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THE MEXICO - U.S. - CANADA FREE TRADE NEGOTIATIONS

ITS IMPLICATIONS FOR CANADA

An extremely well researched and written paper. I really enjoyed reading it, and learned a lot from it. I would encourage you to condense it into a publishable article. A very impressive bibliography also shows the amount of work that you have done. You should feel very good about this paper.

Marketing 6400W

Prof. Charles Mayer

Submitted by:

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THE HISTORY OF MEXICO

The proposed free trade agreement with the United States and Canada represents a drastic change from Mexico's historical traditions and cultural aspirations. Understanding the desire of the Mexican government for a continental free trade agreement is impossible without an understanding of the history of that country. Thus, this report begins with an outline of the history of Mexico.

In 1521, Ferdinand Cortez conquered the Aztec empire and claimed Mexico for Spain. This began three centuries of colonial rule in which the Spanish masters exploited the colony and its Indian population. The colonial period has been described as "a period of comparative peace - the peace of suppression, stagnation, and decay".[1]

A revolution against Spain began in 1810 and culminated in full independence in 1821. Unfortunately, little of the social and economic structure of the new country changed and Mexico fell under the rule of dictators. A second revolution occurred in 1857 and resulted in a new constitution that attempted to restrict the powers of the Roman Catholic church and the small but powerful elite. Various leaders, including Benito Juarez, a full-blooded Zapotec Indian, attempted agrarian reform. However, little actually changed in Mexico as its leaders were preoccupied with fighting the entrenched conservative elite and France's puppet, the Emperor Maximilian.

The violent political instability that characterized Mexico from its independence ended in 1876 when Porfirio Diaz established a dictatorship. Under Diaz, Mexico enjoyed balanced budgets, prosperity, and a national income that increased fivefold. Foreign

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[1]Lewis Hanke. Mexico and the Caribbean (Princeton, N.J.: D. Van Nostrand Company Inc., 1967), 97.

capital was protected and Mexico became a preserve for foreign investment. Unfortunately, few Mexicans shared in the new prosperity. Diaz ruled in the classical tradition of a dictator, using the police and army to maintain power. The church generally preached submission to authority, and thus lost the support of many Mexicans.

Economically, Mexico was primarily an agricultural society in which one percent of the population owned most of the land. The "hacienda" was the principle form of organization. It included homes for the workers, a chapel, a jail, a cemetery, and sometimes a school. Workers were forced to purchase goods from "hacienda" stores where high prices forced many workers into debt slavery. The peons were completely dependent upon the elite landowners who usually lived in Mexico City or a provincial capital. Mexico became a country of immense disparity between rich and poor; a problem that still persists.

The excesses of Diaz led to yet another revolution which began in 1910; a century after the revolt that led to the expulsion Spain. This began a ten year struggle that was characterized by assassinations, murders, riots, and clashes of armies. During this period, the population decreased by one million; the first time in history that Mexico experienced a decrease. A new constitution in 1917 renewed and strengthened the principles of the 1857 constitution. It established a planned agrarian and industrial system, promised land reform, and secular education was replaced by public education. Labour would be allowed to organize, bargain collectively, and strike. Most important, all subsoil minerals and petroleum were declared to belong to the nation and could be exploited only by Mexican nationals or foreigners who agreed to consider themselves as nationals.

The Constitution of 1917 in effect declared war on all the most powerful groups of the past: the clergy, the "hacendados", and the employers. It gave warnings to foreign states that had exploited Mexico. Understandably, Americans with interests in Mexico, including churchmen, landowners and oil companies, opposed the "godless and socialistic Mexico". However, President Wilson recognized the new government of Carranza, and thus put an end to any threat of U.S. intervention. Carranza was eventually executed in 1920 when he tried to escape the country after filling a 20 car train with sacks of bullion and other loot.

Comparative peace returned in 1920 when General Alvaro Obregon came to power. He encouraged trade union organization and modest land reforms. The army was brought under strick civilian control. Attempts at improving the lot of the peasants included the building of large irrigation projects and rural schools. However, the social revolution continued with widespread corruption and bitter disputes concerning direction and pace. This included a struggle with the Church in which the clergy went on a three year strike beginning on July 31st, 1926. Obregon was assassinated in 1928, ending a period described as " 'debased and clouded years in which the revolutionary figures failed'." [2]

The net effect of the Revolution of 1910 was to change the social structure of Mexico. The once powerful and wealthy landowner class virtually disappeared.

