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A NORTH AMERICAN FREE TRADE AREA:

AN OVERVIEW OF ISSUES AND OPINIONS

James E. McConnell
Canada-United States Trade Center
Department of Geography
University at Buffalo
New York 14261

Albert Michaels
Department of History
University at Buffalo
New York 14260

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James E. McConnell and Albert Michaels

ABSTRACT. The purpose of this paper is to provide an overview of the issues and concerns that are likely to be crucial in determining the outcome of negotiations among officials from Canada, Mexico, and the United States to create a North American free trade area. At the outset, the authors outline some of the key conditions and events that led to the development of closer relationships among the three countries during the middle and latter parts of the decade of the 1980s. Despite their misgivings about each other and their wariness of entanglements, the three North American countries began to move closer together in several important spheres during the latter part of the 1980s. Perhaps the most noticeable evidence of the increased ties among the three includes the expansion of commodity trade and capital investment flows; in 1986, Mexico joined Canada and the U.S. as a member of the GATT; later, in 1989, Canada joined the Organization of American States and entered into a formal trade pact with its southern neighbor; and, the new president of Mexico began to implement a remarkable plan for the country's economic recovery and to make overtures to the U.S. about entering into a more formal trade and investment agreement.

The next two sections of the paper contrast on a country-by-country basis the factors that are working for and against the creation of a free trade area The analysis suggests that strong resistance exists in each of the three countries for a trade accord, and that this resistance is coming primarily from organized labor groups, environmentalists, and some regional businesses that feel threatened by reducing trade barriers with Mexico. In contrast, the factors that favor the creation of such a trilateral region include the strong economic complementarity that already exists among the three countries; the desire on the part of the three to at least attempt to work within the confines of the GATT charter to develop a workable trade pact; and the realization that it is in the best interests of the hemisphere to assist Mexico in its efforts to transform its economy and to create a stable political environment.

In the final section of the paper the authors present six interrelated factors that are likely to influence the probability that a trilateral trade agreement will be reached by the three North American countries. Three of the factors are "internal" to the region, and include: the perceived outcome of President Salinas' efforts to transform Mexican economic policy; economic conditions and political considerations in Canada and the U.S. over the next few months; and the specific issues that are actually negotiated in the free trade talks. In addition, three factors "external" to the trilateral region may also influence the outcome of the negotiations, and these are: what happens to the ongoing discussions of the Uruguay Round of the GATT; the rising tide of sentiment in Europe and East Asia of relying upon regional solutions to resolve global trade issues; and mounting pressure elsewhere within the Western Hemisphere to pursue formal trade agreements with the U.S.

INTRODUCTION

The opportunity to create a trinational market area of 360 million people with a combined purchasing power approaching $6 trillion is becoming increasingly attractive to many constituencies in Canada, Mexico, and the United States. Underlying this enthusiasm are two important considerations. First, recently stalled negotiations among the members of the GATT and the forging of closer economic ties among nations in the European Community and in the Pacific Rim appear to be moving the global community increasingly toward the formation of regional trading blocs. In contrast to the nondiscriminatory principles of GATT, regional trading blocs are founded upon the principle of preferences. Such moves toward regionalism in international trade and investment transactions tend to generate reciprocal actions by other nations as a mechanism of defense. Thus, efforts to create a North American Free Trade Area (NAFTA) can be viewed as a means of countering bloc formations in Europe and Asia.

A second factor that underlies enthusiasm for an NAFTA is the adage from geopolitics that the geographic proximity of nations plays an important role in determining the foreign policy relationships among these same nations. An overwhelming reason for moving toward a North American trade area is the physical proximity of these countries. By adjusting and harmonizing various rules, regulations, and standards, the economic heartlands of these three countries--stretching some 2000 air miles from southern Ontario to Mexico City--could be integrated by a dense and low-cost network of transportation and communications that is unequalled elsewhere in the world.

Although the prospects for a trinational commercial union in North America seem bright at the present time, the issue is not without controversy and potential roadblocks. The purpose of this paper, therefore, is to provide an overview of the key issues and concerns that will likely be crucial in determining the outcome of negotiations among officials from the three countries.

PRECIPITATING EVENTS

On September 25, 1990, President George Bush asked the United States Congress for authority to negotiate a free trade agreement with Mexico. President Salinas of Mexico had visited the United States in June, 1990, and had requested a free trade pact between the two countries. After President Bush's statement, the Canadian Prime Minister, Brian Mulroney, sent letters to Bush and Salinas expressing Canada's interest in joining free trade negotiations between their two countries [Buffalo News, September 25, 1990]. Ending months of speculation, Canada, Mexico, and the United States announced on February 5, 1991 their intention to enter into trilateral negotiations aimed at creating a North American free trade area.

It would appear, therefore, that events are moving the United States close to the desire expressed by President Ronald Reagan in his last State of the Union message. "Our goal," Reagan said, "must be a day when the free flow of trade . . . from the tip of Tierra del Fuego to the Arctic Circle . . . unites the people of the Western Hemisphere in a bond of mutually beneficial exchange" [Latin American Working Group, n.d., p. 7]. The willingness of Mexico and Canada to discuss entering into a free trade accord was a total change from a decade earlier when both countries seemed determinedly opposed to any such agreement.

This change has taken place gradually over the past 25 years. In 1965 Mexico took a major step away from economic protectionism by creating the Border Industrial Parks, or Maquiladora program. The Mexican government hoped that these parks would stimulate economic development in the then stagnant northern part of Mexico. Previously, the Mexicans had required that its own nationals control the majority interest in any company operating in Mexico. The new program allowed 100 percent foreign-owned production facilities on the condition that the total output of these facilities be exported. Machinery, raw materials, and semi-finished components could be imported for these factories without duties. Companies had to post a special bond promising to re-export all of the finished products from these facilities. The program proved very successful, and by 1990 it had created almost 500,000 jobs. It accounted for 80 percent of Mexico's manufactured exports and nearly 40 percent of its sales to the United States. The Industrial Parks provide the bulk of Mexico's foreign exchange earnings, and practically all new Mexican jobs created since 1980 are in this area [Drucker, 1990].

Like Mexico, Canada was forced to abandon its traditional policies by political and economic events. Great Britain joined the European Economic Community in 1972. At this point, Britain abandoned all Commonwealth preferences in trade, which proved to be a tremendous disappointment to those Canadians who traditionally had seen themselves as closer to Great Britain than to the United States. The British decision strengthened those Canadians who wanted to draw closer to the United States and reduce the trade barriers between the two nations. It only made sense for Canada to compensate for the British move to Europe by moving closer to the United States, although even the most enthusiastic Canadian proponents of US-Canadian free trade had to realize that the balance of power that existed within the EEC would be lacking in any US-Canadian agreement. Canadian Minister of External Affairs, Mitchell Sharp, defined the problem when he stated: "There is certain balance in the decision-making of the European Economic Community that would not be conceivable in a bilateral Canada-US arrangement" [Hendrickson, 1981, p. 41].

The 1973 oil shock greatly facilitated discussion of closer ties within North America. The Arab oil embargo created a fear in the industrialized world that oil was scarce, and demonstrated that supplies were politically vulnerable. OPEC had succeeded in wresting control from the western companies. The cartel clearly intended to be paid dearly for its valuable resource and to control its production for its own advantage. After the Arab-Israeli War broke out in October, 1973, the OPEC countries dictated to the oil companies just what the price of oil would be. The benchmark price of oil rose from $5.40 a barrel in 1974 to $14.54 a barrel in October, 1979. The fall of the Shah's government in Iran lead to a sharp drop in Iranian exports and the price of oil doubled again to the $30+ range. Fearing both rising costs and insecure supplies, the United States began to look toward its neighbors, Canada and Mexico. Both had large oil reserves (Mexico is reported to have reserves as high as 260 million barrels), both exported oil, and neither belonged to OPEC [Lewis, 1980]. Mexico seemed to be the answer to the United States' energy problem.

