligible.

#### *Wages and Productivity in the United States*

Because the net impact of NAFTA on overall employment in the United States is small, the impact on wages is also likely to be minor at the national level. Still, important changes have occurred in the structure of U.S. wages that most studies attribute in part to trade; consequently, NAFTA is likely to account for some of those observed effects. The main structural change is the widening gap between the wages of skilled and unskilled workers that has been observed for the last three decades. There is a large literature that attempts to explain this divergence, with most economists identifying technological change as the main driver of this increasing gap. But most analyses find that trade has also played a role. While estimates of the impact of trade on low-skill wage depression vary depending on the methodology of the study, many researchers attribute about 20 percent of increased earnings inequality to trade. One study estimates that 40 percent of the growing wage gap can be attributed to a combination of trade and immigration.<sup>33</sup> This is potentially relevant to a discussion of NAFTA impacts, because immigration from

Mexico to the United States has increased since the agreement took effect, contrary to many predictions. Other studies look not at overall trade but at the growth of global production chains, or outsourcing, which allows U.S. manufacturers to maintain the high-skilled stages of production processes in the United States while sending low-skilled operations abroad.<sup>34</sup> This would tend to raise skilled wages (or depress unskilled wages) through the operation of supply and demand. To the extent that NAFTA reduced tariff barriers for the cross-border shipment of intermediate goods and provided greater guarantees for investments, it undoubtedly contributed to the observed growth of shared production between the United States and Mexico. However, this trend is also evident with respect to U.S. production chains involving many other low-wage countries.

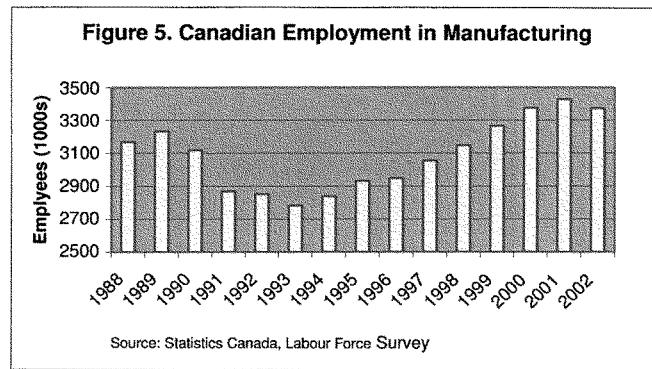
Since the early 1990s, unit labor costs in U.S. manufacturing have fallen, because productivity has grown faster than wages. This decoupling of productivity from wage increases is seen in all of the NAFTA countries. In Mexico, the decoupling began after enactment of NAFTA, and in Canada it began after CUFTA took effect. In the United States, the trend began in the 1980s, when U.S. manufactured goods faced a serious challenge in the U.S. market from European and Asian imports. While this failure of wages to keep pace with productivity growth cannot be attributed directly to NAFTA, it is clear that increasing international economic integration has allowed employers to capture a greater share of productivity gains than had been the case during the period when these economies were less open to trade. It is not surprising that the trend in Mexico and Canada is so closely aligned with the advent of NAFTA and CUFTA, respectively, given that the United States is the dominant trading partner of each country. The U.S. economy, on other hand, was more affected by multilateral tariff reductions effected in successive rounds of General Agreement on Tariffs and Trade (GATT) negotiations, because two-thirds of U.S. trade is with partners other than Canada and Mexico. The likely channels through which this phenomenon operates include the integration of global labor markets for certain types of labor through outsourcing and production chains, which increase the available supply of low- and medium-skilled labor relative to demand. It is also likely that the relative bargaining power of labor is reduced by the possibility of outsourcing or plant relocation, even when it does not actually occur.

### ***Employment in Canada***

The impact of NAFTA on Canada cannot be understood without combining NAFTA's effects with those of its predecessor, the Canada-United States Free Trade Agreement (CUFTA), which took effect on January 1, 1989. NAFTA incorporated the provisions of CUFTA and also liberalized trade between Canada and Mexico. But trade with Mexico continues to be a small share of Canada's total trade—less than 1 percent of Canadian exports go to Mexico and 3.6 percent of its imports are from that country. Therefore, the main impact of NAFTA/CUFTA on employment in Canada and the Canadian economy in general can be traced to the phasing in of the CUFTA provisions.

A recent study of CUFTA effects on employment by Daniel Trefler advances considerably the level of analysis relative both to earlier studies of the Canadian experience and to studies that examine U.S. and Mexican employment impacts.<sup>35</sup> The carefully constructed model examines

the effects of CUFTA on employment, wages, and productivity in manufacturing industries in Canada. It controls for several other factors, such as the business cycle, that might account for changes. Trefler finds that in those industries that were most affected by Canadian tariff cuts and therefore were most exposed to import competition, employment fell by 12 percent. In the export-oriented industries that experienced the largest U.S. tariff cuts and therefore benefited most from the agreement, there was no increase in employment.<sup>36</sup> Insofar as Canadian tariff cuts under CUFTA were deeper than U.S. tariff cuts, the greater impact on import-competing industries is not surprising; but the lack of any net job creation in export industries is noteworthy. This result runs counter to the findings of earlier studies, which found that employment losses in U.S. and Canadian industries that compete with imports were more than offset by employment gains in export-oriented industries. Those studies suffered from serious methodological flaws, but the direction of the results seemed intuitively logical based on trade theory and they were widely accepted, despite actual observed net job losses. The Trefler study calls into question whether a net positive impact on jobs from trade liberalization can be inferred, at least between two industrialized countries and in the short-to-medium term (see Figure 5).

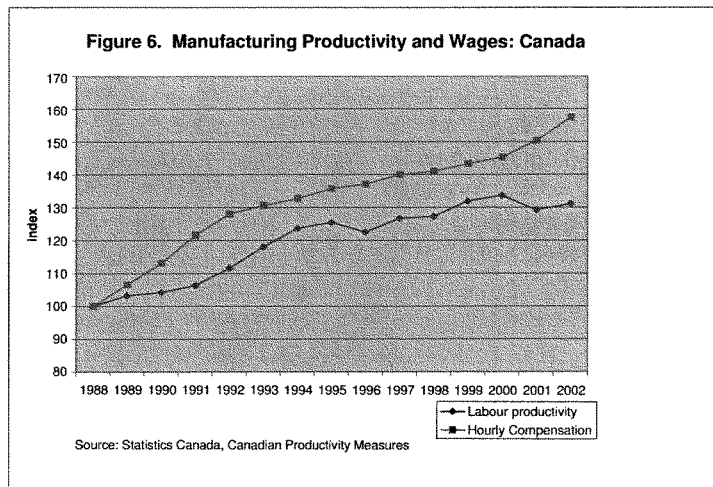


Trefler did find that both groups of industries experienced fairly strong productivity gains.<sup>37</sup> Over the medium term (in this case, a decade), employment in the Canadian manufacturing sector recovered, and by 1999 achieved levels last seen in 1989.<sup>38</sup> Growth continued in 2000 and 2001, with manufacturing employment hitting a peak in 2001 of 3.4 million jobs, about 250,000 more than pre-CUFTA levels, before declining again in the recession that began that year. In addition, the manufacturing sector constitutes a slightly larger share of the Canadian economy (22.4 percent in 2002) than its counterpart in the United States (20.6 percent the same year), which suggests that the productivity gains may have helped the long-term survival of Canadian manufacturing, although exchange rate movements undoubtedly played a role as well. The industries that showed positive employment trends by the late 1990s included automobiles and auto parts, electronics, plastics, and, somewhat surprisingly, apparel.<sup>39</sup> That industry underwent

significant restructuring, with higher-skilled operations becoming a larger share of employment than sewing and other lower-skilled jobs.

### *Productivity and Wages in Canada*

Overall real wages in Canada were only slightly higher in 2002 than in 1989, but manufacturing earnings fared somewhat better.<sup>40</sup> This suggests that NAFTA/CUFTA or trade more generally did not have a negative impact on Canadian wages, since earnings in nontraded sectors increased more slowly than in manufacturing. As in the case of both Mexico and the United States, productivity increases in Canada significantly outstripped wage increases, in both manufacturing and nonmanufacturing sectors (see Figure 6).



### *Inequality in Canada*

Incomes in Canada are relatively more equal than in either Mexico or the United States, but inequality has been on a marked upward trend since 1989.<sup>41</sup> The richest 20 percent of households increased their share of national income, from 40.7 percent of total income that year to 42.8 percent in 2000, while all other households experienced declines in their share. Only the top 20 percent of households had higher real incomes in 2000 than in 1989. The other 80 percent of Canadian households saw real incomes decline from 1989 to 1994 and then recover slightly, but not enough to make up for the earlier decline.