> "...new social classes with a decisive political power emerged in the brand new collective owner of the land, the industrial worker, a popular army, and a new upper middle class so new, so tender, so fragile that not one of the thousand millionaires ...in Mexico has had his wealth over 20 or 30 years...not one of the great newspapers survived. Only two of about 50 banks continued under the new regime."

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[2]ibid, 104.

In 1928, Plutarco Elias Calles assumed the presidency. In an attempt to bring an end to the political strife of Mexico, he formed the "Partido Nacional Revolucionario" which later changed its name to "Partido Revolucionaria Institucional" (RRI). It has remained the cornerstone of the Mexican political system. PRI has bound the various political bosses, interest groups, labour unions, and peasants. A small group within the party prearranges elections and writes legislation. No president can hold office for more that one six year term. Through PRI, Mexico has developed the paradox of a one party state that allows free speech, free press and free assembly.

The socialistic reforms continued throughout the 1930s. Railroads were nationalized and land reforms continued. In 1938, Mexico took the largest step of the reform movement by nationalizing the 17 foreign owned oil companies under a government corporation called Pemex. This move was viewed by Mexicans as a regaining of their sovereignty. Oil is still symbolic with Mexican nationalism.

In 1940, a new president came to power and Mexico began a political shift to the right. This marked the end of the real revolution. In 1910, over 95% of the rural population did not own any land. By 1940, they owned over half the available cropland. However, agricultural production had not increased. With the population having increased by five million, it was felt that the land and labour reforms hand not brought any substantial improvement to the standard of living of the masses. Thus, there was a sense that it was useless to expropriate the rich any further if the result was the continuance of mass poverty. The emphasis was now on industrial growth which was to be achieved more through capitalist measures than socialism.

Mexico's "guided" democracy is not one that Americans and Canadians easily understand. It has rigged elections but allows freedom of

speech. Alfredo Phillips, Mexico's ambassador to Canada, explained in Toronto: "Our democracy is not like Canada's; but it is a democracy."[3] PRI is characterized by bossism, opportunism, favouritism, and corruption. Presidents are preselected by the outgoing president and plebiscites merely ratify a "fait accompli". Elections only serve to expose the president-to-be to the people and to give him an opportunity to explain his program and cultivate a popular image. However, PRI's role has been to "contain dispute, to minimize the friction of change";[4] and it has preformed this roll well.

Since 1929, PRI has held the presidency, all state governorships, all federal senatorial seats, and has controlled the federal Chamber of Deputies. Minor parties are now allowed token representation in the Chamber of Deputies where 100 of 400 seats are reserved for opposition parties. Not until the last election was an opposition member allowed to assume the governorship of a state. However, the main function of opposition parties is to act as a safety valve for frustration with official policy. PAN, a right wing party, is the preferred opposition. In 1985, it was allotted 32 of the 100 seats reserved for opposition parties. However, the left wing Democratic Revolutionaries is rapidly gaining popularity.

Whatever its faults, until recently, PRI has brought political stability to Mexico by balancing various forces within society. Mexican presidents must respond to the pressures of businessmen, labour, agriculture, the intellectuals, the politicians, and the Catholic Church. PRI has enabled Mexico to break out of the vicious circle of dictatorship, misery, and revolution. "It was founded on the sound principle that if the contending factions in

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[3]Alfredo Phillips, 24 September 1990.

[4]Hanke, 231.

the 1910 revolution were to achieve the ideas for which they had fought, they would have to bury their differences and work together. By providing the government with an ideological base of support and an apparatus through which political rewards could be distributed, the PRI has managed in the years since its foundation to stabilize a nation once racked by political chaos."[5]

Mexicans view their history as an epic struggle of the people. Through it they have developed a fierce nationalism and a fear of foreign "imperialism". It is this fear that President Salinas must contend with in the present free trade negotiations.

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[5]Mexico, (Alexandria: Time Life Books, 1986), 139.