Pressure began to build in the United States for closer linkages with Canada and Mexico. Senator Max Baucus (D., Montana) stated that "the simple fact is that our own needs have propelled us to look more closely than ever before at North America as an economic unit. And, not to the surprise of experts, we are discovering the strength of this continent as an economic entity. Without doubt, the U.S., Canada, and Mexico, taken together, form the largest single and most vital economic trading bloc in the world" [Henrikson, 1981, p. 38].

In 1979, anti-American revolutionaries seized power in oil-rich Iran, increasing the pressure from Senators Domenici, Baucus, and others to investigate the possibilities of a North American accord. The United States Congress requested that the President's Special Trade Representative conduct a study of how a trilateral agreement between Mexico and Canada would function, and the United States Senate created a caucus on North America. These efforts did not lead to any significant proposals, yet movement toward cooperation was occurring on a regional level. In the late 1970s, frequent cross-border negotiations took place between US state governors and their Mexican and Canadian counterparts on trans-national problems such as water, energy use, and the environment [James, 1980].

Fortune magazine published a perceptive and pessimistic article in 1979 on the current prospects for a free trade agreement. The author, Herbert E. Meyer, wrote that US proponents of free trade were principally motivated by the desire to increase the flow of oil and natural gas from Canada and Mexico to the United States. He pointed out that the Mexicans and Canadians were not sympathetic to US needs. Both Canada and Mexico had protectionist legislation that gave them large surpluses in their trade with the United States. The Canadians feared that US branch plants in Canada could not compete with their US counterparts and would inevitably close down. Mexican industrialists doubted that they could compete with US manufacturers in their own market because of American producers' technological edge. Technological backwardness also explained Mexico's refusal to join GATT. Overall, Meyer argued that the size and power of the United States precluded any agreement. North American free trade would be closer to "COMECON" than to the EEC, and the Canadians and Mexicans "just won't buy it." Meyer concluded that North American free trade amounted to "an idea whose time has not yet arrived" [Meyer, 1979, pp. 118 - 124].

The proponents of free trade, mainly politicians from border states, persisted in their advocacy. Former governor Ronald Reagan (R., Calif.) entered the 1980 presidential race with a speech from the New York Hilton. The only major foreign policy recommendation in this speech was a call for a "North American accord." He promised that if he were elected president, he would promote such an alliance, which he called the key to the future security of all three nations. Reagan said that "we live on a continent whose three countries possess the assets to make it the strongest, most prosperous, and self-sufficient area on earth. Within the borders of this North American continent are the food, resources, technology, and undeveloped territory which properly managed, could dramatically improve the quality of life of all its inhabitants . . . It may take 100 years, but we can dare to dream that at some future date the map of the world might show the North American continent as one in which the peoples of its three strong countries flow more freely across the present borders than they do today" [New York Times, November 14, 1979]. Reagan did not suggest any specific measures to implement this program.

On the other side of the US political spectrum, Governor Edmond Brown Jr. (D., Calif.) also made a North American accord a part of his presidential agenda. In a speech before the 1980 Democratic convention at New York's Madison Square Garden, Governor Brown advocated a "type of economic community that will bring along with us our brothers and sisters who share this land of North America; Mexicans, Canadians, native Americans--North and South--all are part of our destiny and it is time that we recognize that we are part of theirs" [New York Times, "Brown Advocates Closer Ties with Mexico," August 14, 1980].

The events of the year proved Meyer rather than the presidential hopefuls to be correct. In May, Prime Minister Trudeau of Canada and President Lopez Portillo of Mexico met to discuss energy cooperation. They both rejected the idea of a North America accord. They agreed that such a pact would only accentuate US economic dominance [Riding, 1980; and James, 1980].

Before assuming the presidency, Ronald Reagan traveled to Ciudad Jurez to meet with Mexican President Lopez Portillo to discuss regional cooperation. Lopez Portillo was less than enthusiastic. The Wall Street Journal explained Mexican reluctance as related to three factors: Mexican historical anger, fear that its industry could not compete with its more sophisticated northern neighbors, and Mexican suspicion that a North American accord would only serve the energy interests of the United States at Mexico's expense [Getschow, 1981]. The Mexican position reflected a new awareness of potential power. Lopez Portillo believed that Mexico's newly discovered oil reserves would usher in a new era of economic growth. Mexico had the seventh largest oil reserve in the world and would soon become fourth in oil production. Lopez Portillo claimed that he was determined to maximize Mexico's energy advantage. He believed that an energy accord with the United States would only limit Mexico's development options. In the end, he refused to consider abandoning Mexico's traditional policy of protectionism and resisted US pressure to join GATT.

The reluctance of Canada, like that of Mexico, was partially based upon tradition. The Canadians had always suspected the motives of the United States and feared US dominance. Canada was reluctant to forego its traditional closeness to Great Britain and its European markets even after Great Britain joined the EEC. In addition, the Canadians were not enthusiastic about becoming involved in Latin America. They had earlier refused to become a full member of the Organization of American States. The Canadian Department of External

Affairs did not even have a Latin American division until 1961, yet in 1972 the Canadians did accept observer status at the OAS, and Canada subsequently joined the Inter-American Development Bank to which it contributed $1 billion in the 1970s [Jackson, 1982, pp. 15 - 17]. In 1980, historian Robin Winks wrote that "most Canadians have concluded that they have little in common with Latin America. Canadians saw their tradition as evolutionary rather than revolutionary and their social and political structures as democratic as contrasted to those of the Latins which were non-democratic. The English-speaking Canadians feared that any implication of cultural proximity might be used by Quebecers who were inclined to insist that they were Latins too" [Winks, 1981, pp. 25 - 29]. The Canadians disliked the 1947 Rio Pact with its provisions for collective security. The Canadian government was apprehensive that Canadian foreign policy disagreements with the United States would be brought to a head at the OAS, and was also concerned that if Canada were to join the OAS, it would raise unrealistic expectations of Canadian aid to Latin America [Stephen Banker, 1982, pp. 23 - 26]. Finally, some Canadians, like some Mexicans, feared that US political, economic, and cultural domination would undermine its more compassionate system of government and way of life. Even the Conservative Brian Mulroney announced after taking office that "free trade affects Canadian sovereignty and we will have none of it" [Malloy and Urquhart, 1990].

MOVEMENTS TOWARD CLOSER INTERACTION

Despite their misgivings about each other and their wariness of entanglements, the three North Ameircan countries began to move closer together in several important economic spheres during the latter part of the 1980s. Most notable have been the successes made in increasing commodity trade linkages. While trade between Canada and the United States more than doubled to some $170 billion over the decade of the 1980s, important advances in trade were also being forged between Mexico and its two neighbors to the north. More specifically, by 1990, Mexico's two-way trade with Canada had increased to over $2 billion, while the value of its shipments to and from the United States had risen to some $50 billion. Thus, as the three countries moved into the decade of the 1990s, the most important export and import market by value of shipments for both Mexico and Canda was the United States; the first- and third-ranked export markets for the U.S. were Canada and Mexico, respectively; and the second- and third-ranked import markets for the U.S. were Canada and Mexico, respectively [International Monetary Fund, 1990, pp. 123-125, 279-280, and 402-404).