Given the relatively better performance of wages in manufacturing than in most other sectors, it seems clear that trade-induced changes in wage income patterns is not the explanation for the decline in incomes for 80 percent of Canadian households and the increasing economic inequality in Canada over the NAFTA/CUFTA period. However, a significant factor in household income in Canada is transfer payments from government, particularly to the bottom 40 percent of households, and these did decline due to cuts in government funding for social programs and changed eligibility requirements. For example, since NAFTA/CUFTA took effect, the proportion of unemployed workers receiving unemployment benefits declined from 87 percent to 36 percent. This decline is attributable to a number of factors, including macroeconomic policy. However, a strong concern of NAFTA/CUFTA critics was that trade opening to the United States would put downward competitive pressure on Canada's social safety net, which in most cases was superior to that of the United States. It cannot be ruled out that increasing liberalization of trade was a factor in the downward pressure on unemployment insurance and other social benefits in Canada and the resulting widening gaps in disposable household income. Further studies are needed.

***Conclusion: Learning from the NAFTA Experience***

At twelve years, the long-term effects of NAFTA on employment, wages, and incomes in the countries of North America cannot be judged definitively. However, short- and medium-term impacts can now be assessed on the basis of substantial, accumulating data, as presented above. That assessment also provides some potentially useful guidance for measures that might improve the employment and distributive outcomes of future trade agreements.

***Employment***

The most salient result of the NAFTA experience and the one most at odds with predictions of political advocates is that the trade agreement has produced disappointingly small net gains in employment in the countries of North America. In Mexico, employment destruction in domestic manufacturing and agriculture has all but swamped job creation in export manufacturing. In the United States, NAFTA has had either a neutral or very small net positive effect on employment. Meanwhile, in Canada, CUFTA led first to a significant net decrease in jobs in traded sectors, followed by a slow recovery of employment to pre-CUFTA levels after ten years, then a continued increase in subsequent years. The political and rhetorical claims for trade as an engine of net job growth are not borne out by experience, at least in the medium term.

Such claims have always been at odds with the predictions of trade theory. In theory, if an economy is at full employment before opening to trade, the shifting of resources into different productive activities based on comparative advantage will not result in a net gain or loss of jobs, but rather in a different mix of industries and employment. The gains from trade in a full-employment economy would be seen in rising wages and incomes, according to basic trade theory. The United States and, arguably, Canada have been at full employment during most of the NAFTA period. Thus, the lack of any significant job growth due to NAFTA in Canada and

the United States is not at odds with the predictions of economic theory, although it certainly contradicts the claims of NAFTA boosters. What is surprising, even from the perspective of economic theory, is the weak job creation in Mexico, which is far from full employment. As noted earlier, it is impossible to determine with certainty the precise share of agricultural job losses and manufacturing job gains in Mexico that resulted directly from NAFTA. However, the trade pact has been the single most important factor in Mexico's changing pattern of trade, and the overall growth of jobs in all traded sectors since 1993 has been very weak. It is thus evident that NAFTA has not been a robust job creator for the low-wage, labor-abundant trading partner.

In developing economies with surplus labor, such as Mexico, the NAFTA experience demonstrates that trade pacts cannot be counted on to produce much, if any, net employment growth in the absence of other targeted policies. Policies to maximize employment gains from trade would include measures to promote domestic supplier and support industries and terms in the trade agreement that reward rather than discourage the use of domestic inputs in the production of exported goods.

The experience of Mexico also suggests that a developing country with a high proportion of its labor force in low-productivity agriculture should negotiate very long transition periods for the phase-out of tariffs on basic crops. The negative situation currently faced by Mexico also demonstrates that a developing country must use that transition time aggressively to prepare the rural population for the wrenching adjustment it will face. Policies should be adopted to shift farmers to competitive crops, to develop alternative sources of employment in rural areas, and to invest heavily in education to prepare the population for more modern occupations. Another important factor for Mexico was that some of its most important basic crops, such as maize, were exposed to competition from subsidized U.S. crops that are sold at artificially low prices, sometimes below the cost of production. Further, U.S. policy on agricultural subsidies changed significantly in ways that were not foreseen during the NAFTA negotiations, most notably in the passage of the farm bill in 2002 that increased subsidies. Successful competition will be impossible for the developing country under those circumstances.

The transition times negotiated by Mexico were too short, and the government did not adopt sufficiently vigorous rural adjustment policies to help subsistence farmers adapt to the new trade conditions. In trade negotiations with developing countries with significant employment in subsistence agriculture, the US and its partners should carefully consider the sequencing of liberalization, to allow the absorption of rural workers into other sectors that expand due to liberalized access to foreign markets, before basic crops are liberalized. Developing countries will also need special safeguard mechanisms to protect the incomes of their rural households during the long transitional period.

The experience of Mexico also suggests that the government relied too heavily on export-led growth, adopting policies that repressed wages in order to pursue global competitiveness. These wage policies had the effect of depressing domestic demand in Mexico, which made the economy even more dependent on export sectors for job creation, in a vicious circle. A more balanced strategy of stimulating domestic demand through wage increases (commensurate with productivity gains) and support to rural households would likely produce better overall employment results.

### *Productivity*

The one employment area where a clear positive impact has been seen during the NAFTA period is the growth of productivity in all three North American countries. At least in Mexico and Canada, which cut tariffs deeply and were exposed to competition from their giant neighbor, NAFTA likely played a significant role in the observed productivity growth. In Canada, increased productivity may have contributed to a medium-term revival and perhaps even long-term survival of the manufacturing sector.

However, the strong productivity growth in the United States and somewhat weaker growth in Mexico and Canada may have had the unwelcome side effect of reducing the pace of job creation in the three countries, as workers produced more and fewer new jobs were created.

Throughout North America, there has been a decoupling of productivity growth from wage growth over the last decade.

### *Wages*

During the NAFTA period, productivity growth in Mexico has not translated into wage growth, as it did in earlier periods. Mexican wages are also diverging from, rather than converging toward, U.S. wages, as trade theory would suggest.

Because the net impact of NAFTA on U.S. employment is small, the impact on overall wages is also likely to be small. But a widening gap between the wages of skilled and unskilled workers is partly attributable to trade, and NAFTA probably accounts for a small portion of the observed growth in wage disparity within the United States.

Overall real wages in Canada were only slightly higher in 2002 than when CUFTA took effect in 1989, but manufacturing earnings had fared somewhat better. This suggests that NAFTA and CUFTA did not have a negative impact on wages, since earnings in non-traded sectors increased more slowly than in manufacturing. As in the case of Mexico, productivity increases in Canada significantly outstripped wage increases.

In all three countries, the evolution of wages and household incomes since NAFTA took effect has been toward greater inequality, with most gains going to the upper 20 percent of households and higher-skilled workers. While this trend is clearly compounded of many factors, more open trade appears to be one element—along with continental and global competition over the location of production—that restrains wage growth.

Whether productivity gains lead to higher wages also depends on the nature and quality of the institutions that determine the distribution of productivity gains within a society between the return to workers as higher wages and the return to investors as higher profits. Institutions that govern the ability of workers to organize unions and bargain collectively over wages are important determinants of distribution, as are government mechanisms such as minimum wage

policies. If productivity gains are to be shared with workers in the form of rising wages, the institutions and public policies that affect wage outcomes will need to be strengthened. Weak laws and institutions related to freedom of association and collective bargaining should be addressed in conjunction with trade liberalization. Minimum wage policies need to be reconsidered; dispute resolution mechanisms, such as arbitration, could also be strengthened.

### *Income Distribution*

Income inequality has been on the rise in Mexico since NAFTA took effect, reversing a brief downward trend in the early 1990s. Compared to the period before NAFTA, the top 10 percent of households have increased their share of national income, while the other 90 percent have lost income share or seen no change. Regional inequality within Mexico has also increased, reversing a long-term trend toward convergence in regional incomes.

In a trend that predates NAFTA, income inequality in the United States has been increasing for most of the last two decades. The growing wage gap between high-skilled and low-skilled workers is one of the causes, and to the extent that trade is a factor in the wage gap, it is also implicated in growing inequality.

Incomes in Canada are relatively more equal than in either Mexico or the United States, but inequality has been on a marked upward trend since CUFTA's entry into force in 1989. Because manufacturing wages have performed better than wages in most other sectors, it seems clear that trade-induced wage changes are not the cause of the observed increase in inequality. Rather, a reduction in transfer payments from government, which play an important role in the incomes of the bottom 40 percent of households, accounts for most of the change. The weakening of the Canadian social safety net, which generates these transfer payments, was a concern of CUFTA opponents, but there is currently no clear evidence to support a causal relationship.

If the gains from trade are to be shared widely throughout a country, the institutional mechanisms that govern how costs and benefits of economic change are distributed may need to be strengthened. Government measures that affect income distribution, such as tax and transfer mechanisms, should be reviewed and fortified to deal with the impact of trade opening.

The experience of each of the NAFTA countries confirms the prediction of trade theory that there will always be winners and losers from trade. The number of losers may equal or even surpass the number of winners, especially in the short-to-medium term. In Canada, it took a decade for manufacturing employment to recover from the initial displacements caused by CUFTA. In Mexico, rural farmers are still struggling to adapt to NAFTA-induced changes. The short-to-medium term adjustment costs faced by the losers from trade can be severe, and the losers are often those segments of society least able to cope with adjustment, due to low skills, low savings, and low mobility. It must also be recognized that there may be permanent losers from trade, due to limitations of education, skills, geographic isolation, and other factors.