ECONOMIC BACKGROUND

By 1940, it was essential that Mexico shift from an agricultural economy to a more industrialized one. The "ejido" (collective farms) agrarian reforms had successfully transferred ownership of over half Mexico's cropland to the peasants. Unfortunately, there had been no increased agricultural production since the revolution of 1910. More important, Mexico's population had increased by five million. Mexico had two-thirds of its workforce in agriculture but was a net food importer. The "ejido" had neither the capital nor the technology to improve agricultural production.

The Mexican government instituted a protectionist trade and development policy known as "import substitution industrialization" (ISI). Mexico had no entrepreneurial class, raw materials represented the bulk of exports, and the population was growing dramatically. The government believed that high tariffs and import restrictions were essential to industrial development. High tariffs and import restrictions isolated the Mexican economy.[6] Foreign investment was encouraged, but limited to 49% ownership of a corporate stock.

The ISI did help to create a hugh industrial base. The Mexican economy developed more rapidly and uniformly than any other in Latin America. It was given a kick start from the shortages in the U.S. caused by World War II. The government was active in the economy as an investor, provider of substantial credit, and an entrepreneur. However, government owned firms accounted for only 10% of total industrial production. From 1950 to 1969, the GDP grew at a faster rate than the population. Per capita income in the 1950s increased fivefold. Growth rates in the early 1970s exceeded the average for all Latin America, the U.S., and Western

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[6]Claudio X. Gonzalez, 24 September 1990.

Europe.[7]

By the early 1970s about 80% of Mexico's manufactured goods were domestically produced. Growth in the industrial and service sectors resulted in a shift of the labour force away from agriculture. In 1950, 62.4% of the labour force was in agriculture. By 1980, this figure had declined to 37.4% and is expected to drop further to 17.8% by the year 2,000.[8] This shift in the labour force has transformed Mexico from an agricultural to an urban society. Mexico City had become the most populated city in the world.

Mexico exported agricultural products, minerals, oil, shrimps, and manufactured goods. By the 1960s, its agricultural production was sufficient to meet domestic requirements. Government spending on large scale irrigation projects, and the use of fertilizers explained the increased production. Mexico imported intermediate and capital goods; but, few consumer goods. Any deficits in the trade balance were more than offset by revenues from Mexico's favourable tourist trade and by importing capital.

Mexico's rapid industrial development was due to political stability, diversified natural resources, agricultural raw materials, a sophisticated financial system, a professional civil service, and geographic proximity to the U.S. The ISI enabled Mexico to construct the apparatus of a modern state: civil service, public banking institution, public work, tax system, import controls, subsidies, and price controls.

The oil shocks of the early 1970s further fed Mexican economic and social policy. The Mexican government borrowed heavily on foreign

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[7] Mexico, Time Life Books Inc., 273.

[8] ibid, 15.

markets to finance their industrial policy and social services. The foreign debt increased from $4 billion in 1971 to $51 billion in 1982. The debt was to be financed through ever increasing oil revenues. Foreign investors believed Mexico was a safe country for their money. It had not defaulted on a debt since 1917.

As late as 1973, Mexico was an importer of oil. However, the dramatic increases in the price of oil led to new exploration and increases in technological investments. The result was a boom for the Mexican oil industry. Between 1973 and 1982, production soared by 600%. By the mid 1980s Mexico's proven reserves of oil and natural gas were second only to Saudi Arabia at 72 billion barrels.[9]

Despite the success of the ISI in developing an entrepreneurial class and in major macroeconomic improvements; maintaining a closed economy had serious long-term repercussions. "Sheltered from competition and coddled with government favours, domestic producers got away with being inefficient, charging high prices and shipping shoddy products. The results were not good. Protectionist Mexico couldn't compete in world markets and, when its oil riches went bust, the country plunged into six years of stagnation and inflation still referred to, in a shorthand of sorts, as 'la crisis'."[10]

These problems were compounded by corruption, unrest, and a small business underground in which an estimated 25% of GDP was lost to the black market. Industries were producing high-priced goods rather than appealing to mass markets. The majority of industries were small, family owned operations in which a lack of technical

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[9]ibid, 12.

[10]Richard Alm, "Here Comes Mexico", Toronto Star, 17 June 1990.

knowledge and financial resources resulted in extremely low productivity.

