

# NAFTA's Promise and Reality

LESSONS  
FROM  
MEXICO  
FOR  
THE  
HEMISPHERE

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Introduction



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# Introduction

JOHN J. AUDLEY

*...a giant sucking sound...*

—ROSS PEROT, 1994

*NAFTA fuels economic growth and dynamic trade, stimulates investment while creating productive partnerships, works for small and medium-sized businesses and provides fairness and certainty. NAFTA partners promote environmental protection, and provide greater job opportunities in North America.*

—THE GOVERNMENTS OF THE UNITED STATES,  
MEXICO, AND CANADA, 1999

**LATIN AMERICAN AND CARIBBEAN COUNTRIES FACE AN ENORMOUS CHALLENGE:** How to grow their national economies, create good jobs, and generate the revenues necessary to provide basic public goods such as human health and environmental protection. Their task is burdened by more than two decades of weak economic performance that has failed to create jobs for a workforce expected to grow by 1.9 percent a year from 2001–2010. Nearly one person in ten is out of work. Current per capita income stands at a meager US\$3,580, and according to the Inter-American Development Bank, approximately 150 million people—one out of every three people living in Latin America and the Caribbean—earn less than US\$2 a day. To compound the problem, governments throughout the region admit that, while they may have enacted sound environmental and public health laws, the laws are rarely enforced, especially in rural areas.

Hoping to avoid another “lost decade” similar to the 1980s, thirty-four governments from the Western Hemisphere met in 1994 to outline an ambitious agenda to advance prosperity, democratic values and institutions, and security throughout

the hemisphere. Negotiating a Free Trade Area of the Americas (FTAA) was central to their agenda. According to the heads of state attending the 1994 meeting, “Free trade and increased economic integration are key factors for raising standards of living, improving the working conditions of people in the Americas, and better protecting the environment.”<sup>1</sup> Many officials and observers in the hemisphere believed that free trade would remedy ailing economies.

In total, Latin American governments are negotiating or have completed seventeen different free-trade agreements with member states of the Organization for Economic Cooperation and Development (OECD). Most recently, in January 2003, the governments of Costa Rica, El Salvador, Guatemala, Honduras, Nicaragua, and the United States announced the launch of comprehensive trade negotiations, which are scheduled to be completed by the end of 2003, prior to completion of the FTAA. According to the U.S. Trade Representative, Ambassador Robert Zoellick, the U.S.-Central American Free Trade Agreement (CAFTA) negotiations would further the regional integration the Central Americans have themselves begun, and thereby complement efforts to promote the successful conclusion of the FTAA negotiations.

Twenty-five years ago, Mexico faced a similar economic situation, and adopted a similar prescription. Mexico’s earlier economic strategy of import substitution and a large role for the public sector had increased jobs and economic output, but it had also left Mexico with a crushing external debt that sparked a major economic crisis in 1982. Mexican president Miguel de la Madrid Hurtado responded by moving Mexico toward an export economy. Despite considerable domestic opposition, in 1986

Mexico joined the General Agreement on Tariffs and Trade (predecessor to the World Trade Organization, or WTO). President Carlos Salinas de Gortari built on de la Madrid's initial steps toward liberalization by reducing the size of the public sector, promoting land ownership reform, and securing a commitment from the United States and Canada in 1991 to negotiate a free-trade agreement.<sup>2</sup> The North American Free Trade Agreement (NAFTA) went into force in 1994, marking the first major trade deal between developed and developing countries.

What has Mexico's experience been after twenty years of trade liberalization and ten years of NAFTA? How have the lives of Mexicans changed? Has the Mexican government developed the capacity to create conditions that put Mexicans to work, protect their health and the environment, and give them real alternatives to migration? In short, what lessons can be learned by other Latin American countries from Mexico's attempt to use trade liberalization with the United States and Canada as its engine for economic development?

