

Seven Myths About NAFTA *and Three Lessons for Latin America*

Myth 1

NAFTA has been a positive contribution to Mexico's strategy of export-led growth.

Facts: GDP growth rate in Mexico has remained stagnant since 1983. NAFTA did not change that. Since NAFTA was approved average per capita GDP growth has been 1% (similar to performance during the slump of the 1930s and in strong contrast with 3.4% of the period 1945-1980). Export-led growth turned out to be a mirage. The export sector expanded but remained uncoupled from the domestic sector and unable to provide dynamic impulses to the rest of the economy creating productive linkages.

Myth 2

NAFTA generated a significant expansion of exports and a sizable surplus in Mexico's trade with the United States.

Facts: Mexico has a permanent trade deficit. The myth of Mexico as an export giant evaporates when we consider that, next to the surplus with the US, there is a booming trade deficit with Asia and Europe (which increased by 600% and 400% respectively since 1994). Mexico's exports to the US represent 90% of total exports; NAFTA engendered a colossal distortion of trade flows that contributed powerfully to dismantle the productive capacity of the country. On the other hand, fifty percent of the surplus with the USA is explained by maquiladora exports, while the remaining fifty percent is due to oil and automotive exports in equal shares. Thus, exports of cheap labor and natural resources are at the center of the trade surplus with the US. Exports are concentrated in a very small number of branches and are dominated by a tiny group of transnational corporations.

Myth 3

NAFTA generates big foreign investment flows into Mexico, opening development opportunities.

Facts: Foreign investment has been flowing into Mexico but an important part of that is short term portfolio investment which does not translate into productive projects. In addition, about 20% of foreign direct investment has

taken the form of mergers and acquisitions which do not represent new greenfield investments and, in many cases, have led to job losses as downsizing is introduced. FDI is concentrated in a very small number of branches and firms. In fact, in 2002, only one project (the purchase of Banamex by Citigroup) was responsible for 45% of total FDI. FDI has not enhanced competitiveness of the industrial sector and has not led to significant transfer of technology. On the other hand, NAFTA's chapter 11 on foreign investment effectively forbids Mexico to use of key industrial policy instruments (such as performance requirements). Financial deregulation accompanying NAFTA opened new and more attractive opportunities to financial investment and speculation. This helps explain why total productive investment dropped from 22% to 18% between 1994 and 2003 (down from 30% during the seventies).

Myth 4

NAFTA helped Mexico recover more rapidly from the 1994 crisis.

Facts: Mexico's economy has not recovered fully from the crisis triggered by the peso devaluation in December 1994. The harsh adjustment program that followed brought about the worse recession in sixty years, an economy-wide payments crisis and the fraudulent bailout of the banking system. The liabilities of that handout represent today 15% of GDP and threaten to lead to a fiscal crisis. In addition, the international financial rescue package operated by the US Treasury in 1995 was aimed at salvaging foreign investors and would have been implemented with or without NAFTA. In case of balance of payments crises, NAFTA's chapter XXI (specifically article 2104) forbids the use of emergency measures that are accepted under WTO's rules. Had these emergency measures been applied, the outcome for Mexico's economy in 1994 would have been dramatically different.

Myth 5

NAFTA has contributed to macroeconomic stability in Mexico

Facts: The illusion of macroeconomic stability centers on reduced inflation, which is simply a result of an overvalued exchange rate and the repression of aggregate demand. The latter is achieved through the containment of wages and a contractionist monetary policy. As a result of this restrictive monetary posture, fresh credit to the non-banking sector is now 60% less than its level in 1994. From the standpoint of public finance, the real fiscal deficit is currently six times larger than the level authorized by Mexico's congress. This situation is unsustainable and will lead, sooner or later, to a fiscal crisis.

Myth 6

NAFTA has created employment opportunities, increased wages and improved welfare for Mexicans

Facts: Between 1994 and 2003 new entrants to the labor force totaled 9.3 million persons; but during that period only three million jobs were created in the formal sector. Thus, 60% of the demand for new jobs remains unsatisfied, forcing people to explore other survival strategies in the so-called informal sector. Between 1994-2003 minimum wages and contractual wages lost 20% and 19% of their purchasing power respectively. Wages and benefits in the manufacturing sector during that period dropped 9%. Despite a marginal increase during the period, wages in the maquiladora industry remain 40% below manufacturing wages. Finally, workers in US affiliates operating in Mexico earn 75% less than their counterparts in US affiliates in Canada. The ratio of Mexican to US manufacturing wages (in US dollars) remains unchanged at 2:10.

Myth 7

NAFTA has contributed to reduce poverty and improve the environment

Facts: Income distribution has worsened during the Nafta years. The number of households living in poverty has grown 80% since 1984 and NAFTA did not redress this trend. Today, 70% of Mexico's population lives below the poverty line. The World Bank estimates 25 million Mexicans live in extreme poverty, other more rigorous estimates put this figure at 40 million. Rural poverty is rampant and migration has increased. The toll in terms of health and malnutrition is dramatic, with 60% of indigenous children suffering severe malnutrition. Consumer welfare has not improved as the price index of basic products (the so-called canasta básica) increased by 257% between 1994-2002. The cost of environmental degradation is calculated at 10% of GDP per year, dwarfing economic growth. Between 1990 and 1999 the land area covered by forest fell from 32% to 28%, while carbon dioxide emissions per capita grew from 3.7 to 3.9 metric tons. Chapter 11 provisions serve to downgrade local environmental concerns as witnessed by the Metalclad case decided by a NAFTA arbitration panel in 2000.

Three Lessons for Latin America

Lesson 1

There are other avenues for economic integration in which development of the domestic market is the priority and the role of the State as an actor promoting sustainable development is not forsaken. This alternative path implies recovering the use of macroeconomic and sector level policy instruments to induce growth and harness it for development. It also implies the respect for local priorities, the recognition of asymmetries between countries and a socially responsible approach to economic and environmental sustainability.

Lesson 2

As Nafta, FTAA is designed to consolidate neoliberalism. As such, FTAA will be another corporate-led process in which trade liberalization is tailored to the needs of giant firms. FTAA will not usher in a healthy export-led growth strategy, but will be based on low wages, bad jobs and no productive linkages. Low wages and restrictive macroeconomic policies will intensify social inequality and project poverty to extreme levels. A high percentage of Latin American exports already comes from low-productivity and natural-resource intensive sectors. FTAA will lead to severe depletion of the regions' natural resources.

Lesson 3

FTAA will accelerate the loss of sovereign control over policy instruments critical for any development strategy, both at the macro and sector levels. This will take place at the precise moment in which Latin American economies will need to adjust to the shock of full trade liberalization. NAFTA's investment rules are particularly dangerous as they forbid access to key industrial policy instruments. By granting national treatment to US firms and accepting the flood of imports, FTAA will further contribute to dismantle already weakened local productive structures. For these and other reasons, it is clear that FTAA will be a formidable obstacle to the social and economic development of Latin America.