In addition to strengthening trade ties, the three countries also increased their ownership of assets in each other's territory. For example, of the total stock of foreign direct investment in Mexico, about two-thirds of it is owned by the U.S. and 2.4 percent by Canada; approximately 70 percent of all Canada's foreign direct investment is in the U.S.; and the value of Mexican assets in the U.S. is estimated to be from $40 billion to over $80 billion [Investment Canada, 1990, p. 2].

Given their relative proximity in North America and their strong economic ties to the United States, it was perhaps inevitable that Canada and Mexico would grow closer together. There was a belief in both countries that they had much in common in their opposition to the United States. Both countries opposed the United States' boycott of Cuba. After 1959, Canada and Mexico were the only Western Hemispheric countries that still maintained relations with Cuba. Both opposed Ronald Reagan's policies in El Salvador and Nicaragua. They argued that the Central American turmoil had its origins in the region's underlying social and economic problems rather than in Cuban or Soviet intervention. Furthermore, the Canadians sought a natural ally in Mexico. It was a constant objective of Canadian foreign policy to be not "left alone with the United States" [Hendrikson, 1981, p. 27]. On March 30, 1973, the Toronto Globe and Mail editorialized that: "If Canada is to pursue an interest in Latin America on a bilateral basis . . . Mexico is a logical country to begin with." On October 15, 1975, the Toronto Star carried an article in which the argument was made that "there is one thing that nearness to the American giant has done for Canada and Mexico; it has made them feel like first cousins. Each one feels she must do something about US domination." Canada and Mexico were drawing closer together, and Canada was losing its reluctance to become involved in Latin America.

In 1989, Canada finally joined the Organization of American States. The Latin American nations had supported this move because they hoped that Canada would prove to be a "counterweight" to the United States [Louis H. Diuguid, 1989]. Canada's decision to join the OAS did not result from increased Canadian trade with Latin America, but it did signal a new orientation away from Europe on the part of Canadian foreign policy. It also indicated that Canada, adrift from the British Commonwealth, understood that it had to grow closer to its continental neighbors as a defense against the growing regional trade blocs in Europe and the Pacific Rim.

In the late 1980s, first Canada and then Mexico began to reconsider a North American trade accord. The Canadians signed a free trade accord with the United States in 1988. This encouraged the Mexicans to believe that Mexico could look to Canada for advice on negotiating with the United States. Mexican President Salinas travelled to the United States in June, 1990, and called for a free trade accord with the United States. Presidents Bush and Salinas then issued a joint statement agreeing to negotiate a US-Mexico trade agreement. In July, the Mexican Senate endorsed the proposal. In September, 1990, the Economist quoted President Salinas as saying that Mexico will be added to the American-Canadian free trade area in "much less than three years" [The Economist, 1990]. Six days later, the New York Times reported that President Bush, "acting more swiftly that expected, will ask Congress next week for authority to negotiate a comprehensive free trade agreement with Mexico." The Times predicted that if Congress approved, negotiations would begin sometime in April, 1991 [Farnsworth, 1990]. In 1990, Prime Minister Mulroney of Canada travelled to Mexico and declared that he was not against a free trade zone involving Mexico, the US, and Canada. Previously, no elected Canadian official had ever suggested a North American "scheme" [Hendrickson, 1981]. On September 24, 1990, the Canadian government asked to join the forthcoming talks between Mexico and the United States [Buffalo News, 1990].

Many reasons help explain the drastic change in Canadian and Mexican positions on a free trade accord. For example, the end of the Cold War had cooled the Central American crisis and lessened the tension among the United States, Canada, and Mexico. The Canadians had rejected the Lake Meech accord and Quebec was moving closer to the United States. The 1990 Ontario elections were won by the anti-free trade Socialist New Democratic party. This victory will probably strengthen the determination of separatist elements in Quebec to minimize their relations with Canada and draw even closer to the United States. In the United States, state governors continued to make bilateral agreements with their Mexican and Canadian counterparts. These agreements had the effect of reducing areas of disagreement between the United States and its two neighbors, as well as establishing a precedence of successful bilateral negotiation. The US governors sought to encourage cross-border trade, investment, and transportation links. The governors of California, Arizona, New Mexico, and Texas meet regularly with their six Mexican counterparts in a Border Governors conference. The governors of Washington and British Columbia launched a Pacific Northwest Economic Partnership in which Oregon, Idaho, and Alberta have also evinced an interest. They have named their region Cascadia [Holstein, et.al., 1990, pp. 40 - 43].

By 1989 the United States and Canada had formally entered into a Free Trade Agreement, which called for the gradual and systematic reduction of most trade barriers. The Mexican change of heart was more radical and resulted from serious and deep structural economic difficulties. The failure of its old protectionist economic policy had led Mexico to seek a way out of its most serious economic crisis since the revolution of 1910. The stagnant Mexican economy needed to create one million new jobs a year. Free trade seemed to be the only way to achieve this. President Lopez Portillo (1974 - 1982) had dissipated oil revenues and carried out ill-considered reforms that led to a massive capital flight. He took "Mexico to its apogee in statism" [Wilkie, 1990, p. 22]. Public- sector jobs rose from 2.2 million to 4 million. Public-sector employees accounted for 20 percent of salaried Mexicans, collecting 40 percent of all salaries. Lopez Portillo began a cycle of increased money supply, inflation, and foreign loans to replace declining export revenue and currency devaluation. During his six-year term, inflation averaged 36 percent per year, and reached a high of 59 percent in 1982.

Faced with declining oil revenues, the Mexican government was unable to service its debt. In 1982, the government declared an internal emergency, nationalized the commercial banking system, froze all dollar accounts, converted dollar accounts to pesos, and, at the same time, devalued the peso. The result was that Mexico suffered a flight of private captial of over $8 billion [Wilke, 1990, pp. 23-28]. Oil revenues were wasted and corruption reached unprecedented heights. The public debt rose to $79.3 million dollars, an increase of 114 percent. Most important, the economic crisis undermined the Mexican self-confidence in the late 1970s, which had encouraged Mexico to reject US overtures on free trade. Lopez Portillo's successor, Miguel de la Madrid (1982 - 1988), began economic liberalization. In 1986, Mexico finally joined GATT. The next year, the United States and Mexico signed an understanding "concerning a framework of principles and procedures for consultations regarding trade and investment relations." The agreement calls for regular meetings to deal with specific trade problems between the two countries [Farnsworth, 1989].

In 1988, Carlos Salinas de Gortari became president of Mexico. Salinas had been budget minister and architect of Lopez Portillo's economic liberalization. He had three degrees from Harvard University and a solid grasp of economics. Only 40 years old, Salinas considered himself to be the embodiment of a new generation of Mexican politicians. He was determined to continue the re-orientation of Mexican economic policy, which he had begun under de la Madrid. He assembled a team of brilliant technocrats: Jaime Serra Puche, the new Minister of

Trade, who had a doctorate of economics from Yale and was a close friend of his US counterpart, Robert Mosbacher; and Pedro Aspe, Minister of Finance, who has been called by Jude Wannaski "the best Minister of Finance in the world" [Manniski, 1990]. Their policy has aptly been called "Salinastroika" [Goldman, 1990, pp. 45 - 54]. They lowered maximum tariff rates and removed most non-tariff barriers. They "defined the minimum debt relief which was needed to sustain Mexican economic recovery and persuaded the United States to incorporate their ideas into what is now called the Brady Plan" [Storga, 1990]. The bankrupt and inefficient Telefonos de Mexico was to be sold to private investors. Salinas began by liberalizing Mexico's foreign investment code and privatizing state-owned industry, including some within the hitherto sacrosanct petro-chemical sector. The banks that were nationalized under Lopez Portillo were now to be returned to the private sector. Under the new laws, foreign investors could account for up to 30 percent of the bank's ownership.