The oil price collapse of 1981 caused the ISI to implode along with the Mexican economy. During the credit boom, many businesses overexpanded and created a hugh overcapacity. Declining oil prices combined with soaring interest rates resulted in Mexico being unable to meet its debt obligations. Inflation began to run rampant and the peso came under serious pressure. In a seven month period in 1982, it was devalued from 26 to 130 pesos per U.S. dollar.

On September 1, 1982, President Portillo, with less than three months remaining in his mandate, announced that the 54 private banks would be nationalized. This was done without consulting president-elect de la Madrid. Portillo needed a scapegoat and accused "a group of Mexicans, supported by the private banks"[11] of looting the country. The government could now regulate interest rates, business loans, and the flight of capital.

When Miguel de la Madrid took power he began a policy of economic reforms designed to open up the Mexican economy and satisfy the World Bank's demands for an austerity program. He disbanded the ISI, lifted foreign exchange controls, slashed government spending, and opened the borders to foreign capital. He imposed austerity measures aimed at limiting foreign borrowing, reducing government debt, and restricting imports. Mexico was no longer to have a closed economy. In 1986, Mexico joined the GATT. "Mexico came to realize that it could no longer depend upon oil and minerals for export earnings."[12]

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[11] Mexico, Time Life Books Inc., 137.

[12] Gonzalez, 24 September 1990.

By the end of his term in office, de la Madrid's austerity measures had cost his administration the credibility of the general population. However, his policies of opening the economy set the stage for his successor, Carlos Salinas de Gortari.

MEXICO'S ECONOMIC AND SOCIAL PROBLEMS

Mexico suffers from a host of problems that seem to deft solutions. There is a hugh national debt, high unemployment, overpopulation that is increasing at an alarming rate, and corruption at every level of society. Forty percent of the working population is underemployed.

Mexico must cope with a massive national debt that presently stands at $117 billion.[13] In 1988, the national debt absorbed 60% of federal spending. A large influx of capital in the last two years has contributed to an 80% reduction in interest rates. This has considerably eased the country's debt servicing burden.

The demographics of population growth intensify the problem of overpopulation. In 1985, 40% of the population was under the age of 14. Today, 65% of the population is under the age of 25.[14] Mexico is in desperate need of economic growth to provide jobs for its growing labour market. If new entrants to the labour market find employment, economic growth could be among the fastest of any nation in the world. If instead Mexico fails to provide jobs for its people, the standard of living could drop even further than the 50% it has declined since the early 1980s.[15] The search for employment has resulted in a mass illegal migration to the United States. The U.S. Bureau of Census estimates that 3.5 million to 6 million Mexicans are presently in the U.S. without proper papers.[16]

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[13]Ross Laver, "Mexico Fights Back", Maclean's, 21 March 1990, 40.

[14]Gonzalez, 24 September 1990.

[15]Laver, 40.

[16]Mexico, Time Life Books Inc., 31.

Mexico exhibits the paradox of having a large industrial base with the majority of its population living in poverty. Despite impressive increases in productivity in the past 50 years, little benefit has accrued to labour or peasant groups. Instead, "...benefits of economic growth had gone mainly to a relatively small bourgeois group, and had so far brought little, if any improvement in the lives of the poor".[17] In 1950, the poorest fifth of the population received only 4.7% of national income while the top fifth received 58.9%. By 1980, these figures were 3.3 % and 55.1% respectively.[18] "While it nurtures a manufacturing boom, Mexico's challenge is also to bring (its) sprawling underclass into the mainstream."[19] Salinas has attempted to defuse this potentially explosive problem by increasing government spending on public works to $1.6 billion.[20]

Mexico has created a free trade zone, known as the "maguiladora", along the U.S.border. Firms are allowed to import duty free for production of exports. A cluster of 1,500 factories, employing half a million workers, manufacture and assemble components for U.S. industry. In recent years, a few Japanese and European firms have also set up factories in this area.

Both large MNCs and smaller U.S. firms are attracted to the "maguiladora" by cheap labour. Workers are paid as little as $1.00 per hour. They live in abysmal conditions with foul water, ruined roads, a poor telephone system, no sewers, and a despoiled environment. Some point to this area, where a quarter of the

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[17]Thomas E. Wed, Mexico: A Country Study, (Washington: U.S. Government Printing Office, 1983), 435.