Because the impacts of trade are uneven, governments should establish mechanisms that help offset the losses suffered by those in declining sectors. Trade adjustment assistance should provide income support to workers and small farmers during transitional periods, as well as

funds for training for new occupations. Such policies are highly desirable complements to trade pacts. The existing trade adjustment assistance program in the United States and the broader social safety net in Canada serve these ends, although both countries' plans have critical gaps that should be addressed. In Mexico, budget constraints and policy choices have precluded the establishment of even the most basic unemployment insurance and social safety net. The harsh impact of agricultural trade liberalization on subsistence farmers there has not been offset by appropriate government policies. Developing countries negotiating with wealthier trading partners will likely need financial assistance from those countries, as part of the trade package, for transitional adjustment programs.

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<sup>1</sup> William J. Clinton, Remarks at the Signing Ceremony for the Supplemental Agreements to the North American Free Trade Agreement, September 14, 1993. *Public Papers of the Presidents of the United States*, vol. 2, 1993 (Washington, D.C.: U.S. Government Printing Office, 1993).

<sup>2</sup> Remarks by the President at the Signing Ceremony for Chile and Singapore Free Trade Agreements, September 3, 2003. Available at [www.whitehouse.gov](http://www.whitehouse.gov).

<sup>3</sup> National Employment Survey (ENE), Mexican National Institute of Statistics, Geography, and Informatics (INEGI) and the Ministry of Employment and Social Insurance (STPS). Available at: [www.inegi.gob.mx](http://www.inegi.gob.mx).

<sup>4</sup> In 2002, 89 percent of total Mexican exports went to the United States, while 1.7 percent went to Canada; 63 percent of total Mexican imports were from the United States and 4.2 percent were from Canada. (The data for Canada are from Statistics Canada, National Income and Expenditure Accounts; for Mexico, from INEGI, System of National Accounts; and for the United States, from the Bureau of Economic Analysis, National Income and Product Accounts.)

<sup>5</sup> INEGI, Monthly Industrial Survey (EIM). This survey also excludes microenterprises, small businesses with fewer than five employees that operate in the informal sector. Available at: [www.inegi.gob.mx](http://www.inegi.gob.mx).

<sup>6</sup> Ibid.

<sup>7</sup> Enrique Dussel Peters, "Industrial Policy, Regional Trends and Structural Change in Mexico's Manufacturing Sector," in Kevin J. Middlebrook and Eduardo Zepeda, eds., *Confronting Development: Assessing Mexico's Economic and Social Policy Challenges* (Palo Alto, Calif.: Stanford University Press, 2003).

<sup>8</sup> *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 no. 3621 (Washington, D.C.: U.S. International Trade Commission), August 2003. Available at [www.usitc.gov](http://www.usitc.gov)

<sup>9</sup> Ibid.

<sup>10</sup> Rogelio Ramirez De La O, "What Has Changed in the Performance of Employment and Wages in Mexico after NAFTA?" paper prepared for the Third Seminar on Income and Productivity of the North American Commission on Labor Cooperation (February 2000). Available at [www.naalc.org/english/publications](http://www.naalc.org/english/publications)

<sup>11</sup> This effect could be amplified by a tendency in Mexican monetary policy to overvalue the peso as means of controlling inflation. This disadvantages Mexican producers when they try to export, while imposing less of a burden on U.S. multinationals using Mexico as an assembly platform, since the movement of components into Mexico and of finished products out will largely cancel out or at least smooth out the exchange rate effects.

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<sup>12</sup> These figures are for overall manufacturing. The definition of *unskilled* here is possession of up to twelve years of formal education, while *skilled* is defined as possession of thirteen years or more. Jose Romero and Alicia Puyana, *The Mexican Economy after Two Decades of Trade Liberalization*, 2002. Paper on file with the author.

<sup>13</sup> *United States Dumping on World Agricultural Markets*, Cancun Series Paper no. 1 (Minneapolis: Institute for Agriculture and Trade Policy), 2003. Available at [www.iatp.org](http://www.iatp.org)

<sup>14</sup> INEGI, National Income and Expenditure Survey (ENIGH) and STPS/INEGI National Employment Survey (ENE). Available at: [www.inegi.gob.mx](http://www.inegi.gob.mx).

<sup>15</sup> *World Trade Report 2003* (Geneva: World Trade Organization), August 2003. Available at [www.wto.org](http://www.wto.org)

<sup>16</sup> INEGI, National Occupation and Employment Survey (ENOE). Available at: [www.inegi.gob.mx](http://www.inegi.gob.mx).

<sup>17</sup> There are a variety of definitions of the informal sector. The definition used here was developed for STPS by Clara Jusidman in 1993. It takes into account establishment size, the position held, and the industry involved.

<sup>18</sup> Maria Elena Vicario, Sandra Polaski, and Dalil Maschino, *North American Labor Markets: A Comparative Profile*, Secretariat of the North American Commission for Labor Cooperation, Washington, DC, December 2003). Available at [www.naalco.org](http://www.naalco.org). The authors' calculations are based on data from the Mexican National Institute of Statistics, Geography, and Informatics (INEGI) and the Ministry of Employment and Social Insurance (STPS).

<sup>19</sup> Carlos Salas and Eduardo Zepeda, "Employment and Wages: Enduring the Costs of Liberalization and Economic Reform," in Kevin J. Middlebrook and Eduardo Zepeda, eds., *Confronting Development: Assessing Mexico's Economic and Social Policy Challenges* (Palo Alto, Calif.: Stanford University Press, 2003).

<sup>20</sup> See, for example, Raymond Robertson, "Trade Liberalisation and Wage Inequality: Lessons from the Mexican Experience," *World Economy*, vol. 23, no. 6 (June 2000), pp. 827-49.

<sup>21</sup> Carlos Salas and Eduardo Zepeda, *Wages and Productivity in Mexico: Theoretical and Empirical Issues*, July 2003, paper commissioned for the report, *NAFTA's Promise and Reality, Lessons from Mexico for the Hemisphere*, Carnegie Endowment for International Peace, 2004. Salas and Zepeda study on file with the author.

<sup>22</sup> *The Mexican Economy* (see note 12), based on data from the Ministry of Labor and Social Welfare National Employment Survey.

<sup>23</sup> The labor side-agreement to NAFTA includes provisions for public petitions to any of the member governments if labor rights violations occur in any of the other NAFTA countries. Several petitions have been filed alleging interference with freedom of association and collective bargaining rights in Mexico. The petitions were filed with the U.S. National Administrative Office, the body that administers the agreement for the United States. While expressing its findings in diplomatic terms, the National Administrative Office did find significant shortcomings in this area in many cases (see [www.do.gov/ilab/programs/nao](http://www.do.gov/ilab/programs/nao)).

<sup>24</sup> See, for example, Martin Ravallion, "Can High-Inequality Developing Countries Escape Absolute Poverty?" World Bank Policy Research Working Paper no. 1775 (Washington, D.C.: World Bank), 1997. The World Bank Web site provides a useful summary of research on this topic at [www.worldbank.org/poverty/inequal/abstracts/index.htm](http://www.worldbank.org/poverty/inequal/abstracts/index.htm)

<sup>25</sup> Dani Rodrik, *Where Did All the Growth Go? External Shocks, Social Conflict and Growth Collapses*, (Cambridge, Mass.: Kennedy School of Government, Harvard University), 1997, provides a political-economic model. Other models are catalogued at the World Bank Web site ([www.worldbank.org/poverty/inequal/abstracts/index.htm](http://www.worldbank.org/poverty/inequal/abstracts/index.htm)).

<sup>26</sup> Data based on INEGI, ENIGH; and *The Mexican Economy* (see note 12).

