

A Renegotiation “Made in America”

NAFTA’s Uncertain Future

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From the beginning, the renegotiation of NAFTA was marked by President Trump’s statements underlining its negative effects on his country. More than an interest in “modernizing” it, his main motive seems to be either getting more favorable terms for his country or cancelling it altogether. His constant statements and those of his cabinet members have emphasized economic nationalism over the content of the agreement, despite the fact that this affects the interests of a large number of companies and the consumers in their own country.

In the 23 years since it came into effect, NAFTA has profoundly changed the productive structure of North America by modifying the rules of the game of two variables, trade and foreign direct investment (FDI). In the last decades of the twentieth century, and in the context of the third technological revolution combined with important changes in

multinational companies, it has spawned a profound productive integration by turning the organizational forms of international production into global value chains.¹

When the treaty was signed, the regional/global value chains were not important in the world’s economy. Today, however, 80 percent of global trade is carried out through global value chains.² That is why what is at stake in the current negotiations are not mere trade flows, but many productive processes integrated into regional value chains that have become a veritable division of labor among the three signing countries, which exchange the inputs needed to carry out production through their trade back and forth. I should underline that this globalization of the production process is by no means exclusive to the NAFTA region: this is a worldwide process in which Asia, the European Union, and North America have all developed strong links.

As Table 1 shows, the percentage of national value-added content in the total exports of all the countries in the

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TABLE 1
PERCENT OF NATIONAL VALUE-ADDED
CONTAINED IN SELECTED COUNTRIES AND REGIONS'
TOTAL EXPORTS (1995 and 2009)

	1995	2009
United States	91.6	88.7
Mexico	73.4	69.6
European Union	90.5	86.3
Czech Republic	67.9	60.6
Germany	81.3	73.3
Japan	93.1	85.2
South Korea	76.2	59.3
China	88.1	67.3

Source: Developed by the author using WTO-OECD data, <http://stats.oecd.org/index.aspx?r=8490>, accessed in July 2017.

sample show a downward trend, reflecting the integration of the productive processes.

This is a qualitatively different situation from that of 1994, when the agreement was just starting off; and that is why the decisions made for what has been called “NAFTA 2.0” can change or affect the functioning of many companies and industries. It is also why one of the most polemical points in the discussions is raising the rules-of-origin requirements and establishing, in addition, “national content rules of origin,” as the U.S. president has stated. In fact, imposing a percentage of U.S. content on trade in order to qualify for zero tariffs in the region has no precedents in any trade negotiations and is a very aggressive proposal. In addition, it is directly aimed against Canadian and Mexican interests, because it would mean that manufacturing, for example in the auto industry, would have to be carried out mainly in U.S. plants, and assembly plants that are now situated in Canada or Mexico would have to return to U.S. soil.

In addition to changing “national content,” the United States has expressed interest in considerably increasing the regional content of production, specifically, again, in the auto industry, for its products to be eligible for the zero tariff within the region. The auto industry’s rules of origin were stipulated in the agreement in order to give tariff privileges fundamen-

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tally to companies producing within the North American region as a whole; the percentage agreed upon for the sector was 62.5 percent. Undoubtedly these rules of origin encouraged European and Asian auto manufacturers to produce inside the North American region instead of merely exporting their products to the United States, Canada, and Mexico, but the United States has said it intends to considerably increase the rules of origin requirements. That would mean a hike in the percentage of automobile content produced within the region that would be required to benefit from NAFTA’s tariff advantages.

Increasing the percentage required in the rules of origin too much could be counterproductive since, instead of raising production in the region, companies from non-NAFTA countries might think it more advantageous to simply export their cars. Caroline Freund has said that toughening up these rules would only lead to lowering the regional content in final goods and interrupting value chains since, by increasing them more and more, importers would avoid the preferences stipulated in NAFTA due to the costly rules of origin. So, instead, they would trade according to the standards of “most favored nation” established by the World Trade Organization (WTO). She goes on to say that if the rules of origin requirements were increased, it would also not favor U.S. content value. If the aim is to bolster the latter, other measures should be taken. In fact, advancing toward the establishment of a worldwide norm would be an important objective for guaranteeing that companies that export to multiple destinations would not be forced to choose among agreements.³

The U.S. negotiators seem to have adopted a strategy of putting points on the negotiating table that have increasingly difficult and unacceptable implications for Mexico and Canada. In the fourth round, they proposed a “sunset clause” that would effectively end the agreement every five years unless all the parties agreed to renew it.