[18]Mexico, Time Life Books Inc., 153.

[19]Stephen Baker, Elizabeth Weiner, and Amy Borrus, "Mexico: A New Economic Era", Business Week, 12 November 1990, 104.

[20]Laver, 40.

population lives in poverty, as an example of how growth in the Mexican economy is not fostering better working conditions for the Mexican worker. They fear that a free trade agreement might turn Mexico into one big "maguiladora".

In addition to the disparity between rich and poor, Mexico suffers from regional disparity. The highest per capita income is in the Federal District of Mexico City, Baja California, and urban areas along the U.S. border. The rural areas meanwhile, suffer from extreme poverty. It is in these rural areas that the opposition to the government is most deeply rooted.

REFORMS UNDER SALINAS

Carlos Salinas de Gortari was elected president of Mexico in 1988. The election results were controversial with many believing that he actually lost. However, since the PRI controls the electorial machinery, Salinas was able to claim slightly over 50% of the popular vote.

Like his predecessor, Salinas is a Harvard graduate. He believes that Mexico's economic and social problems can only be solved through a comprehensive restructuring of the national economy. He views an open and free economy as the only means of lifting Mexico out of poverty and providing for an increasing population. To achieve his goals, he has completely reversed 50 years of government policy.

The economic overhaul of Mexico's economy has been referred to as "Salinastroika". It is based on the belief that there are three critical success factors to Mexico's restructuring: first, the ability to penetrate foreign markets; second, access to technology; third, the ability to link manufacturing to foreign economies.[21] Restructuring of the economy is dependent upon abandoning the closed economy and replacing it with an open, market-oriented economy. The private sector is to be the engine that drives the new economy. "Salinas is only setting the stage; businessmen are the actors."[22]

Salinas began a program of privatization. To date, over 800 of 1,200 government enterprises have been privatized. These include the banks, both major airlines, and the telephone system. He has cropped the public sector and unleashed market forces to promote

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[21]Luis Carcoba, 24 September 1990.

[22]Alfredo Phillips, 24 September 1990.

efficiency and new technology in the private sector. Government is committed to encouraging business, not to doing business itself.

Mexico is in desperate need of investment that cannot be generated from domestic savings. It also finds itself competing with low-cost havens in eastern Europe and Asia for technology and scarce world capital. Therefore, Salinas has lifted almost all currency and ownership controls. Mexico now gives many exemptions to a law prohibiting more than 49% foreign ownership of a Mexican corporation.

The top marginal tax rate has been reduced from 60% to 35%. Tariffs have been reduced from an average of 45% to 10%. Non tariff barriers have been all but eliminated. Only 6% of imports now require licences compared to 95% in 1982. Salinas broke the powerful and corrupt Oil Workers' Union by jailing its leader, Mr. Joaquin Hernandez Galicia. He also began imprisoning rich tax dodgers.

Most important, Salinas has tried to gain the confidence of international markets. Alfredo Phillips admitted that Mexico's poor image as a debt burdened Third World nation must change.[23] The government's steps towards fiscal responsibility have certainly been encouraging. Spending cuts and tax hikes have reduced inflation from 160% in 1987 to 20% in 1988. In 1981, the deficit was 8% of GDP. By 1989, Mexico had the largest budget surplus in its modern history at 8% of GDP.[24]

The improvements in the government's finances have been matched by the private sector. Private corporate debt has declined from $24 billion in 1982 to $4.7 billion in 1989. As a result, Mexico's

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[23]ibid

[24]H.E. Dr. Jaime Serra, 24 September 1990.

private sector now has access to lending from foreign banks.[25]

Mexico has shown dramatic success in its goal of diversifying industrial production from import substitution to exports; and in lessening dependency on oil for export earnings. In 1982, oil accounted for 78% of exports; while non-oil exports totalled only $4 billion. By 1990, oil accounted for only 33% of exports; while non-oil exports had increased to $16 billion.[26]

The Salinas administration represents an extraordinary change in attitude for Mexico. They have become gung-ho free marketers. Salinas believes that future economic growth is dependent upon access to U.S. markets. For this reason, he wants a free trade deal with the United States. Presently, two-thirds of Mexican exports go to the U.S. U.S.-Mexican trade has tripled to $52 billion in the last four years. Also, Mexico now imports nearly as much from the U.S. as does Japan. Meanwhile, Mexican-Canadian bilateral trade amounted to only $2.3 billion.[27] Yet, Canada has been asked to join into the negotiations and on September 24th, 1990, Trade Ministers Crosby and Serra jointly announced Canada's participation.