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- <sup>27</sup> Gerardo Esquivel, *Sources of Regional (Non)Convergence in Mexico* (Washington, D.C.: World Bank), 2002. Available at [www.worldbank.org](http://www.worldbank.org)
- <sup>28</sup> Diana Alarcon and Eduardo Zepeda, "Economic Reform or Social Development? The Challenges of a Period of Reform in Latin America Case Study of Mexico," *Oxford Development Studies*, Vol. 32, No. 1, March 2004.
- <sup>29</sup> Apparel imports, for example, come from many countries. Apparel imports from Mexico may have displaced imports from other countries rather than U.S. production.
- <sup>30</sup> *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 no. 3621 (Washington, D.C.: U.S. International Trade Commission), August 2003. Available at [www.usitc.gov](http://www.usitc.gov). The USITC model is based on a computable general equilibrium model but uses actual trade flows and other macroeconomic and microeconomic data from the U.S. economy for the period 1978-2001. It controls for such factors as exchange rate shocks to isolate the effects of NAFTA tariff changes. It also takes into account the phased-in nature of the agreement and the growing share of trade in the U.S. economy.
- <sup>31</sup> In *The Impact of Trade Agreements* (see note 30), the USITC estimates that U.S. labor income would have been \$40 billion less if not for the effects of five trade agreements, including the Tokyo and Uruguay rounds of the General Agreement on Tariffs and Trade (GATT), NAFTA, CUFTA, and the United States-Israel Free Trade Agreement (p. 339). Separately, the study finds that 25 percent of the total impacts attributable to all five agreements were contributed by NAFTA and CUFTA (pp. 332-33).
- <sup>32</sup> Mary Jane Bolle, *NAFTA: Estimated U.S. Job "Gains" and "Losses" by State over 5 1/2 Years* (Washington, D.C.: Congressional Research Service), February 2, 2000.
- <sup>33</sup> George J. Borjas, Richard B. Freeman, and Lawrence F. Katz, "How Much Do Immigration and Trade Affect Labor Market Outcomes?" *Brookings Papers on Economic Activity*, vol. 1, (1997), pp. 1-67.
- <sup>34</sup> Robert C. Feenstra and Gordon H. Hanson, *Global Production Sharing and Rising Inequality: A Survey of Trade and Wages* (University of California, San Diego, and National Bureau of Economic Research, 2001).
- <sup>35</sup> Daniel Trefler, *The Long and Short of the Canada-U.S. Free Trade Agreement*, University of Toronto, Canadian Institute for Advanced Research, and National Bureau of Economic Research, December 3, 2002. Available at [www.chass.utoronto.ca/~trefler/fta.pdf](http://www.chass.utoronto.ca/~trefler/fta.pdf)
- <sup>36</sup> The study actually showed a 3 percent employment loss in the export industries, but it was statistically insignificant.
- <sup>37</sup> However, the average annual productivity gains during this period were significantly less than those observed in the 1960s and 1970s.
- <sup>38</sup> *North American Labor Markets* (see note 18). Data based on Labour Force Survey, Statistics Canada.
- <sup>39</sup> *Ibid.*
- <sup>40</sup> *Ibid.* Data based on Survey of Employment, Payrolls, and Hours, Statistics Canada.
- <sup>41</sup> *Ibid.* Data based on Survey of Consumer Finances, Statistics Canada.

**Statement of Cathy Saucedo  
Director, Special Enforcement Division  
Trade Enforcement and Facilitation  
Office of Field Operations  
Department of Homeland Security  
U.S. Customs and Border Protection  
Senate Finance Committee  
U.S. Senate  
September 11, 2006**

Chairman Grassley, Ranking Member Baucus, and Members of the Committee, it is a privilege and an honor to appear before you today to discuss the operational impact and enforcement efforts of the North American Free Trade Agreement (NAFTA) by U.S. Customs and Border Protection (CBP) of the Department of Homeland Security.

I want to begin by expressing my gratitude to the Committee for the interest and support you provide as CBP continues to administer and enforce the NAFTA while facilitating the flow of legitimate trade that is so important to our nation's economy.

Your support has enabled CBP to make significant progress in implementing, administering and enforcing the NAFTA, as well as the many free trade agreements (FTA) that have entered into force. CBP looks forward to working with you to build on these successes.

**Background**

U.S. market opening initiatives took a significant step forward with the entry into force of the U.S.-Canada Free Trade Agreement in 1989. This FTA greatly liberalized trade between the U.S. and Canada. It was the first FTA that had specific rules of origin, which provided concrete, non-subjective methods for determining the origin of a good.

In 1994, the US-CFTA was superseded by the NAFTA. Implementation of this trilateral FTA with the United States' two largest trading partners not only led to a surge in U.S. exportations, but also resulted in a dramatic increase of importations from Mexico and Canada. The NAFTA improved upon the foundation of the US-CFTA by refining the specific rules of origin, adding more precise value concepts through a regional value content (RVC) methodology, and providing transparency requirements while continuing to facilitate trade. Since its implementation in 1994, the administration of the NAFTA has improved over the years, although CBP continues to experience operational challenges.

### **NAFTA Successes**

The NAFTA provides for specific rules of origin to determine whether a good qualifies for preferential tariff treatment. The concept of product specific rules was first introduced in the US-CFTA, and sought to remove subjective interpretation of substantial transformation. The basis for these rules lies within the international nomenclature of the Harmonized Tariff Schedule (HTS), which contains a set of headings and subheadings that are internationally uniform and used by nearly all of our trading partners. The fact that these rules, known as tariff shift rules, use the common language of the HTS in the process of determining whether a good is originating provides for a streamlined application of the provisions of the NAFTA. The specificity of the tariff shift rules provides for an agreement that can be administered and enforced with greater ease than previous trade programs.

Moreover, there is flexibility within certain specific rules for industrial products in the form of a regional value content (RVC) test. This is an alternate method of determining eligibility for preference in the event the good does not meet the requirement of the tariff shift rule. The RVC requires that a certain percentage of the value of the good be attributable to materials produced in and processing that occurs within the territory of the U.S., Mexico or Canada.

Since the implementation of the NAFTA, there have been various trilateral agreements to modify or simplify certain specific tariff shift rules that were overly complex or did not reflect current sourcing patterns. The NAFTA parties have, to date, agreed on three separate sets of liberalized rules of origin. This was accomplished through established NAFTA working groups, which included consultation with industry and Congress in order to be consistent with current production realities. This process is ongoing, with another round of changes expected to be considered in 2007.

The NAFTA was the first FTA to address the concepts of transparency and facilitation within the context of implementation, administration, and enforcement of the agreement. CBP promoted transparency through the creation of a temporary NAFTA center manned by CBP NAFTA experts to assist the trading community as well as our field offices during the implementation phase and beyond. This NAFTA center provided operational support to all parties involved in NAFTA transactions, such as importers, exporters, Import Specialists and CBP Officers.

In the spirit of facilitation, the NAFTA negotiators ensured that the flow of trade was not disrupted or hindered by waiving the requirement of the presentation of the Certificate of Origin (CO) as a condition of release of the goods. Although CBP does not require the presentation of the CO as a condition of release of the goods, the CO must have been properly completed by the exporter and must be in the possession of the importer prior to making a claim for tariff preference under the NAFTA, and must be presented upon request by CBP. Canada has

adopted this same procedure while Mexico continues to require the presentation of a CO prior to release of the goods.

CBP continues to refine the application of the NAFTA and has introduced increased flexibility regarding the presentation of the CO. Initially, the CO had to be completed on an official CBP form as directed by the trilaterally negotiated Uniform Regulations. However, in July 2005, CBP began to allow the CO to be in any format as long as all the required data elements are present and the CO is in the possession of the importer and is signed by the exporter. CBP now allows for an alternate CO, which can be in any format and a computer generated CO, which requires pre-approval prior to use.

In the area of textiles and wearing apparel, CBP was instrumental in creating, and currently chairs, the Textile Enforcement Subgroup of the *ad hoc* NAFTA Working Group on Textiles and Apparel. Working with our NAFTA partners, CBP has consolidated verification efforts of NAFTA duty preference claims into a single trip, fashioned after our Textile Production Verification Team (TPVT) visits. These highly successful trips provide CBP a cost effective way to verify NAFTA claims, by allowing CBP personnel to personally inspect foreign factories making trade preference claims. The success of the TPVT style NAFTA verifications have prompted both Canada and Mexico to contemplate conducting similar verifications for their enforcement efforts.

In continued efforts towards the facilitation of trade, CBP has instituted the Free and Secure Trade (FAST) program along the borders of Canada and Mexico in 2002. FAST provides for expedited processing of participants' qualifying merchandise and allows for a harmonized clearance process for low-risk shipments. The FAST program is directly tied to other CBP supported programs to promote and enhance security and safety measures while enhancing economic prosperity, such as the Customs-Trade Partnership Against Terrorism (C-TPAT) program.

Additionally, the U.S., Canada and Mexico are actively engaged in the Security and Prosperity Partnership of North America (SPP), which was launched in March of 2005. This trilateral initiative is premised on mutually reinforcing security and economic prosperity through greater cooperation and information sharing among the three countries of North America while respecting the sovereignty and unique cultural and legal heritage of each country. As you can see there are various efforts and ambitious programs to continue to facilitate trade, increase security and build upon existing relationships.

#### **NAFTA Challenges**

The NAFTA has been in effect for over twelve years and although the experience CBP has gained through implementing, administering and enforcing the first

multi-lateral FTA that the U.S. has entered into has been overwhelmingly positive, there have been some challenges posed by the Agreement.

NAFTA employs 2 sets of tariff rules to determine whether or not imported merchandise is eligible for a NAFTA benefit. First, there are permanent concise tariff shift rules used to determine whether or not the merchandise originates under NAFTA. Second, a temporary country of origin marking rules are used to determine which of the two NAFTA countries is the origin for duty purposes. For example if you have an imported good made in Canada with parts from China, Canada and Mexico, you would use the tariff shift rules to determine if the good was entitled to a NAFTA benefit. If it does, the marking rules determine the rate of duty (that from Canada or Mexico) would apply for those goods where Canada and Mexico have a different duty rate. This difference will disappear in 2008 when all NAFTA duties are eliminated for Mexico (duties for Canada were eliminated by 1998).

As previously mentioned, the provisions of NAFTA require a properly completed NAFTA Certificate of Origin, or "CO", be signed by the exporter and that the CO must be in the possession of the importer at the time a claim for preference is made. If the CO is not presented upon request, is not properly completed, or is not in the possession of the importer at the time the claim is made, the NAFTA requires that the claim be denied regardless of whether the good is in fact originating per the specific rules. This presents rigorous, paper intensive, recordkeeping requirements for the trading community and requires that claims be denied based solely on a paper document rather than the origin rules. We have remedied this provision in subsequent trade agreements.