The very idea of putting that on the table cancels the important benefits NAFTA has offered Mexico: certainty for its FDI. When a company is thinking of investing in production, it has to calculate its expenditures and ensure that they

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will pay off for many years. The trade agreement liberalized not only trade, but also FDI. The idea of a trade instrument that would have to be reevaluated every five years throws out all the benefits that could accrue to our country and interrupts any healthy economic inertia.

President Trump has been very clear when he has said that NAFTA should come to an end to negotiate a good deal and that he likes bilateral treaties.⁴ The profoundly asymmetrical relationship among the three NAFTA signatories will strengthen the United States even more at a bilateral negotiations table, and we should remember that his treatment of Mexico is a reflection of much more than an economic negotiation: Donald Trump wants to put the brakes on the political, social, and cultural influence that Mexican society has in the United States. He is negotiating a trade deal as part of a broader project, aware that the population pyramid is a “risk” for white Anglo-Saxon predominance. His immigration policy goes hand in hand with his trade policy. Canada knows this, and that is why its foreign affairs minister and chief NAFTA negotiator, Chrystia Freeland, stated that her country “isn’t the United States’ problem.”⁵

If Trump has the idea of bilaterally negotiating a treaty with Mexico, his interests have already been sketched out in the points he has put on the table: increasing U.S. content in their trade; eliminating the U.S. trade deficit with Mexico; ensuring that its manufacturing industry not go to Mexico; refusing to consider any issue related to conflict resolution; and creating obstacles for the trade of different seasonal agricultural products imported from Mexico. In fact, in the midst of the third round of negotiations, Trump issued his statement about U.S. imports of Mexican agricultural products and also, in the case of the Boeing-Bombardier conflict, decided to levy a 220-percent tariff on the Canadian company.

The conflict between Boeing and Bombardier originated when the former brought suit against the latter for illegal trade practices, arguing that the Canadian firm sells its C Series jets at very low prices in the United States. In response, the U.S. imposed an extremely high tariff on Bombardier imports;

the Canadian government, in turn, threatened to cancel the purchase of 18 Boeing aircraft. Northern Ireland manufactures the wings and other parts for the Bombardier jets, and this global value chain production also led British Prime Minister Theresa May to enter the fray, stating that she was “bitterly disappointed” with the United States for imposing those tariffs on Bombardier.⁶

Unfortunately, the future of Mexico’s auto industry will be affected. Whether trade is carried out through the WTO, a bilateral agreement is signed with the United States, something of NAFTA is preserved, or no agreement is signed at all with the U.S., European, U.S., and Asian investors will have to reevaluate their strategies, since they brought their resources into Mexico to a great extent with the huge U.S. market in mind. NAFTA included mobility of investment, and that could be lost, but what is very likely, in any case, is that Trump will continue to take measures to spur manufacturing to return to the United States.

Another very vulnerable sector in Mexico is agriculture, particularly in two areas: the big agricultural exporters, who came out the winners with NAFTA, and the grain producers, whose sector was finally dismantled by the agreement as a corollary of terrible long-standing Mexican government public policies. I should underline another very serious factor consolidated by NAFTA: Mexico has become a net importer of corn, the basis for the national diet. That is, we are dependent on imports for the number-one foodstuff in our diet due to the policies of dismantling agricultural production destined for the domestic market.

What other countries have protected and considered strategic, and, therefore, that should be protected using criteria that go beyond costs and competitiveness, in Mexico is disregarded. For example, this is why Mexico has become a net importer of U.S. corn. This is the context in which during the renegotiations, the United States has declared its intention of limiting the importation of fruit and vegetables to certain seasons as a result of strawberry and blueberry producers’ pressure.⁷ These sorts of measures would be the beginning of the fragmentation of the North American agricultural market, which has operated in many parts of the agricultural and animal husbandry sectors through regional value chains.⁸ Undoubtedly, this attitude on the part of the United States would be an incentive for Canada and Mexico to also levy tariffs on other products.