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[25]ibid

[26]ibid

[27]Baker, 103.

CANADIAN OPPOSITION TO A NORTH AMERICAN FREE TRADE AGREEMENT

Bilateral Canada-Mexico trade in 1989 was only U.S. $2.3 billion. Mexico is only Canada's 17th largest trading partner representing less than one percent of Canadian trade.[28] With present trade between the two countries so low, very little would appear to be at stake. However, many Canadian businessmen feel "Canada can ill afford to stand aloof while current discussions take place between the United States and Mexico which could reshape North American trade and investment flows."[29] They fear that if Mexico and the U.S. sign a FTA, Canadian goods will face stiff competition in the U.S. market. This could nullify any opportunities gained through the Canada-U.S. FTA.

Alfredo Phillips stated: "Canada is a high priority for Mexico." However, Salinas' interest in Canada appears to be motivated more from political considerations than economic. There is still a prevalent anti-"Yanqui" sentiment in Mexico. A North American free trade agreement, that included Canada, would be easier for Salinas to sell politically than a bilateral agreement with the U.S.

Canada's participation in the present negotiations is occurring at a time when a recession and numerous plant closings are causing many Canadians to question the benefits of the Canada-U.S. FTA. As could be expected, the Canadian Labour Congress is leading the fight against a trilateral agreement. "...Canadian Labour Congress statistics show 80,000 jobs were lost as a series of plants shut down or moved to cheaper production sites in the southern United States and Mexico. Ontario was hardest hit."[30]

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[28]Laver, 40.

[29]Econoscope, The Royal Bank of Canada, November 1990.

[30]Linda Diebel, "Canadian activists meet in Mexico City to fight free trade", Toronto Star, 5 October 1990, A19.

The CLC sent a delegation of activists opposed to a NAFTA to a conference in Mexico City. The CLC fears a further loss of Canadian jobs to low-paid Mexican workers. They are also concerned about pressure to lower wages and a deterioration of living standards for Canadian workers. Bruce Campbell, researcher with the CLC, said of a NAFTA: "It cuts jobs for thousands, especially in the lower-end manufacturing sector, and forces them into even lower-paying service.[31]

Some labour leaders are radical in their opposition and challenge the so called benefits that will occur to Mexican workers. Leo Gerard of the United Steelworkers said Canada should impose a special tariff on countries that oppress workers. The duty should equal the differential in wage rates between the two countries and the proceeds would be used to modernize Canadian industry and help developing countries.

As radical as Gerard's views might appear, they have been echoed by Audrey McLauglin, federal NDP leader: "'Our party says we cannot continue to build our economies by exploitation of other people.'"[32] She wants any agreement to include standards for workplace safety and protection of the environment.

Ontario Premier Bob Rae has said of a NAFTA: "'It is an absurd adventure...at this point to do this without providing any kind of protection or leadership for workers whose lives have already been devastated by the impact of free trade.'"[33] He also has called for

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[31]Shawn McCarthy, "Free trade with Mexico would cost jobs, MPs told", Toronto Star, 8 November 1990.

[32]Tim Harper, "New trade pact with Mexicans morally wrong, NDP leader says", Toronto Star, 15 October 1990, A3.

[33]Peter Morton and Geoff Scotton, "Canada to join in U.S.-Mexico pact", Financial Post, 25 September 1990, 1.

any agreement to include environmental protection, labour standards, basic democratic rights, and measures to protect communities and workers.