As you might be able to deduce by the fact that the exporter is required to complete the CO, the NAFTA is an exporter focused agreement. Although the importer makes the claim and is responsible entity, the exporter has a critical role in a NAFTA transaction. The determination as to whether or not a good is originating is made by the exporter who may or may not fully understand the requirements to claim preferential treatment under NAFTA. CBP does have the ability to verify the origin of a good for which NAFTA preference is claimed through a verification to include a verification visit. However, there are several steps necessary prior to initiating verification, and these steps can interfere with the ability to accurately gauge the veracity of a party's preference claim. CBP must first obtain the CO from the importer, which must be completed according to the requirements. If a properly completed CO is received, CBP must then go beyond the CO in order to determine the origin of the good. This is conducted through the exporter, who is required to substantiate that the good meets the specific rules through additional supporting documentation, such as bills of materials, cost data, affidavits, and production information. A shortfall of the NAFTA is that the importer, who is ultimately responsible for the claim, is not an active participant in the verification process. Additionally, although CBP must

conduct verifications through the exporter, CBP has no jurisdiction over an entity in a foreign country.

A verification can include a visit to the site of production in Canada or Mexico. This allows for an extension of CBP's enforcement capabilities, however, the NAFTA contains strict guidelines that must be adhered to, such as notification to the exporter 30 days prior to the visit, that impact effective enforcement capabilities. There is no flexibility with which to conduct strategic enforcement actions, as the exporter will have been provided with sufficient notice, allowing dishonest exporters and producers to make operational adjustments well in advance of the verification visit. This notice effectively allows those exporters and producers the opportunity to 'clean up their act.'

For NAFTA claims, the importer is the responsible entity for making the claim and paying any duties and potential penalties. However, it is the exporter who is required to support the claim during verification by CBP. Although the U.S., Canada, and Mexico have trilaterally discussed amending the restrictive verification visit procedures to allow for more flexibility, no agreement has been reached to date. Thus the exporter focused regime presents logistical and administrative burdens to importers, exporters as well as CBP.

An additional area that presents challenges involves textiles and wearing apparel. Twelve years after the implementation of the free trade agreement, the three NAFTA parties still have not agreed upon verification procedures for certain textile goods receiving preferential tariff treatment. A limited quantity of products of Canada and Mexico currently receive duty-free treatment up to specified quantities even though they do not meet the rule of origin or tariff shift requirements. These Mexican and Canadian goods receive benefits under Tariff Preference Levels as if they met the tariff shift rules. CBP continues to meet trilaterally with Mexican and Canadian government officials in an ongoing effort to resolve differences and agree upon verification procedures.

In addition to verifications, CBP has actively enforced the NAFTA through audits of the exporter to ensure claims for preference are valid. Mexican officials conduct comparable audits in the U.S. with different approaches resulting in dissimilar outcomes. During the audit process, CBP allows the Mexican exporter a reasonable amount of time to produce supporting documentation, often granting extensions due to the detailed requests for information. However, Mexican authorities do not allow U.S. exporters flexible timeframes for providing such documentation. If the U.S. exporter does not have every document requested by the Mexican authorities during the site visit, the Mexican government officials make the assumption that the goods do not qualify and claims for preference are denied without further opportunity for presentation of information. This different approach in audit operating procedures, results in a significant variance in compliance rates for claims made in Mexico and the U.S.

NAFTA provides for workgroups among the Parties to address these types of challenges and other concerns in the areas of administration, interpretation and enforcement. These workgroups successfully tackled many issues during the first few years. However, the Parties have not been able to make any progress on this particular issue to date.

#### **The Framework For Post-NAFTA FTAs**

The NAFTA's concrete and transparent obligations for the importer, exporter, and government agencies have taught us a great deal regarding provisions that work well and those that require refinement. The NAFTA serves as a framework for the newer FTAs, furnishing some key provisions and concepts that allow for more effective enforcement and transparent administration. New FTAs also have the benefit of restructuring restrictive provisions, creating more flexibility without compromising enforcement.

The newer FTAs have shifted from an exporter focus to an importer focused regime, allowing the responsible party (the importer) to carry through its responsibility from the beginning of the transaction to the end. Additionally, the agreements eliminate the Certificate of Origin as a formal document by permitting the information to be presented in any format and by electronic means has also become less restrictive by allowing the importer, exporter, or the producer to complete the certificate while the importer maintains the ultimate obligation of supporting a claim.

CBP continues to promote the usage of the product specific rules and regional value content calculations modeled after the NAFTA, with modifications based on lessons we've learned and industry input. Regional value content calculations have been simplified by basing the equations on the value of materials and the appraised value of the good at the time of importation.

#### **Conclusion**

Mr. Chairman, Members of the Subcommittee, I have briefly discussed the operational impact and enforcement efforts of the NAFTA that CBP has encountered over the past twelve years. The NAFTA has been monumental in the creation of a framework from which new FTAs are being modeled and shaped. We have gleaned the positive and effective provisions that allow for an enforceable and operationally sound agreement, and have also streamlined the more complicated concepts. We continue to maintain and administer the largest multi-lateral agreement the U.S. has entered into while retaining effective enforcement methods. CBP strives to improve upon the NAFTA through regulatory updates and hopes to resume tri-lateral discussions on pertinent issues. Thank you for this opportunity to testify. I will be happy to answer any of your questions.

## United States Senate

WASHINGTON, DC 20510-5003

**Senator Craig Thomas, Chairman  
Subcommittee on International Trade  
Finance Committee  
“NAFTA at Year Twelve”**

**Monday, September 11, 2006**

Throughout history, trade has played an important role in the growth of society. From the opening of the Silk Road in 1000BC, to the completion of the Panama Canal in 1914, nations are continually looking for more efficient ways to move products around the globe. As transportation systems become more advanced, people and goods are able to move more rapidly. Distances, as measured in time, have become significantly shorter.

Additionally, the ability of humans to communicate was forever changed with the invention of the telephone. Today, satellite technology and the internet provide a level of communication most people only dreamed about 20 years ago. While not all flaws have been addressed, as the people in Wyoming can attest to, they system in place today is quite remarkable.

As technology has advanced and global infrastructure improved, the opportunity to engage in trade has changed dramatically. Businesses and entrepreneurs have access to nearly every corner of the world. Opportunities that didn't exist just a decade ago are suddenly a possibility.

Though the United States is the largest trading nation in the world, our potential has yet to be achieved. Industries and businesses in the U.S. continue to face trade barriers that unnecessarily restrict the flow of U.S. goods and services, and give an unfair advantage to competitors.

The U.S. soda ash industry is a perfect example of how trade barriers hurt U.S. industry. Until recently, the United States was the world's largest exporter of soda ash. Despite producing the highest quality soda ash in the world, primarily from deep underground mines located in Wyoming, trade barriers have limited the ability of the industry to compete in global markets. The United States now trails China in global exports of soda ash, which in turn has resulted in a significant loss of high paying, quality jobs in the U.S. industry. Negotiating with other countries is crucial if the U.S. is to be successful in obtaining market access and ensuring that the “playing field” is level for all participants.

While trade plays a key role in the U.S. economy, not all sectors benefit from trade. It is important that our negotiators not lose sight of the fact that some industries are more sensitive to trade than others. Special attention must be made to ensure that we are not taking one step forward and two steps back.

In 1993, President Clinton submitted to Congress the North American Free Trade Agreement (NAFTA). The legislation represented the most comprehensive trade agreement ever negotiated by the United States. While previous trade agreements focused primarily on reducing tariffs and improving market access, NAFTA created a framework to address a broad range of trade related issues. When the agreement was implemented on January 1, 1994, the world's largest trading block was established.

Much has changed in the world during the twelve years since NAFTA took effect. The European Union has expanded and rivals the NAFTA countries in both population and gross domestic product. Bilateral trade agreements have grown exponentially, and the economic awakening of China and India have forever changed the global trade landscape. Political changes around the world, while too numerous to list, have also impacted the dynamics of international trade and will continue to do so well into the future.

We are here today to receive testimony on NAFTA's impact in the intervening twelve years, and to share ideas on how to build on the agreement's strengths and avoid its weaknesses in the future. It is important to examine and learn from our experiences, and to use that knowledge to make better decisions.

We will also hear from the U.S. Customs and Border Protection regarding the agreement's affect on border services between the NAFTA countries. With a more than 150 percent increase in the trade of goods between the United States and Mexico and Canada since 1994, there is no question that the impact NAFTA has had on Customs operations over the years is significant. Finding ways to improve the current system of clearing goods entering our country is a goal we can all agree is worthwhile.

I'm pleased to welcome our outstanding witnesses to today's hearing. This is a difficult day for many people across our great country and I'm glad that you are able to join us. There is no event in recent years that has had a more profound impact on America than the September 11, 2001 attack on our nation. Today marks the 5<sup>th</sup> anniversary of that senseless attack which took the lives of nearly 3,000 innocent people, injured scores of others, and changed our nation forever. And as we go about our business today, it is important to remember those who were killed and those who continue to carry the scars of that day. Keep them in your thoughts.