Like Mulroney in Canada, Salinas initially dismissed any idea of free trade with the United States. In a January, 1988, interview, he used language reminiscent of Lopez Portillo to reject the idea. "I am not," he said, "in favor of any free trade or common market plan because there is such a different economic level between the US and Mexico" [Rother, 1990]. Within a year he had reversed his position. The Mexicans watched, with alarm, the growing regionalization in Europe and Eastern Asia. In January, 1990, Salinas had visited Western Europe in search of investment capital. His meetings with Helmut Kohl and Margaret Thatcher ended in disappointment. Salinas found that the European leaders were fascinated with Eastern Europe and had little time for the rest of the world [Pastor, 1990, pp. 27 - 31]. Salinas gave an interview to the Wall Street Journal in which he pointedly drew parallels between Mexico and Eastern Europe. He said that Eastern Europe would now provide West Germany with "a tremendous pool of skilled, cheap labor. This is something you do not see in the US - Canadian situation." Salinas was clearly offering Mexico as the Eastern Europe of a North American economic community [Wall Street Journal, 1990]. Another factor influencing a more positive approach to free trade was Mexican disappointment with the initial result of the new reforms. Mexico's planners had hoped that the new reforms would lead to a large influx of foreign capital. Although there was substantial improvement in Mexico's balance of payments, the results had not met their expectations. They now gambled that a US-Mexican free trade accord would increase the confidence of the international investment community in Mexico. They were desperate to increase productivity and reduce inflation.

The Iraqi invasion of Kuwait also played a role in increasing the possibility for a North American trade accord. President Bush had an added incentive to maximize US access to Mexican and Canadian energy supplies. On the other hand, rising energy prices increased Mexico's self-confidence, and Mexicans believed that they could now enter negotiations with the United States from an increasingly powerful position.

FACTORS OPPOSING A NORTH AMERICAN FREE TRADE AREA

1. Opposition in Mexico

Powerful opposition to a free trade accord continues to exist in Mexico. The Mexican political Left, gathered around Cuauhtemoc Cardenas and the Party of the Democratic Revolution, has expressed an ambivalent interest in free trade. Writing in a United States journal, Cardenas has accused Salinas of "unprecedented subordination" to US interests in the areas of drugs, immigration, and industrialization. He has accused Salinas of gambling that "he can buy off" Mexico's middle and lower classes with a large influx of resources from the United States. According to Cardenas, Salinas is hoping that his economic reforms will bring about sufficient prosperity for the official party to remain in power. He contended that the government is holding off democratic political reforms in the hope that prosperity will make them irrelevant for the power structure. Salinas was offering the United States long-desired economic concessions, but, in return, the United States would have to accept the existing Mexican political system, "warts and all." Cardenas accused the Mexican government of trying to integrate economically "behind the backs of the Mexican people." Cardenas insisted that economic reform should be tied to social equity, political democracy, and decentralization. He warned the United States that the economic reforms would not take hold without a broad consensus of support from the Mexican people [Cardenas, 1990]. Cardenas' principal advisor, Munoz Ledo, has endorsed free trade, at least in principle. Like Cardenas, he has expressed concern about the speed of the implementation process and its links to democratization [Asman, 1990].

For many union leaders in Mexico, a free trade deal would flood the country with imports, create chronic unemployment, open the nation to increasing control from the outside world, and eventually lead to the exploitation of Mexican workers. Interestingly, even AFL-CIO officials in the U.S. are supporting their Mexican counterparts by claiming that a free trade agreement between Mexico and the U.S. will "do little to improve the lives of Mexican workers because their low wages must be maintained to attract continued U.S. investment in Mexico" [International Trade Reporter, 1991, p. 19]. Moreover, Mexico has had traditional hostility toward foreign investment in such areas as natural resources, banking, and services. Not only are many Mexicans fearful of external control over vital resources and sectors (Mexico has a long tradition of hostility to foreign bosses), they are also concerned that their relatively small manufacturing and service establishments--long protected by high tariffs--will not be able to complete against the larger multinational corporations from Canada and the U.S.

Mexicans from all sides of the political spectrum are deeply concerned that the Salinas government will give up Mexico's traditional control of its oil industry, railroads, and electricity. They are already alarmed over concessions made in the petro-chemical industry. A well known Mexico City columnist, Gaston Garcia Cantu, has described recent events as "an annexation similar to that of Texas in 1836 and a betrayal of the rest of Latin America." Influential Mexican social scientist Lorenzo Meyer wrote in the newspaper Excelsior that "Mexico should take decisions knowing as much as possible what we will gain and lose by integrating ourselves with the economy of a great power from which we previously considered it our historic and patriotic duty to protect and separate ourselves" [Rother, 1990]. The oil industry is a particularly sensitive issue. The Mexicans nationalized the foreign-owned oil companies in 1938, and there has been a state monopoly ever since. However, the oil industry has been hampered by inefficiency and corruption. It is desperately in need of foreign technology and investment. The United States has a strong vested interest in expanding Mexico's oil production, and it would seem logical for US trade negotiators to press this point, although Mexicans are likely to refuse. Francisco Rojas, director general of Pemex, has said that Mexico will not modify long standing strictures on foreign equity participation. Mr. Rojas has repeatedly insisted that "oil is and will continue to be a resource of the state" [Moffett, 1990]. On November 1, 1990, President Salinas vigorously promised a large group of Mexican politicians that Mexico would make no compromise on the oil issue. He said, "I want to confirm the fact that Mexico will maintain its ownership and complete dominion over hydrocarbons" [Uhlig, 1990].

Conservative business interests in Central Mexico, especially in the highly protected areas of textiles and leather goods, will certainly oppose free trade. The financial and service sectors in Mexico City will also be threatened by foreign competition. Most Mexican firms are simply too small to compete with US-based multinationals. US negotiators are likely to insist upon a comprehensive trade and investment package, including the lifting of the remaining heavy foreign investment restrictions and increasing access to Mexican markets for US services. In addition, US imports could do serious damage to Mexican agricultural interests, specifically in grain, poultry, and livestock. The Mexican chemical industry could also be negatively affected. Currently the average Mexican duty on chemical imports is 20 percent. If this tariff is significantly reduced under a free trade agreement, the Mexican chemical industry may have great difficulty remaining competitive.

Another thorny problem will be bilateral negotiations over extensive liberalization of US laws governing movement of labor. The Mexican co-ordinator general of the free trade accord of the Mexican Commerce Ministry has claimed, "Mexico does not want to export workers, but wants to export goods . . We want to provide them the opportunity to work here. We would not put on the table the idea that the FTA (foreign trade agreement) should lift all immigration barriers" [Upendra Nath Mishra, 1990]. Yet more than 1 million Mexicans work in the United States illegally, and some US officials believe that Mexico would like to include labor as a service during the up-coming free trade negotiations.

2. Opposition in the United States

Although a bilateral trade agreement with Mexico and a trilateral agreement involving Mexico and Canada have strong support from the Bush administration and from most American businesses, very strong objections to such accords are voiced from several quarters of the country. For example, many critics are reluctant to move into such negotiations so quickly that the ongoing multilateral trade talks (which are currently stalled in Geneva) of the GATT members become permanently derailed, and that the U.S. would then be viewed as attempting to create a "fortress North America" rather than a nondiscriminating global environment for trade.