#### **OUR OBJECTIVES**

This report has two objectives. First, we set out to determine how the quality of life in North America, particularly in Mexico, has fared as a result of trade liberalization in North America. While we touch on the experience of all three countries, we emphasize Mexico's experience since the enactment of NAFTA, as it is more relevant to other developing countries interested in strengthening their economic ties with wealthy countries such as Canada and the United States. Our study is different from those already done by some research institutions, advocacy groups, and intergovern-

mental organizations because we answer this question about the lessons of NAFTA by analyzing what conventional NAFTA studies pass over. Our analysis focuses on people, their communities, and the choices they make as they attempt to negotiate their social and economic environments. We emphasize changes in household income, paychecks and productivity, rural employment, and agricultural production and land use, and the overall effect of these changes on migration and environmental quality. We then examine how NAFTA's trade rules and institutions played a role in these changes. In short, while most positive analyses focus on the macro level and most negative analyses rely only on losses and not gains, our analysis provides a rigorous and balanced assessment of NAFTA by focusing on its effects on people's lives, livelihoods, and households.

Our second objective is to offer insights to other countries, particularly in Latin America, that are interested in strengthening their bilateral and multilateral economic ties within the region. While not entirely similar, Mexico's economic and cultural history and rich ecosystem are more closely linked to those of its Latin American neighbors than to those of the United States or Canada. These similarities mean that NAFTA's record can offer insights to other countries as they consider the potential costs and benefits of agreements such as CAFTA and FTAA.

#### **OUR CONCLUSIONS**

■ NAFTA has not helped the Mexican economy keep pace with the growing demand for jobs. Unprecedented growth in trade, increasing productivity, and a surge in both portfolio and foreign direct investment have led to an increase of 500,000 jobs in manufacturing from 1994 to

2002. The agricultural sector, where almost a fifth of Mexicans still work, has lost 1.3 million jobs since 1994.

- Real wages for most Mexicans today are lower than they were when NAFTA took effect. However, this setback in wages was caused by the peso crisis of 1994–1995—not by NAFTA. That said, the productivity growth that has occurred over the last decade has not translated into growth in wages. Despite predictions to the contrary, Mexican wages have not converged with U.S. wages.
- NAFTA has not stemmed the flow of poor Mexicans into the United States in search of jobs; in fact, there has been a dramatic rise in the number of migrants to the United States, despite an unprecedented increase in border control measures. Historical migration patterns, the peso crisis, and the pull of employment opportunities in the United States provide better explanations for the increase in migration than NAFTA itself.
- The fear of a “race to the bottom” in environmental regulation has proved unfounded. At this point some elements of Mexico’s economy are dirtier and some are cleaner. The Mexican government estimates that annual pollution damages over the past decade exceeded US\$36 billion per year. This damage to the environment is greater than the economic gains from the growth of trade and of the economy as a whole. More specifically, enactment of NAFTA accelerated changes in commercial farming practices that have put Mexico’s diverse ecosystem at great risk of contamination from concentrations of nitrogen and other chemicals commonly used in modern farming.
- Mexico’s evolution toward a modern, export-oriented agricultural sector has also failed to deliver the anticipated environmental benefits of reduced deforestation and tillage. Rural farmers have replaced lost income caused by the collapse in commodity prices by farming more marginal

land, a practice that has resulted in an average deforestation rate of more than 630,000 hectares per year since 1993 in the biologically rich regions of southern Mexico.

Put simply, NAFTA has been neither the disaster its opponents predicted nor the savior hailed by its supporters. But while NAFTA’s overall impact may be muddled, for Mexico’s rural households the picture is clear—and bleak. NAFTA has accelerated Mexico’s transition to a liberalized economy without creating the necessary conditions for the public and private sectors to respond to the economic, social, and environmental shocks of trading with two of the biggest economies in the world. Mexico’s most vulnerable citizens have faced a maelstrom of change beyond their capacity, or that of their government, to control.

In response to the growing challenges facing rural Mexico, many households have developed survival strategies to meet basic subsistence needs. These strategies include a mix of increased cultivation of basic crops and off-farm employment, often in the informal sector, and in some cases in maquiladora plants that have relocated away from the northern border into the hinterlands. Many rural workers have nonagricultural activities as their primary occupations, while relying on sporadic agricultural work to supplement their incomes. Mexico’s agricultural policies provide commercial farmers with substantial support, but do not benefit subsistence farmers. More than ever, families rely on remittances sent home by those who migrate to the United States, with or without legal status. Finally, to reduce expenses, rural households also fall back on more traditional approaches to heating their homes and feeding their families. The net environmental loss associated with an increase in the farming of marginal land and illegal logging and poaching for fuel and food places some of the most important biological reserves in the hemisphere at risk of irreparable damage.