**Testimony before the International Trade Committee****Senate Foreign Relations Committee**

By Sidney Weintraub  
William Simon Chair in Political Economy  
Center for Strategic and International Studies

September 11, 2006

The politically correct position on the left in the United States is that the North American Free Trade Agreement has been a failure. The argument is that Mexican economic growth has been disappointing even as the United States has had a bilateral trade deficit with Mexico in the 12 years that the agreement has been in effect. The reasoning is simple: because these developments occurred after NAFTA came into existence on January 1, 1994, the adverse economic effects must have been caused by NAFTA. I will give comments on Canada later; U.S.-Canada free trade began in 1989, and free trade between these two countries has not been controversial.

At its core, NAFTA was a trade agreement; or a trade and investment agreement. The objective was to increase trade between the member countries and encourage foreign investment into Mexico to stimulate production for Mexico's exports. Focusing for the moment on U.S.-Mexico relations, these two goals were amply achieved. Mexican merchandise exports to the United States from 1993 (the year before NAFTA) to 2005 grew by 400 percent (in current dollars), and U.S. exports to Mexico over the same period grew by 245 percent. Foreign direct investment into Mexico averaged about \$3 billion a year in the five years before 1993 and has averaged \$12 billion a year ever since. Some of this trade and investment growth probably would have occurred in any event, but econometric analysis shows that NAFTA added an extra dimension to the growth.

Mexico's real GDP growth from 1994 to 2005 has averaged 2.8 a year, which is inadequate to create enough jobs for new entrants into the labor force. Looking at the other two NAFTA partners the average GDP growth over the same time was 3.4 percent a year for Canada and for the United States 3.2 percent a year. This lack of job-creation has surely stimulated emigration to the United States. It is hard to argue, as those who oppose NAFTA have essentially done, that Mexico's net export growth reduced job creation. Common sense demands that we look for more rational reasons for the inadequate level of GDP growth necessary for creating enough jobs. The reasons are not hard to find—and they have to do with inadequate economic policies in Mexico. It has been evident for some time that Mexico has deep structural problems. Tax collections have been about 11 percent of GDP, compared with, say, the 18 percent of GDP at the federal level in the United States. (The figure in the United States is about 35 percent when state tax revenue is added; Mexican states, by contrast, collect little revenue directly.) Tax reform is sorely needed.

In order to meet budgetary needs, the Mexican federal government levies taxes of about 6 percent of GDP on *Petróleos Mexicanos* (Pemex), the state oil company; and this, in turn, has left Pemex with too few financial resources for exploration and development. This is a serious issue in that without new finds, and at current rates of production,

Mexico has only about 10 years of proven oil reserves. Mexico already must import natural gas and petroleum products. The budgetary shortage is somewhat mitigated today because of high prices for oil exports; but this has not led to government reduction in the taxes it imposes on Pemex.

Mexico's educational structure at primary and secondary levels is inadequate. The labor system is inflexible; the high cost of dismissing workers has led to a structure of part-time hiring precisely to avoid these dismissal costs, as well as to a large informal economy that is about 40 percent of the total labor force. Investment is impeded by an uncertain justice system. I have seen no reliable calculation of the cost in GDP of these structural faults, but my estimate is that this may be as high as 2 percentage points a year. NAFTA by itself cannot be expected to compensate for these large domestic problems.

Mexico does have a law in effect to promote competition, but in practice major monopolies and oligopolies are permitted to flourish. These exist for oil, natural gas, communications, and other activities. Examples abound of government procurement contracts rigged in favor of chosen companies and not determined by unbiased bidding. Such actions also have a deleterious effect on GDP growth.

Mexico, in recent years, has had stringent fiscal and monetary policy. Some Mexican analysts advocated larger fiscal deficits and looser monetary policy in order to raise economic growth. Less rigorous financial policies, however, might have stimulated inflation; this is now only about 3 percent a year. Mexico's new president, Felipe Calderón, inherits a sound financial structure, and this is one of his main assets.

Calderón also must deal with one of the most unequal societies in the world in terms of income and opportunity distribution. About 40 percent of the population lives in poverty. The recent election showed that Mexican society is sharply divided, with about 35 percent of voters each for the center right and center left. The new president faces a complex social situation. The income disparities coincide with the country's geography: the northern states benefited from increased economic activity with the United States, while the southern states did not. NAFTA exacerbated the north-south division, but the reality has existed for a long time.

The north-south disparity is not an artifact of NAFTA; it is a shortcoming of national economic and social policy of Mexico. I believe that the two richer countries of NAFTA, the United States and Canada, should provide aid to help Mexico's less-developed regions, conditioned by Mexico's own efforts to help these regions, along the lines practiced in the European Union. The development disparities in Mexico—in personal income and regionally—are a source of great potential instability that could affect the United States. Indeed, it does affect the United States right now in immigration flows from less-developed regions in Mexico.

Analysts have criticized NAFTA's agricultural provisions. The criticism deals mainly with farming in south-central and southern Mexico, a region that has little irrigation and must rely on uncertain rainfall for harvest outcomes. The farm owners and farm workers in these regions are able to subsist, but not much more, and need government help. One indicator of rural poverty is that Mexico's rural areas contain more than 20 percent of the population and contribute perhaps 6 to 7 percent of national GDP. The hope of the Mexican drafters of NAFTA was that overall Mexican growth would create enough jobs in urban areas to receive impoverished immigrants from rural areas. Economic growth

and job-creation was insufficient to accomplish this. Much of the emigration from rural areas bypassed Mexican cities and ended up instead in the United States.

There are now calls from Mexican political figures of just about all persuasions to alter the terms of NAFTA as they pertain to corn, a Mexican staple. Under NAFTA, the import tariff for corn was supposed to phase out gradually over 15 years—to reach zero in 2008. My recommendation is to negotiate a side agreement to NAFTA (that is, not to open all of NAFTA's agricultural provisions to re-negotiation, as President Vicente Fox has suggested), to alter the time for elimination of Mexico's corn tariffs. The United States subsidizes corn and that is a further argument the Mexicans make for giving them some flexibility on corn. Terms for the export of U.S. poultry to Mexico were revised a few years ago to resolve a bilateral trade problem.

NAFTA did not cause the rural problem, other than to set an arbitrary deadline. The rural population in Mexico has long been impoverished and opportunities in the *campo* were horrible long before NAFTA. The only long-term hope for most subsistence farmers and *jornaleros* (landless peasant workers) is to immigrate to places where opportunities are greater.

As an economist I focused on NAFTA's economic effects. U.S.-Mexican political relations also changed after NAFTA came into being. Mexican politicians today rarely use anti-Americanism to curry favor with the electorate. Mexican universities have set up many new centers to study the United States and Canada since NAFTA came into effect, and U.S. universities have done the same to study Mexico. Business people from both countries have developed closer relations, as have government officials. Environmental groups now cooperate across the border in ways they did not earlier. Bilateral problems have not disappeared, but they are now amenable to constructive discussion.

I will close with a word on Canada. Its economic growth rates have been satisfactory, about 3.4 percent a year over the last 13 years. Canada also has a trade surplus with the United States. Who doesn't? The issue of sovereignty loomed high when the decision had to be made in Canada on entry into free trade with the United States, and the election of 1988 focused on that issue. The Progressive Conservatives under Prime Minister Brian Mulroney won that election and the Canada-U.S. Free Trade Agreement went into effect. The connection between free trade and sovereignty has hardly been made since in Canada.



COMMUNICATIONS

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**STATEMENT OF  
STEVE BECKMAN  
DIRECTOR, GOVERNMENTAL AND  
INTERNATIONAL AFFAIRS DEPARTMENT  
INTERNATIONAL UNION, UNITED AUTOMOBILE, AEROSPACE &  
AGRICULTURAL IMPLEMENT WORKERS OF AMERICA (UAW)  
to the  
International Trade Subcommittee  
Committee on Finance  
United States Senate  
September 11, 2006**

The North American Free Trade Agreement (NAFTA) has come to represent what is wrong with current U.S. trade policy. Its serious adverse effect on workers, the environment, and on the ability of governments to regulate the economy in the public interest have produced broad opposition to NAFTA in all three countries -- the U.S., Canada and Mexico -- and to its use as a model for other trade agreements. The UAW strongly opposed the negotiation of NAFTA and strongly opposed its approval by Congress in 1993. Now, after 12 years of NAFTA-inspired job losses, downward pressure on wages, deterioration in respect for core labor standards and ballooning trade deficits, we remain convinced that our initial assessment of NAFTA was accurate.

The UAW has played a leading role in identifying the flaws in NAFTA and insisting on the need to renegotiate it. We have been particularly concerned about the dislocation of workers in the U.S. auto industry due to a surge of imports. The U.S. trade deficit in automotive products with Canada just about doubled from 1993 to 2005, and with Mexico it skyrocketed by 658 percent, jumping from \$3.6 billion to \$27.3 billion. The auto trade deficit with Canada has climbed by an additional 9 percent so far this year and, with Mexico, by 13 percent. Under NAFTA, the deficit in automotive trade with Mexico and Canada combined soared from \$13.2 billion to \$45.0 billion. New investments in our neighboring countries, particularly in Mexico, have added capacity there to assemble vehicles and produce parts, contributing to the loss of hundreds of thousands of U.S. jobs. Unless NAFTA is fundamentally changed, we expect the auto deficits with Canada and Mexico to continue to grow, putting ever-greater pressure on the jobs and incomes of UAW members.