Other major U.S. complaints come from regional businesses and labor constituents who see free trade with Mexico as a major threat to their livelihood. Many are concerned that, because of the huge differences in the size and level of economic development of the U.S. and Mexican economies, the U.S. will have to accept an asymmetrical agreement in which Mexican tariff reductions and other trade-related matters will be phased in more slowly than on the U.S. side. Moreover, the AFL-CIO claims that "a free trade agreement will only encourage greater capital outflows from the U.S. and bring about a further increase in imports from Mexico, further harming the U.S. industrial base" [New York Times, 1990]. Even U.S. automakers are worried about "made-in-Mexico Japanese cars heading north to compete with Canada- and U.S.-made vehicles" [Baker, et.al., 1990, p. 42].

It is also likely that strong and well-organized opposition will be heard from various industrial groups and labor unions in the "rust belt" states. For example, groups such as the Religion and Labor Council of Kansas City and the Federation for Industrial Retention and Renewal in Chicago are gearing up for a fight in Congress against free trade with Mexico. The basic position of such groups is that a free trade pact with Mexico would spark a second wave of U.S. investment in Mexico, beyond the maquiladoras clustered along the border, which would then result in the further relocation of production and assembly operations southward. As argued recently by an economist for the United Auto Workers, a U.S.-Mexican trade accord "is an extension of the southern strategy to move manufacturing to the low-wage, non-union Sunbelt" [Holstein and Borrus, 1990, p. 113]. Other unions argue that not only will a trade pack with Mexico cost U.S. jobs, it will also put new downward pressures on manufacturing wages in the U.S. Parenthetically, it is interesting and important to note that these same arguments were used in 1987 and 1988 by individuals in Canada who were opposed to the creation of the Canada-U.S. Free Trade Agreement. Despite claims to the contrary, most of these critics have no doubts that the low-cost labor in Mexico will cause some shifting of economic activity and jobs--particularly blue-collar ones--south of the border. The unknown question is how many such jobs will be lost.

Such concerns about job migrations have even caused some to wonder how much political support will exist for a trilateral agreement in border cities, such as Buffalo, New York, which have presumably benefitted in several ways from the new Canada-U.S. trade pact. The logic is that legislators from these border locations, who may have strongly supported a trade accord with Canada, are likely to be opposed to a similar pact with Mexico for fear of losing newly won employment from Canada to lower-cost locations in Mexico. However, a recent analysis of these Canadian-owned subsidiaries and their parent corporations suggests that such fears are unfounded [MacPherson and McConnell, 1990]. The study reports that most of these establishments were located directly across the Ontario-New York State border where a physical presence could be established in the U.S. and where, at the same time, the parents could remain in very close geographic proximity to their subsidiaries.

Maintaining close geographic ties with these subsidiaries is considered to be a very important strategic objective because most of the parent corporations are relatively small and new to international business. At this point in time, therefore, it is unlikely that these corporations would be attracted to locations some 1500 miles away in Mexico.

In addition, many environmentalists in the U.S. are increasingly concerned that trade liberalization will undermine their attempts to impose rigorous environmental standards upon U.S. industry. With free trade, industries obeying these new standards would be operating under a distinct disadvantage with foreign competition that does not have to meet the same standards. The Wall Street Journal quotes a Green economic theorist and World Bank economist, Herman Daly, who has advocated that the US "abandon the free trade system and impose stiff tariffs to greatly reduce the incentive to produce goods for the American market" [Postrel, 1990]. The stunning defeat of most environmental initiatives in the November, 1990, elections has probably dealt a crippling blow to environmentalists' attempts to derail the free trade negotiations. However, a strong possibility exists that the environmentalists could ally themselves with labor unions and other interest groups to put enormous pressures on the Democratic Party.

Congressional members of the Democratic Party, allied to African-Americans, environmentalists, and especially labor unions, might also oppose free trade. The 1988 Trade Law requires that President Bush's formal request for a "fast-track" free trade agreement trigger a statutory notice to the House Ways and Means and Senate's Finance Committees. The committees would then have 60 legislative days in which to determine whether such agreement would be in the interest of the United States. The Senate Finance Committee almost blocked the Canadian-US free trade agreement, so the future of a free trade accord with Mexico is far from assured in Congress. Business Week fears that Congress could inflame Mexico by holding "televised hearings on election fraud or torture south of the border. It would be likely that the anti-Yanqui fury would be enough to force Salinas away from the table" [Baker, et al., 1990, p. 41].

Other U.S. leaders fear that free trade with Mexico would undermine U.S. drug interdiction efforts. Some U.S. drug enforcement officials predict that free trade with Mexico "would grease the tracks for cocaine shipment" [Baker, et al., 1990, p. 41]. In October, 1990, three US senators vociferously opposed the delivery of military helicopters to Mexico. This equipment was to be used by the Mexican government for the war against drugs. These senators claimed that the Mexican Attorney General, Enrique Alvarez del Castillo, who would command the police using the helicopters, is corrupt, unreliable, and probably in league with the drug-runners [Krauss, 1990]. The kidnapping-death of U.S. DEA agent Enrique Camarena Salazar has left bitterness and mistrust on both sides of the border.

3. Opposition in Canada

As the United States and Mexico move closer to formal negotiations for a free trade area, many in Canada find themselves between the proverbial "rock and a hard place." They can stand by while the U.S. and Mexico form a bilateral trade accord, or they can maneuver Canada into a tripartite round of negotiations with the hope of creating a North American trade accord. Although it appears at the time of this writing that the Canadian government favors the latter stance, both positions are receiving intense criticism from within Canada.

For instance, many Canadians argue that a bilateral trade agreement between the U.S. and Mexico would benefit the former at the expense of both Mexico and Canada. Their position is that such a "hub-and-spoke" system, with the U.S. hub having separate spoke bilateral accords with Canada and Mexico, would allow the U.S. to get preference in the Mexican market in competition with Canada, and preference in the Canadian market in competition with Mexico [Wonnacott, 1990, pp. 6-7]. For some Canadian critics, therefore, the worse-case scenario for Canada is a U.S.-Mexican bilateral pact.

As a Bureau of National Affairs reporter notes, the following potential problems could arise if Canada is excluded from a U.S.-Mexico agreement:

1) "Canada's share of the U.S. market in a number of areas is protected by U.S. protectionist policies, specifically through quotas and tariffs on Mexican imports. Since Mexican exports to the U.S. bear an increasing resemblance to those from Canada, particularly in the automotive sector, Canadian exports to the U.S. could be hurt.

2) The U.S.-Canada FTA does not offer duty-free status to goods purchased in the U.S. if they are manufactured in a third country, but manufactured goods with a sufficiently low proportion of intermediate content from a third country could qualify as U.S. goods. Canada could expect more imports of U.S. finished products containing intermediate components made in Mexico.

3) Greater penetration of the U.S. market by Mexican imports could force U.S. producers to shift a portion of their output to Canadian markets, putting even greater competitive pressure on Canadian producers.

4) Lower labor costs and geographic advantages could divert investment from Canada to Mexico by both North American and overseas firms looking for a production base in North America. The U.S. could also be the preferred investment location since it would be the only country with free access to markets in all three countries" [International Trade Reporter, September 19, 1990, p. 1447].