Trade agreements do not need to result in this kind of hardship for the world’s rural poor. Negotiated

properly, they can open doors to new markets while providing adequate protections from the stress associated with exposure to global competition and the increased pressure on natural resources. Trade should not be seen as an end in itself; instead, it should be used as a tool to strengthen economies through the operation of comparative advantage. At the same time, governments must respond to economic opening with effective policies, such as the deployment of social safety nets and trade adjustment assistance, and develop and implement programs that protect labor rights and the environment. As nations consider how best to use trade agreements to foster development, we offer the following insights:

- Developing countries interested in freer trade should negotiate longer and more gradual tariff reduction schedules for agricultural products imported from wealthy countries, and negotiate special safeguards to protect against the dumping of subsidized crops. The need for “shock absorbers” is especially great for the poorest developing countries where agriculture is a principal source of employment. Regional and bilateral trade agreements should not allow developed countries to duck the crucial issue of producer subsidies in agriculture.
- Trade agreements should allow developing countries to adopt policies that maximize employment gains from trade by promoting the development of domestic suppliers and that do not favor imported components. Whether the suppliers are owned by domestic or foreign firms is not relevant; what is relevant is whether the suppliers create jobs.
- Developing countries should bargain for meaningful financial support for transitional trade adjustment assistance, from trading partners and from international donor organizations. Such adjustment assistance should include training for workers and subsistence farmers in new skills and access to credit that allows and encourages small farmers to develop economically and environmentally sound farming practices. Assistance to the rural poor should be aimed at allowing them to transition to livelihoods that are sustainable in the modern global market—and should acknowledge that the process of urbanization will continue.
- Developing countries should adopt and implement policies that help distribute the gains from trade more equitably, through better tax and minimum wage policies and the expansion of freedom of association and collective bargaining rights. They should commit to national action plans that build environmental infrastructure. Because these policies may be valued by their wealthier trading partners, developing countries may win additional advantages in trade agreements by making these commitments.
- To minimize the environmental implications of trade liberalization for agriculture, and the tendency of export growers to adopt chemical-intensive production methods, trade agreements should set standards that allow developing countries to take advantage of the growing demand for organic food products.
- The movement of workers is a powerful social and economic force, and countries at all levels of development have good reason to discuss temporary migration in a variety of contexts, which may include future free-trade negotiations. However, given the political sensitivity of the issue, migration should not be allowed to jeopardize agreements on the movement of goods and capital and on other ways of providing services.

#### **LONG-TERM STRATEGIES**

Free-trade agreements should not be thought of as an end in themselves; nor should they be loaded with unrealistic expectations. Instead, they should be viewed as part of a larger effort toward substantive bilateral and regional cooperation toward

common goals. Migration, labor, and environmental protection are examples of topics on which deeper cooperation is sorely needed.

Trade liberalization is facing a crisis of legitimacy among people around the world, from rural farmers in Latin America to cotton producers in Africa to manufacturing workers in the United States and Europe. Governments can win back public support for new trade agreements, but they must change their current tactics. First, they must stop making empty promises that trade liberalization alone will bring new jobs or clean environments, or stem the flow of illegal migration. Second, they must enhance long-term development and avoid unnecessary setbacks by strengthening their domestic economies' capacity to respond to shocks when exposed to the global marketplace. The needs of developing countries must be taken into account in trade negotiations in meaningful ways that create real opportunities for development and growth, so that these countries' citizens can also become consumers in the global economy. That, in the long-term, is how everyone will achieve greater prosperity.

## NOTES

- 1 Ministerial Declaration, First Summit of the Americas, Miami, Fla., 1994, available at [www.ftaa-alca.org/ministerials/miami\\_e.asp](http://www.ftaa-alca.org/ministerials/miami_e.asp).
- 2 Carlos Salinas de Gortari, *Mexico: The Policy and Politics of Modernization* (Barcelona, Spain: Plaza & Janes, 2002). See especially parts 1 and 2.