In addition to moving automotive production, employment and investment to Mexico, employers have used the threat of moving there to intimidate workers in the U.S. during union organizing campaigns and collective bargaining. In this

way, downward pressure on the wages and benefits of UAW members and millions of other American workers has been exacerbated by NAFTA.

Mexican workers in the automotive industry have also suffered under NAFTA. The buying power of their wages has fallen and thousands of jobs have been lost due to corporate restructuring. The Mexican economy's manufacturing sector has become increasingly dependent on the expansion of low-wage jobs in maquiladoras that supply the U.S. market; this reinforces downward pressure on Mexican workers' wages and living standards, and makes their jobs dependent on exports to the U.S. rather than on domestic economic growth and development.

There are other forces contributing to the downward pressure on wages in Mexico. It has become common for employers there to make threats to move jobs from Mexico to China and other lower-wage countries, to demand higher productivity for less pay to remain "internationally competitive," and to push more workers out of the "formal" economy, where health insurance and other benefits are supposed to be provided, into the "informal" economy, where legal protections are minimal. The displacement of millions of Mexican farmers and farm workers due to increased imports of corn and other crops from the U.S. that resulted from NAFTA contributed to a sharp increase in the number of Mexican workers looking for jobs. That also depressed wages and added to the number of Mexican workers seeking work in the U.S. in order to support themselves and their families.

NAFTA's side agreements on labor and the environment have failed to improve conditions for workers and respect for environmental laws and policies in the region. The cooperative activities and procedures for bringing labor and environmental violations to public attention have produced no meaningful results. The UAW has participated in several cases that identified violations of worker rights in Mexico, but the empty promises of the side agreement ensured that absolutely no remedy was provided to the workers' whose rights had been violated and that no offending employers were penalized in any way. The same abuses that created the political pressure to negotiate these side agreements continue unchecked today.

NAFTA's thoroughly inadequate side-agreements on labor and the environment have largely disappeared from public view because their uselessness has been so thoroughly demonstrated. And the level of respect for the fundamental rights of workers in all three NAFTA countries is even lower today than before NAFTA went into effect in 1994, contributing to the growing income inequality in the region.

The NAFTA rules covering investment have allowed corporations to directly challenge government regulations and policies that interfere with their profitability -- even when the government action is to protect public health and safety and

promote economic development. Foreign investors in the U.S. are provided with broader rights by NAFTA than U.S. citizens and domestic firms. The investment provisions have constrained the policies of all levels of government in the U.S. – federal, state and local, and there is growing opposition to these provisions by state and local elected officials.

In addition to these many negative impacts of NAFTA, the use of this agreement as a model for subsequent free trade negotiations has sent U.S. trade policy and trade rules farther down the wrong path. The Bush Administration's active pursuit of bilateral and regional FTAs has now created a web of international trade obligations that ties the U.S. to the NAFTA model for years to come. This is one of the most important, and dangerous, effects of NAFTA.

While the UAW has been consistently critical of NAFTA, we have not been content to only criticize it. We have advocated the renegotiation of NAFTA to fix the problems we have identified and to establish a more beneficial basis for trade and broader ties between the U.S., Canada and Mexico. A revised NAFTA would improve the ability of the U.S. government to protect against surges of imports that cause serious and, often, permanent dislocation for American workers in high-productivity industries that pay family-supporting wages, including the automotive industry. The U.S. government must be able to act quickly and effectively to limit imports of vehicles or parts to prevent cutbacks in employment and production in the United States. American workers cannot rely on current NAFTA provisions to provide that relief.

To ensure that trade leads to improved living standards and working conditions in North America, economic and social development must be based on the adoption of the highest level of worker rights and standards and environmental standards in all three countries. These rights and standards must be included in the agreement itself, not relegated to "side agreements," as is the case in NAFTA today. The Bush Administration's approach – to include only the requirement to enforce national labor laws in the text of subsequent free trade agreements – ignores the need to implement the core labor standards of the International Labor Organization and to require upward harmonization of worker rights protections.

Incorporating these protections for workers and citizens into a renegotiated NAFTA is especially important because of the excessive protections for corporations that were included in the agreement. Under NAFTA's investment provisions, owners of patents, copyrights and other intellectual property were provided extensive new protections. These protections for the owners of capital must be reversed in a renegotiated NAFTA and a fair balance reached between the interests and rights of workers and the rights and responsibilities of investors.

A broad range of other issues, ignored in NAFTA, must also be incorporated into a renegotiated agreement. These would include controls on capital to limit financial speculation, exchange rates and debt relief. Each of these areas can

have a far greater impact on flows of trade and investment than the changes in tariffs and other trade barriers that were covered by NAFTA.

The issues raised here regarding NAFTA apply equally to any other international trade negotiations. All U.S. trade and investment agreements must address the following areas of concern to American workers: dramatically improving the transparency (i.e., openness to input from Congress, unions, non-governmental organizations) of the U.S. negotiating process and of the international institutions in which negotiations and U.S. activity occur (World Trade Organization, International Monetary Fund, World Bank, etc.); limiting the volatility and damaging effects of exchange rates on living standards and trade; controlling the de-stabilizing effect of the international flow of speculative investment capital into and out of countries through regulation, taxation and other necessary measures; focusing on the need to stimulate international economic growth through debt relief for countries that are poor and have been saddled with debt obligations that cannot be paid without imposing terrible economic burdens on their citizens; restricting the use of technology transfer and production-sharing arrangements (offsets) that sacrifice domestic production and employment for the benefit of corporate market access.

The UAW remains intensely concerned about the impact of NAFTA on workers in the U.S., Canada and Mexico and as a model for other trade negotiations. That is why, after 12 years of NAFTA, we believe it is an important priority for the UAW to continue to describe NAFTA's serious flaws and to demand its renegotiation. As part of that process, we are in contact with our union counterparts in Canada and Mexico, with organizations in the U.S. that share our concerns about NAFTA, and with coalitions in Canada and Mexico that effectively represent the aspirations of their citizens for a better approach to international economic integration.

Thank you for providing the UAW the opportunity to present our views on NAFTA at 12. We look forward to working with you to make the necessary changes in NAFTA and U.S. trade policy that will turn international trade and investment from a force that undermines the interests of workers and intensifies inequality within and between nations into a source of balanced, equitable and sustainable economic development for the U.S. and other countries.



**Chamber of Commerce of  
the United States of America**

**Association of American Chambers  
of Commerce in Latin America**



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**Hearing of the United States Senate  
Committee on Finance  
Subcommittee on International Trade**

*on*

**“NAFTA at Year Twelve”  
Monday, September 11, 2006  
2:00 p.m.**

**Dirksen Senate Office Building  
Room 215**

**Testimony for the Record**

*on behalf of the*

**U.S. Chamber of Commerce**

*and the*

**Association of American Chambers of Commerce  
in Latin America**

The U.S. Chamber of Commerce and the Association of American Chambers of Commerce in Latin America are pleased to submit this statement for the record on the substantial benefits the North American Free Trade Agreement (NAFTA) has brought American workers, farmers, and companies.

First, a word about our organizations:

- The U.S. Chamber of Commerce is the world's largest business federation, representing three million businesses and organizations of every size, sector, and region.
- The Association of American Chambers of Commerce in Latin America (AACCLA) represents 23 American Chambers of Commerce in 21 Latin American and Caribbean nations, and its 20,000 member companies represent over 80% of all U.S. investment in the region.

In the 12 years since the NAFTA entered into force, U.S. trade with Canada and Mexico has risen more than two-and-a-half fold, creating significant new opportunities for farmers, workers, businesses, and consumers in all three countries. While opponents of global engagement continue to criticize the agreement to this day, the NAFTA is a remarkable success by any reasonable yardstick.

#### **A Boom in Trade**

First, as a trade agreement, it has ushered in a dynamic era of trade growth. Since implementation of the NAFTA began in 1994, trade between the three North American economies has risen dramatically. Total U.S. trade with Canada and Mexico rose from \$297 billion in 1993 to \$810 billion in 2005. Canada looms as the largest U.S. trading partner, roughly equaling the European Union, which has a population and GDP roughly 10 times that of Canada. Mexico overtook Japan to become the second largest foreign market for U.S. goods and services. Daily commerce with Canada and Mexico surpasses \$2.2 billion.

A quick glance at the agreement itself reveals why it opened an era of rapid growth in trade. Upon entry into force, Mexico eliminated tariffs on nearly 50% of all manufactured goods imported from the United States and removed many non-tariff barriers. All Mexican tariffs on U.S. manufactured goods were eliminated by 2004, and Mexican tariffs on U.S. agricultural exports will be phased out by 2009. With a few exceptions, all Canada-U.S. trade has been duty free since 1998.