Others in Canada are opposed to any negotiations that would unite the three North American countries into an economic alliance. Many of these same individuals were, and continue to be, opposed to the Canada-U.S. free trade agreement. Their fears of a trilateral trade accord arise from several basic perceptions about such an agreement. For example, New Democratic party trade critic Dave Barrett warns that a North American trade accord would hurt Canadian workers who would have to compete against low-cost Mexican workers. "This whole concept is a nightmare of U.S. continentalists come true: Canada's resources, Mexico's labor, and U.S. capital," he said [International Trade Reporter, September 26, 1990, p. 1468].

Maude Barlow, chairperson of the Council of Canadians, provides further criticism by noting that Canadian jobs have already been lost because of Canadian manufacturers moving their operations to the maquiladora region. Under a trilateral trade accord, she said, "there will be no reason for manufacturing to take place in Canada" [International Trade Reporter, September 19, 1990, p. 1448]. Supporting this position, the Canadian Labour Congress claims that Canada will lose more than 120,000 jobs in the textile industry alone if a North American trade area is created [International Trade Reporter, September 19, 1990, p. 1448]. The position of Canadian labor, therefore, is that job losses are the result of the free trade agreement with the U.S. and not of high production costs in Canada or of relatively poor competitive performances of many Canadian establishments.

The Canadian Liberal Party also opposes free trade with Mexico. Loyd Axworthy, a Liberal member of the House of Commons, recently stated: "How can we be talking of being sucked into a North American free trade agreement when, in fact, this government provides no adjustment, no support, for the Canadian victims of the existing free trade agreement . . . How can we do that and find ourselves putting our workers in double jeopardy not only with the Americans but now with the Mexicans?" [Madore, 1990].

FACTORS FAVORING THE CREATION OF A TRILATERAL TRADE AGREEMENT

A North American free trade agreement would create an industrial super-power with an output of some $6 trillion, a regional market of over 360 million people, a vast storehouse of natural resources, and complementary labor markets. One author claims that such a free trade accord would add 0.5 percent to the continent's economic growth table [Holstein, et al., 1990, p. 41]. Moreover, President Bush has suggested that other Latin American countries might eventually want to join the agreement, and he has called for them to follow Mexico's lead by privatizing their state-owned industries, reducing trade barriers, and liberalizing foreign investment rules. Bush made this suggestion in July 1990, and it has received a positive response from a number of Latin American countries [Wall Street Journal, September 13, 1990]. A problem, at least until recently, has been that most Latin Americans, like Mexicans, have believed that the best way to develop their economies was through protectionism. This policy was costly to industry, it decreased internal competitive conditions, and it was a source of inflation. These countries must now integrate their economies with the rest of the world if they are to attract new technology and capital [Scherer, 1990].

What are the positive reasons the three North American nations have to work toward a regional trading bloc? First, the key benefit of any regional trading bloc is in "easing the way back to a full-blown multilateral trading system, which we currently do not have" [Belous and Hartley, 1990, p. 32]. In other words, the three North American nations have the opportunity to work within the rules and spirit of GATT to develop, in a step-wise manner, a model of economic cooperation that can be followed by other trading partners. The amazing accomplishment of the Canada-U.S. FTA is that the world's two best trading partners were successful in reaching a trade accord covering a very wide range of issues. If these two countries can develop a formal, workable trade pact, hope exists for other nations as well. In addition, a trinational agreement presents both Canada and the U.S. with the challenge of adjusting their already formulated free trade policies to include a newly industrialized country. Such an accord, if reached, will provide a very useful model in the near future if a revitalized GATT emerges. Moreover, it will help the three countries defend themselves against rising protectionist blocs in Europe and Asia.

A second factor that supports the creation of a North American free trade region is the strong economic complementarity that exists among the three countries. For example, Mexico's economic recovery requires large infusions of foreign direct capital investments. If Mexico is successful in creating a favorable domestic environment for foreign investors, capital is abundantly available in Canada and the U.S., and it would likely flow quickly into Mexico. In addition, manufacturers in both Canada and the U.S. need offshore production capabilities to minimize labor costs and thereby to enhance their global competitiveness. The prime choices for locating such activity would appear to be Mexico, certain countries in East Asia, and eastern Europe. The relative advantage of Mexico over the other choices is that it not only possesses a relatively low-cost, highly literate labor force, it is also located in close geographic proximity to the U.S. and Canada, which significantly reduces the transportation costs involved in reaching the rich labor pool.

Another important complementarity of the three countries is the large market that would be open to them under an NAFTA. Such an enlarged and "free" market area is especially crucial to many Canadian and Mexican companies that are relatively small in size and not yet very competitive in the global marketplace. A trilateral free trade area would provide them with a marketing platform within which they could increase their economies of scale and strengthen their global competitive positions.

One further area in which complementarity exists among the three nations is in the abundance of natural resources. Of particular interest are the energy resources of the three countries. Without a new energy policy, the U.S. is very likely to be more than a little bit interested in securing oil from both Canada and Mexico. A trade pact that included provisions for energy sharing might well make a reluctant U.S. Congress more amenable to Mexican concerns about labor mobility across the U.S.-Mexican border. In addition, the Mexican oil industry is in serious need of fresh capital and modern technology. <u>Business Week</u> quotes an influential Mexican director of an economic consulting company as saying: "Eventually, Pemex has to go on the market" [Baker, et. al., November 12, 1990, p. 108]. Moreover, David Goldman writes: "There are hints that Mexico may even encourage some private oil exploration" [Goldman, 1990, p. 48]. In any event, the issue of trade in natural resources figures to be an important component of any trilateral talks.

A third reason favoring a trilateral accord is that it is in the interest of each of the three nations to have economic and political stability in Mexico. Economic growth and development under a free trade umbrella could provide that stability; however, for this transformation to occur, Mexico needs sustained assistance from its two northern neighbors. Mexico's present economic condition puts enormous pressures upon the country's government officials to balance ongoing macro-economic policy reforms with internal economic and political realities and constraints. The country's overwhelming reliance upon the U.S. market for its exports can be reinforced by a new trade accord. In addition, Canadian and American companies can provide financial and entrepreneurial support for the efforts of the Salinas government to integrate the maquiladora production more thoroughly with national industry in other parts of the country. Moreover, both Canada and the U.S., by entering into a formal trade agreement with Mexico, can help the latter restore the confidence of both Mexican and foreign investors, and thereby assist Mexico in attracting the capital resources that are necessary to reduce the country's debt payments and reinvigorate its national economy.

Finally, it seems important to note some of the positive reasons why Canada should support a trilateral trade agreement. A recent report by the Royal Bank of Canada suggests the following rationale: Canada's strong comparative advantages relative to Mexico would offer export opportunities for Canadian agricultural and forestry products, fish, pollution control products, transportation and communication products, and financial services; greater access to duty-free Mexican products would also provide Canadian businesses with cheaper inputs, which could improve Canada's export competitiveness; the availability of cheaper consumer goods would also increase real incomes for Canadians; and participation in trilateral negotiations would enable Canada to safeguard its interests vis-a-vis concerns that arise between Mexico and the U.S. [Royal Bank of Canada, 1990, pp. 1-12].

FACTORS LIKELY TO INFLUENCE THE PROBABILITY THAT AN NAFTA WILL EMERGE

Six interrelated factors are likely to influence significantly the probability that a trilateral trade agreement will be reached by Canada, Mexico, and the United States in the near future. Three of these factors are dependent upon conditions and events that may occur within the three-country area. These "internal" factors are: 1) the perceived outcome of President Salinas' efforts to transform Mexico's economic policies; 2) economic conditions and political considerations in Canada and the U.S. over the next few months; and 3) the specific issues that are actually negotiated in a trilateral free trade agreement.

