

"Did NAFTA Help Mexico? An Assessment After 20 Years," February 2014

Did NAFTA Help Mexico? An Assessment After 20 Years
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Executive Summary

It is now 20 years since NAFTA went into effect, bringing Mexico into a new commercial agreement with the United States and Canada. At the time it was argued, and forecast, that the agreement would boost Mexico's growth and development.

This paper compares the performance of the Mexican economy with that of the rest of the region over the past 20 years, based on the available economic and social indicators, and with its own past economic performance. Among the results:

- Mexico ranks 18th of 20 Latin American countries in growth of real GDP per person, the most basic economic measure of living standards.
- From 1960-1980, Mexican real GDP per person almost doubled, growing by 98.7 percent. By comparison, in the past 20 years it has grown by just 18.6 percent.
- Mexico's per capita GDP growth of just 18.6 percent over the past 20 years is about half of the rate of growth achieved by the rest of Latin America. If NAFTA had been successful in restoring Mexico's pre-1980 growth rate – when developmentalist economic policies were the norm – Mexico today would be a relatively high income country, with income per person significantly higher than that of Portugal or Greece. It is unlikely that immigration reform would be a major political issue in the United States, since relatively few Mexicans would seek to cross the border.
- According to Mexican national statistics, Mexico's poverty rate of 52.3 percent in 2012 is almost identical to the poverty rate of 1994. As a result, there were 14.3 million more Mexicans living below the poverty line as of 2012 (the latest data available) than in 1994.
- We can use the poverty statistics of the UN Economic Commission on Latin America (ECLAC) to compare Mexico's poverty rate with the rest of Latin America. These statistics are computed differently and show a decline in poverty in Mexico. However, according to these measures, the rest of Latin America saw a drop in poverty that was more than two and a half times as much as that of Mexico: 20 percentage points (from 46 to 26 percent)

for the rest of Latin America, versus 8 percentage points (from 45.1 to 37.1 percent) for Mexico.

- Real (inflation-adjusted) wages for Mexico were almost the same in 2012 as in 1994, up just 2.3 percent over 18 years, and barely above their level of 1980.
- Unemployment in Mexico is 5.0 percent today, as compared to an average of 3.1 percent for 1990-1994 and a low of 2.2 percent in 2000; these numbers seriously understate the true lack of jobs, but they show a significant deterioration in the labor market during the NAFTA years.
- NAFTA also had a severe impact on agricultural employment, as U.S. subsidized corn and other products wiped out family farmers in Mexico. From 1991-2007, there were 4.9 million Did NAFTA Help Mexico?: An Assessment After 20 Years 2 Mexican family farmers displaced; while seasonal labor in agro-export industries increased by about 3 million. This meant a net loss of 1.9 million jobs.
- The very poor performance of the Mexican economy contributed to a surge in emigration to the United States. From 1994-2000, the annual number of Mexicans emigrating to the United States soared by 79 percent. The number of Mexican-born residents living in the United States more than doubled from 4.5 million in 1990 to 9.4 million in 2000, and peaked at 12.6 million in 2009.

NAFTA was just one variable among others that could account for Mexico's poor economic performance over the past 20 years. However, it appears to be related to other economic policy choices that have negatively affected the Mexican economy during this period. The IMF notes that "Mexico competes directly with China in the U.S. market, where China accounts for 23 percent of U.S. imports and Mexico accounts for 12 percent." This is a very tough competition for Mexico for a number of reasons. First, Mexico was and remains a higher-wage country than China. Second, China has maintained a commitment to a competitive exchange rate, in effect fixing this exchange rate against the dollar or (since 2005) a basket of currencies. The Mexican central bank by contrast has, as the IMF notes, "a firm commitment to exchange rate flexibility." In other words, the Mexican Central Bank will raise or lower interest rates as necessary to reach its target inflation rate (3 percent), and let the exchange rate go where it may. This means that Mexico's exchange rate is unlikely to be competitive with China's, which further worsens its cost disadvantage. The Mexican Central Bank's form of rigid inflation targeting also adds a large element of unpredictability to the exchange rate, which has a negative impact on foreign direct investment; foreign investors will find it difficult to know how much their assets or output will be worth internationally in the future.

China has other advantages that make it a formidable competitor for Mexico in the U.S. market: the Chinese government owns most of the banking system in China, and can therefore ensure that its most important exporting firms have sufficient access to credit. In Mexico, by contrast, 70 percent of the banking system is not only private but foreign-owned. The Chinese

government also has an active industrial policy that enables it to help its exporting firms in various ways, and spends vastly more on research and development – both in absolute terms and as a percentage of its economy.

NAFTA also increasingly tied Mexico to the U.S. economy, at a time when the U.S. economy was becoming dependent on growth driven by asset bubbles. As a result, Mexico suffered a recession when the stock market bubble burst in 2000-2002, and was one the hardest hit countries in the region during the U.S. Great Recession, with a drop of 6.7 percent of GDP. The Mexican economy was even harder hit by the peso crisis in 1994-95, losing 9.5 percent of GDP during the downturn; the crisis was caused by the U.S. Federal Reserve raising interest rates in 1994.

Conclusion

As was well known at the time of NAFTA's passage, the main purpose of NAFTA was to lock in a set of economic policies, some of which were already well under way in the decade prior, including the liberalization of manufacturing, foreign investment and ownership, and other changes.²⁶ The idea was that the continuation and expansion of these policies would allow Mexico to achieve efficiencies and economic progress that was not possible under the developmentalist, protectionist economic model that had prevailed in the decades before 1980. While some of the policy changes were undoubtedly necessary and/or positive, the end result has been decades of economic failure by almost any economic or social indicator. This is true whether we compare Mexico to its developmentalist past, or even if the comparison is to the rest of Latin America since NAFTA. After 20 years, these results should provoke more public discussion as to what went wrong.