If NAFTA does not continue to exist, trade would be regulated by WTO rules. This would mean that the United States

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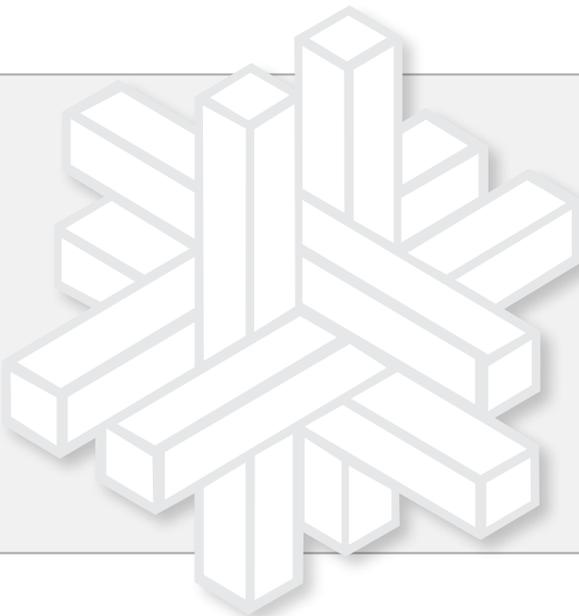
would impose an average tariff of 2.5 percent, and regional trade would come under the “most-favored-nation” clause as stipulated by the WTO. While this tariff is not very high, it does imply considerable cost since Mexico would lose institutional backing and the certainty that NAFTA has given to productive investments. Trump would probably also continue to take different protectionist measures that could affect integrated value chains among the three countries, forcing companies to reconsider location advantages for different phases of their productive processes.

We must not lose sight of the fact that a large part of the business world wants NAFTA to continue. Recently, the head of the U.S. Chamber of Commerce, Thomas Donohue, said that the sectors he represents would do “the impossible” to save NAFTA despite the “several poison pill proposals still on the table that could doom the entire deal.”⁹ Important counterposed economic interests in the three countries are involved in the NAFTA negotiations, but whatever the result, we must not forget that Mexico’s participation in the world economy must be mediated and regulated by a long-term program of economic development that will not only grow the

economy, but will also consider the benefits to its population a priority, including the improvement in the quality of life for Mexican society. **NMM**

NOTES

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- ³ Caroline Freund, “Streamlining Rules of Origin in NAFTA,” Peterson Institute for International Economics, June 2017, <https://piee.com/system/files/documents/pb17-25.pdf>.
- ⁴ Alicia Salgado, “Tensión máxima sobre la Liga NAFTA,” *Dinero en imagen*, October 11, 2017, <http://www.dineroenimagen.com/2017-10-11/91808>.
- ⁵ Alicia Salgado, “Canadá culpará a México de los fallos del TLCAN con Trump,” *Dinero en imagen*, October 10, 2017, http://www.dineroenimagen.com/2017-10-10/91782?utm_source=dineroenimagen_desktop&utm_campaign=relacionados&utm_medium=article.
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- ⁷ Verónica García de León, “EU y Canadá arremeten contra México en la Tercera Ronda de Negociaciones del TLCAN,” *Expansión*, September 27, 2017, <http://expansion.mx/economia/2017/09/27/eu-y-canada-arremeten-contra-mexico-en-la-tercera-ronda-del-tlcan>.
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- ⁹ Valente Villamil, “EU pone más propuestas inaceptables,” *El financiero*, October 13, 2017, http://www.elfinanciero.com.mx/economia/eu-pone-mas-propuestas-inaceptables.html?utm_source=El+Financiero&utm_campaign=8a3a2cbff8-EMAIL_CAMPAIGN_2017_10_13&utm_medium=email&utm_term=0_e6327f446b-8a3a2cbff8-109253673.



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