Another set of factors relates to conditions and events outside of the North American arena. These "external" concerns are: 1) the outcome of the currently stalled talks of the Uruguay Round of the GATT; 2) the rising tide of sentiment in Europe and Asia that regional solutions are necessary to resolve global trading issues; and 3) mounting pressures elsewhere within the Western Hemisphere to pursue formal trade negotiations with the U.S. Each of these concerns is discussed briefly below.

1. "Internal" Factors

Whether or not Canada, Mexico, and the U.S. create a formal trade accord will depend in no small measure upon how successful the Salinas government is in continuing the transformation of the Mexican economy and in convincing potential investors within as well as outside of Mexico that economic policy reforms and political stability in that nation will continue. Since joining the GATT in 1986, Mexico has significantly opened its economy to global competition; it has slashed maximum tariff rates from 100 percent to 20 percent (reducing its average tariff rate to approximately 11 percent); it has maintained efforts to keep inflation down; the government has encouraged entrepreneurial investment, privatization, and deregulation; it has concluded debt-relief agreements with official and private creditors; and it has eased foreign investment rules.

While these are major accomplishments within such a relatively short time span, the important new challenge is continuing this transformation while at the same time balancing short-term gains with long-term objectives. As pointed out by Sidney Weintraub, the major long-term goals of the Salinas government are to keep inflation down, promote non-oil exports, continue to privatize and deregulate the domestic economy, stimulate foreign and domestic investment, and lower the federal debt [Weintraub, 1990, pp. 41-42]. However, as Weintraub points out, all of these objectives cannot be achieved simultaneously. They are dependent upon the continued restructuring of the Mexican economy--a policy, which in the short-run involves slow increases in real wages, a decline in government subsidies, export-led growth, and increasing trade and investment ties to the U.S. [Weintraub, 1990, p. 42-48]. In the short-run, many of these policies may become increasingly unpopular politically, especially if inflation is not curbed and if income distribution problems are not seen to be given sufficient attention by the federal government.

Achieving these long-term goals is also dependent upon convincing potential domestic as well as foreign investors that the Salinas experiment will succeed. It is estimated, for example, that some $85 billion of Mexican capital is invested outside the country [Wall Street Journal, October 1, 1990]. In fact, since 1982, Mexico has transferred more than $40 billion abroad [Weintraub, 1990, p. 42]. These financial assets must be retrieved if long-term economic recovery is to be successful.

Another "internal" consideration that will likely be important in determining whether or not an NAFTA emerges relates to current economic and political conditions in Canada and the U.S. For a variety of reasons, the present economic environment in these two countries is less than ideal to support further efforts to liberalize trade policies on the continent. For example, both countries are in an economic recession, and weekly news of plant closings and increases in unemployment does not bode well in some circles for talking about reducing trade barriers with Mexico. Moreover, the economies of both countries are under severe strain from very high federal deficits and an increasingly costly war in the Middle East. Adding to the negative economic picture is the belief by an increasingly large number of people, particularly in Canada, that the Canada-U.S. FTA is not as economically beneficial as it was supposed to be, and that an NAFTA would only compound existing poor economic conditions.

Characteristically, deteriorating economic conditions in Canada and the U.S. have given rise to increased pressure for protectionists' actions, one of which is to refrain from entering into an NAFTA. Opposition groups in both countries are mobilizing political support for their position. For example, organized labor is leading a broad coalition of agricultural, consumer, and environmental groups opposed to a free trade pact with Mexico, and even some business groups, such as the American Textile Manufacturers Institute, warn that such an agreement threatens the domestic work force [Maggs, February 6, 1991]. Even U.S. Congressional leaders who strongly supported the Canada-U.S. FTA, such as Representative John J. LaFalce (D-Tonawanda), fear that liberalized trade with Mexico will "pull down the quality of American life" [Turner, February 10, 1991, p. A-1]. In short, as the three countries continue to position themselves for possible negotiations, the atmosphere surrounding such talks will be significantly influenced by the economic and political conditions in the two northern neighbors.

A third factor that will likely determine whether or not negotiations for a North American trade accord are initiated is the selection of issues for the actual talks. In other words, the probability that an NAFTA will be created is very much dependent upon the extent to which an agreement can reached prior to the negotiations about what specific issues are to be discussed. At the present time, various groups in all three countries have very different opinions regarding the framework that should be used for the talks. On the one hand, the argument is advanced that an NAFTA should be designed to create a "free trade area," not a customs union or a common market area. As Balassa noted thirty years ago, the first stage of economic integration is the creation of a "free trade area," in which agreement is reached regarding the intra-area movement of goods and services [Balassa, 1961, p. 2] Only at the third stage when a common market area is formed are restrictions abolished on the movement of the factors of production. As Canada's International Trade Minister, John Crosbie, stated recently: "This is a trade agreement. Therefore we don't intend to dictate to Mexico what their social, cultural, or labor policies should be" [International Trade Reporter, February 6, 1991, p. 184].

At the same time, others who have representation in all three countries are demanding that any trilateral trade negotiations that take place must also deal with issues related to the welfare of Mexican workers, environmental protection and pollution-control issues, intellectual property rights and patents, standards and norms for agricultural production and subsidies, the cross-border movement of labor, narcotics issues, immigration, and energy policies [International Trade Reporter, February 6, 1991, pp. 184-185 and 201-203]. This wide ranging set of issues is in marked contrast to the goals set forth in the joint communique issued by the administrations of the three governments. The joint document stated that "the goals of the FTA negotiations are to eliminate progressively obstacles to the flow of goods, services, and investment; provide for intellectual property rights protection; and establish a fair and expeditious dispute settlement mechanism" [International Trade Reporter, February 6, 1991, p. 184].

The disagreement over the issues to be negotiated is especially critical in the U.S. because the Bush administration wants the trilateral trade accord to move through the Congress under the "fast-track" authority granted to the President in the Omnibus Trade and Competitiveness Act of 1988. Such a procedure is considered essential for moving such a bill through the Congress because members of Congress can only approve or disapprove the bill as a whole; they cannot make amendments to the bill. However, the authority to use such a procedure expires on June 1, 1991. Because it is unlikely that a free-trade agreement can be reached by that date, the President is expected to request up to a two-year extension of the fast-track procedure. The interesting political issue at this writing is whether or not Congress will approve such an extension, especially if the U.S. administration seems unwilling to broaden the range of issues, for which many members of Congress are calling. By voting to extend the fast-track procedure, Congressional opponents of an NAFTA would be denying themselves the opportunity in the future to attack individual components of any trade agreement presented to them.

In addition to disagreements over the range of issues to be negotiated, considerable dissatisfaction may arise over the length of time Mexico is given to phase in the various provisions of any trade agreement that is reached. In other words, working out a trilateral trade accord is likely to be a more difficult task than was the case for the Canada-U.S. FTA, given the huge differences in the size and levels of development of the three countries. Such a task could be further complicated if non-trade issues become part of the agenda for negotiations. It is conceivable, therefore, that the U.S. and Canada may have to accept an asymmetrical deal in which Mexican tariff reductions and other trade and non-trade-related matters are phased in more slowly than on the Canadian and American sides. Such an arrangement may or may not be politically palatable in Ottawa and Washington, depending upon the state of domestic and global economic conditions at the time.

2. "External" Factors

Prospects for creating an NAFTA are not only dependent upon economic and political conditions within the trilateral region, they are also affected by events external to the area. This interrelationship between internal and external forces is increasingly important because of the growing interconnectedness of the global economy. Thus, how enthusiastically and successfully the leaders of Canada, Mexico, and the U.S. move into negotiations for a free trade accord will depend in no small way upon conditions and events occurring outside the North American arena. Three such factors seem especially noteworthy at the present time.