Placing this growth in context is useful. U.S. merchandise exports to Canada and Mexico have grown much more rapidly (at 133%) than U.S. exports to the rest of the world (77%) over the past 12 years. According to an analysis by the Office of the U.S. Trade Representative, Canada and Mexico accounted for 36% of U.S. export growth in 2005. For agriculture, Canada and Mexico together account for 55% of the increase in U.S. agricultural exports to the world since the NAFTA came into force. These statistics are a ringing endorsement of the NAFTA's benefits for American workers, farmers, and companies, and

they underscore the usefulness of free trade agreements as a way to boost U.S. economic growth — and, with it, jobs and incomes.

The composition of U.S. trade with Canada and Mexico represents a broad cross-section of the U.S. economy. Exports to Canada and Mexico include a variety of high value-added manufactures such as machinery, transportation equipment, computers and electronic products, chemicals and plastics, medical equipment, and paper products.<sup>1</sup> Services, which represent one of the most dynamic portions of U.S. international trade, are also growing rapidly.

#### **Benefits for the U.S. Economy**

The NAFTA was implemented at the beginning of a major expansion for U.S. manufacturers as a whole. Between 1993 and 2001, manufacturing output in the United States rose by one-third, according to a broad array of U.S. government statistics. U.S. industrial production — 78% of which is manufacturing — rose by 49% between 1993 and 2005, exceeding the 28% increase achieved between 1981 and 1993.

Other data confirm the uptick in manufacturing that coincided with the arrival of the NAFTA. Using Federal Reserve Board data, the Cato Institute's Daniel T. Griswold found that manufacturing output in the United States rose at an annual average rate of 3.7% during the first eight years of the NAFTA, 50% faster than during the eight years before the agreement's enactment. As Griswold points out, "this is not an argument that NAFTA was the primary cause of the acceleration in manufacturing output, but it does knock the wind out of the myth that NAFTA has somehow caused the 'deindustrialization' of America."<sup>2</sup>

The NAFTA certainly created new export opportunities for American manufacturers. According to a July 2005 analysis by the National Association of Manufacturers, Canada and Mexico accounted for 43% of the growth in U.S. exports of manufactured goods since the NAFTA's entry into force. U.S. exports of manufactures to Canada and Mexico grew more than 50% faster than exports to the rest of the world grew during this period. Today, machinery and vehicles are by far the largest categories of U.S. exports to Canada and Mexico.

The NAFTA also created major new opportunities for U.S. service providers. Nearly all services are covered by the agreement with the exception of aviation, maritime transport, and basic telecommunications. U.S. exports of services to Canada and Mexico have in recent years surpassed \$24 billion and \$15 billion, respectively.

In addition, the NAFTA shored up legal protections and enforcement of intellectual property rights, to the great benefit of U.S. creative artists and innovators. The NAFTA covers patents, trademarks, copyrights and related rights, trade secrets, semiconductor

<sup>1</sup> U.S. Department of Commerce, International Trade Administration, TradeStats Express, <http://tse.export.gov/>.

<sup>2</sup> Griswold, Daniel T., "NAFTA at 10: An Economic and Foreign Policy Success," Center for Trade Policy Studies, Cato Institute: December 2002, <http://www.freetrade.org/pubs/FTBs/FTB-001.html>.

integrated circuits, plant breeder rights, geographical indications and industrial designs. The NAFTA enhanced the protection contained in the intellectual property laws adopted by Mexico in 1991.

It's also worth noting that cheaper imports from Canada and Mexico have brought significant benefits for U.S. consumers. Together with the Uruguay Round trade deal that created the World Trade Organization, the NAFTA produced \$1,300 to \$2,000 in increased buying power for the typical family each year, according to the Office of the U.S. Trade Representative.

### **NAFTA's Impact on Jobs**

Assessing the number of jobs created wholly or partly due to the NAFTA is difficult. In the past, the U.S. Department of Commerce used a simple calculation that \$1 billion in exports sustained an average of 20,000 jobs. On this calculation, the number of U.S. jobs that depend on U.S. exports to Canada and Mexico surpassed 6.6 million in 2005, when exports to the two countries reached \$331 billion.<sup>3</sup> Such a figure would represent a sharp increase from 2.8 million jobs in 1993, the year before the NAFTA was implemented, when U.S. exports to Canada and Mexico reached \$142 billion. However, economists have in recent years rejected this back-of-the-envelope approach as too simplistic.

Part of the difficulty inherent in calculating the number of jobs created through trade opportunities arises from extensive indirect effects. For example, the International Trade Administration (ITA) at the U.S. Department of Commerce has calculated that "nearly three-fourths of all jobs supported by manufactured exports are generated indirectly, occurring upstream or downstream from the final production point as export activity triggers ripple effects in supporting sectors throughout the economy."<sup>4</sup> While only a minority of all the workers whose jobs depend on trade opportunities are aware of this fact, the level of awareness among workers whose jobs are only indirectly or partially dependent on trade is even lower.

ITA's study also concluded that "one out of every five manufacturing jobs [in the United States] was directly or indirectly tied to exports," with the figure surpassing one-third in some rapidly growing sectors (e.g., computers and electronic products). ITA also determined that the "job-supporting benefits of manufactured exports are broadly distributed throughout the nation."

Recognizing the impossibility of determining with any precision the reason why any specific job is eliminated — let alone compiling statistics on such causes — the U.S. government several years ago ceased compiling records purporting to show how many jobs

<sup>3</sup> U.S. Department of Commerce, Office of Trade and Economic Analysis, U.S. Foreign Trade Highlights, <http://www.ita.doc.gov/td/industry/otea/usfth/aggregate/H02T06.html>.

<sup>4</sup> "U.S. Jobs From Exports," Office of Trade & Economic Analysis, International Trade Administration, U.S. Department of Commerce, February 2001, [http://www.ita.doc.gov/td/industry/otea/job\\_report/jobs\\_report\\_web.pdf](http://www.ita.doc.gov/td/industry/otea/job_report/jobs_report_web.pdf).

were “lost” due to the NAFTA. However, a quick glance at the U.S. labor market provides useful context. In the 12 years since the NAFTA’s entry into force, U.S. employment has risen by 22.6 million jobs, or 20%. The unemployment rate was 5.1% in the period 1994-2005, compared to 7.1% during the period 1982-1993.

In short, the “giant sucking sound” predicted by one prominent NAFTA critic was never heard. In fact, in 2001-2003, when the U.S. economy lost three million manufacturing jobs, imports of manufactured goods from Mexico actually declined by a small amount. This undermines any suggestion that a surge in Mexican imports was a factor in manufacturing job losses during the 2001-2003 period. As the Economic Policy Institute acknowledged in a 2003 briefing paper entitled “The high price of ‘free’ trade,” NAFTA-related “job losses in most states are modest relative to the size of the economy”.<sup>5</sup>

### **A Foreign Policy Success**

Through the NAFTA, the United States lent timely assistance to Mexico in its transition from a closed economy and authoritarian politics to a new path. As recently as the 1980s, Mexico had one of the most closed economies in the world, and many observers believed its 1988 elections were fraudulent. Credit for the fact that Mexico is today a competitive democracy whose institutions are gaining strength — and its economy is open and increasingly competitive in the global marketplace — goes to the Mexican people. However, the NAFTA provided tools and opportunities that eased the transition.

As the Cato Institute’s Daniel T. Griswold notes: “In the decade since signing NAFTA, Mexico has continued along the road of economic and political reform. It has successfully decoupled its economy from the old boom-and-bust, high-inflation, debt-ridden model that characterized it and much of Latin America up until the debt crisis of the 1980s... Just as important, the economic competition and decentralization embodied in NAFTA encouraged more political competition in Mexico. It broke the economic grip in which the dominant Institutional Revolutionary Party (PRI) held the country for most of the last century.”<sup>6</sup>

As in 2000, when Vicente Fox of the National Action Party (PAN) won the presidency, Mexico’s institutions have been tested time and again over the past decade. A narrow outcome in last July’s presidential election has led the losing candidate to test these institutions once again, but to date the rule of law has prevailed. The NAFTA did not bring free elections to Mexico, but it has been part of a process of strengthening the country’s institutions and shoring up the rule of law that is paying benefits for Mexico’s development.

<sup>5</sup> Scott, Robert E., “The high price of ‘free’ trade,” EPI Briefing Paper #147, Economic Policy Institute: November 17, 2003.

<sup>6</sup> Griswold, Daniel T., “NAFTA at 10: An Economic and Foreign Policy Success,” Center for Trade Policy Studies, Cato Institute: December 2002, <http://www.freetrade.org/pubs/FTBs/FTB-001.html>.

**Conclusion**

Though its critics are loud, the NAFTA has been a remarkable success. It has provided new opportunities for American workers, farmers, and businesses. It has been one of a number of positive factors that boosted U.S. economic growth, productivity, and job creation over the past 12 years. The support of the U.S. Chamber of Commerce and AACCLA for the free trade agreements that have been negotiated in the past five years has its roots in the broad enthusiasm of our member companies that have found practical gains in the NAFTA. It has brought notable benefits for Canada and Mexico. We thank the Senate Finance Subcommittee on International Trade for the opportunity to offer these views and applaud any effort to make the NAFTA's many successes known to a wider audience.