One factor that is likely to be important in the pre-negotiation phase is how optimistic North American leaders are that the stalled talks of the Uruguay Round of the GATT can be moved forward quickly to a successful conclusion. Although the GATT has been enormously successful over the past forty years in reducing tariff levels, its members are currently faced with very difficult issues related to nontariff barriers. In many ways, the current Round of the GATT is the most ambitious so far. For the first time, the organization is trying to deal with trade in services, intellectual property rights, foreign investment, and, perhaps most controversial of all, the issue of agricultural subsidies. Each of these matters is highly complex and politically sensitive.

For many members of the GATT, therefore, hammering out a bilateral or regional trade agreement seems to be a quick and easy solution to international trade problems. By pursuing a more geographically limited objective, the three North American countries are still in compliance with the "escape clause" of Article XXIV of the GATT charter. This provision permits GATT members to form regional blocs if the agreement covers most of the goods and services traded among the members, and if the bloc is not formed to raise new trade barriers to nations outside of the bloc. Nevertheless, it must be noted that the basic principle of a regional trading bloc is preferences, whereas the key objective behind the multilateral GATT system is nondiscrimination. Therefore, at least in the short-term, regional trade blocs violate the multilateral, nondiscriminatory principle of GATT. If the current Uruguay Round of talks resumes quickly and moves to a successful conclusion, pressure in North America to pursue a regional trade accord may be somewhat weakened. Alternatively, if the GATT talks continue to falter, resistance to the regional approach could wane, and the three North American countries could feel compelled to move ahead with trilateral negotiations.

Another external matter that is of concern to the three North American trading partners is the momentum underway in Europe and East Asia to strengthen their economic ties to regional trading partners. Increasingly, it appears that the European Community is perceiving its long-term economic interests to be in eastern Europe and to a lesser extent in the Soviet Union. With its relatively high wage scale, the Community may very well need a high level of protectionism to defend its standards of living while it integrates eastern Europe into its regional economy. At the same time, Japan and several other East Asian countries (e.g., South Korea, Taiwan, Hong Kong, Singapore, Thailand, and Indonesia) are creating a new pattern of horizontal integration. Fostering this closer orientation is the strong export performance of these countries, the relative strength of the yen, and the threat of increased protectionism in North American and European markets [Nanto, 1990, p. 93].

The growth of such blocs creates uncertainty for businesses that depend upon global markets, disrupts corporate planning, and frequently presents government leaders with difficult trade policy and political problems. Such an unstable world environment can lead to a fragmented global trading system where groups of countries respond in kind to perceived, if not actual, protectionism elsewhere. Such posturing within the present global community comes at a very awkward time for the U.S. because many believe that the best hope the country has in the short-term of pulling out of the current economic downturn is to follow an export-led growth strategy [Bergsten, 1991, pp. 2-6]. However, for this strategy to work at the global level, the European and East Asian markets must remain economically healthy and open. If, as many believe, these regional markets are likely to become increasingly difficult to penetrate, then a North American free trade area could become a very viable alternative. Such a strategy, in fact, has been strongly recommended recently by two management professors who argue that "U.S. companies should be seeking their own Eastern Europe--not in Poland, Czechoslovakia, or Hungary, but in Mexico" [Sanderson and Hayes, 1990, p. 32].

A third source of external pressure may come from other countries in the Western Hemisphere. Most of the members of the Central American Common Market, the Andean trade pact, and the recently formed Southern Cone trade bloc have responded positively to the proposal President Bush made on June 27, 1990, for the "Enterprise for the Americas Initiative." The plan includes reducing part of the official debt owed by Latin American countries to the U.S., developing a new program to stimulate increased foreign investment, and giving stronger emphasis to environmental protection in the hemisphere. In anticipation of this Initiative, the U.S. has already signed framework agreements with Bolivia, Costa Rica, Chile, Colombia, Ecuador, Honduras, and Mexico. Similar agreements are expected with Argentina, Brazil, Uruguay, Paraguay, and Venezuela [International Trade Reporter, January 9, 1991, p. 65]. As noted by Kenneth Maxwell of the Council on Foreign Relations, a new psychology is at work in Latin America: almost all of these nations have a new mindset, which favors opening their economies to global competition, privatizing their industries, and stabilizing their economies [International Trade Reporter, January 9, 1991, p. 66].

Most of these Latin American countries seem eager to begin formal negotiations for a free trade pact with the United States. For example, news journalist Charles W. Thurston reports that once an agreement is worked out with one of these regional trade blocs, trade accords with the others will follow quickly [Thurston, 1991, p. 1-A]. Despite their enthusiasm for such an accord, the governments of these Latin American nations are watching very closely what happens to the trilateral negotiations in North America. Given the significant differences among the economic, political, and even legal systems of the three countries, it is unlikely that an NAFTA will be a carbon copy of the Canada-U.S. FTA. Any agreement must accommodate the uniqueness of Mexico and the special problems it brings to the negotiating table. As New York State Congressman John LaFalce has noted, few parallels exist between the Mexican and Canadian situation, and a trade accord with Mexico is "unprecedented" in terms of linking an advanced industrial country with a developing country [International Trade Reporter, February 6, 1991, p. 203]. In the final analysis, it is possible that pressure from the Latin American half of the hemisphere will not only influence the speed with which the three North American governments move into negotiations for a free trade agreement, it will also greatly impact the specific provisions of the final agreement.

CONCLUSIONS

Over the next few months, leaders of government, labor, industry, and various other interest groups in Canada, Mexico, and the United States are expected to be working together to establish the agenda and the procedures that will guide formal negotiations toward a trilateral free trade agreement. At the time of this writing, it appears that the proponents of a North American Free Trade Agreement are facing very formidable opposition in all three countries. Anxieties are building in many quarters, and battlelines appear to be forming throughout the three-country region. Not unlike the debates in Canada over the contents of the Canada-U.S. Free Trade Agreement, concerns are surfacing about sovereignty, the loss of jobs, increased competition for domestic industries, the welfare of workers, and even about the quality of life if a North American trade area is created. What seems different about the current round of discussions on creating a North American trade area is the strong resistance within the United States to such an accord. Many interest groups in the U.S., which are concerned about a wide range of trade and non-trade-related issues, are well organized and vociferously opposed to a trade agreement that includes Mexico.

If the current proponents of the trilateral accord are to be successful in moving a negotiated settlement over the various political and/or legislative hurdles in the three countries, objections to the accord must be addressed in a timely and convincing manner. For example, it must be shown that a trilateral agreement is absolutely necessary at this point in time to enhance the international competitive posture of North American industry and labor. Furthermore, proponents must demonstrate that a North American trade pact will be a win-win-win situation for all three countries in the long-run, and that an adequate "safety-net" will be put in place over the short-run to assist workers, communities, and industries in the adjustment process. If these arguments cannot be made quickly and convincingly, prospects for the creation of a trilateral trade region will likely be tenuous at best. As the international economist Jagdish Bhagwati has noted, profound commitments to trade policies are generally the result of "...a mix of ideological factors (in the form of ideas and examples), interests (as defined by politics and economics), and institutions (as they shape constraints and opportunities)" [Bhagwati, 1988, p. 17]. The course of events in North America over the next few months will determine, at least for this part of the international community, whether or not Bhagwati is correct in his assertion that major new interests and forces, prompted by growing globalization and interdependence in the world economy, are so compelling that "the deck is not stacked in favor of protectionism" [Bhagwati, 1988, p. xii.].

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