Although less radical in its opposition, the federal Liberal party has also expressed concern over a potential agreement. Jim Peterson, the Liberal caucus' industry critic said: "'Direct competition with Mexican workers who earn $1.60 per hour...means transferring Canadian companies and jobs to Mexico.'"[34]

Critics complain that Canadian labour is failing to adapt to the ongoing globalization of world markets. "The more serious problem is labour's failure to adapt to the demands of an economically interdependent world."[35]

However, opposition in Canada does not come solely from the labour movement and the opposition parties in Parliament. It can also be expected from some segments of the media, economic nationalists, and various interest groups. There is a sense that a NAFTA would benefit workers in white-collar and technical jobs at the expense of blue-collar workers. "The only winners, aside from corporations, might be a few high-income yuppies, intent on conspicuous consumption while others lose jobs here or work for starvation wages abroad."[36]

"The problem for proponents of free trade is that the benefits of an accord are less tangible than plant closings."[37] It would be

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[34]Financial Post, Editorial, 12 September 1990.

[35]Fred Blaser, "Canadian labor needs to shift focus", Financial Post, 19 April 1990, 14.

[36]Joan MacNeil, "Continental trade talks a recipe for inequality", Toronto Star, 26 September 1990.

[37]Baker, 113.

extremely difficult for a Canadian government to sell a NAFTA in the present political and economic environment. It might even be political suicide.

MEXICO'S POLITICAL INSTABILITY

It has already been mentioned that Mexico had achieved political stability through the alliances forged by its ruling Institutional Revolutionary Party (PRI). At one time the Mexican president ruled "like an Aztec emperor".[38] However, quarrelling between various factions within PRI has led to serious internal rifts. A number of groups, including much of the National Peasant Confederation, has deserted the party for the left wing, populist Democratic Revolutionaries.

Further, the Mexican government has come under increasing international pressure over corruption, electoral fraud, and human rights violations. The Organization of American States has written a report in which it documented electoral fraud during the 1988 election. Mexico denounced the report, claiming it had "'a democratic system, in which all political parties participate'".[39] Salinas was forced to promise electoral reform, but PRI has been described as being in ruins and for it "to win honestly, Mexicans may have to be convinced that it is willing to lose. So far they are not".[40]

Opponents of a NAFTA are quick to point to Salinas' lack of democratic principles. For example, a recent Toronto Star article attacked his administration for undemocratic practices and human rights violations. "Carlos Salinas de Gortari, Mexico's nominal president, was, by most accounts, defeated in the last election, and only governs by virtue of massive electoral fraud and political

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[38] Mexico, Time Life Books Inc., 139.

[39] Linda Diebel, "The dark side of sunny Mexico", Toronto Star, 14 October 1990, B1.

[40] "Doing the impossible takes a little longer", Economist, 9 June 1990, 43.

oppression. In the last one and a half years, at least 70 opposition figures have been murdered."[41] Even a report from the Jesuit Centre stated that "'repression has increased during the first year of the (Salinas) government'".[42]

In summary, Mexico's future political stability is at best questionable. Wide spread poverty, regional disparity, an increasing desire by a large segment of the population to follow the lead of the eastern European countries into true democracy, and adverse world opinion, may undermine the foundation of Mexico's political system. At best, foreign investors should be wary before committing large amounts of capital to Mexico's economic transformation.

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[41]MacNeil.

[42]Diebel, 14 October 1990, B1.

THE CANADA - U.S. FREE TRADE AGREEMENT (CUFTA)

Potential Effects on the Canadian Economy

Canadian trade policy over the past half century has been guided by the principle, which is embodied in the GATT but not always observed, that substantial economic and other benefits will result from the reduction of barriers to world trade and the maintenance of an orderly system of trade rules.

"Canadian trade policy has been directed, in particular, to gaining more open and secure access to markets in the U.S. in exchange for a reciprocal dismantling of Canadian barriers to imports".[43] An important objective has always been to put in place rules to constrain the adoption of trade protective measures by the U.S. that could damage Canadian interests.

The Canada-U.S. free trade agreement offers the potential for increased real incomes and increased trade to both countries. But the size of such gains will depend on the relative impact of changes on several key factors. These include specialization, scale and rationalization, terms of trade, trade diversion, and the flexibility of both product and factor markets. The expected adjustment problems could be more manageable if appropriate assistance policies are adopted.

The CUFTA should increase real income in Canada by redistributing income shares toward the factors of production used extensively in exporting sectors. The pull exerted on factors toward tradeable sectors depends in part on the relative rates of protection (tariff

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[43] G.E. Salembier, A.P. Moroz, S. Frank.
The Canadian Import File: Trade, Protection and Adjustments, (Montreal: The Institute for Research and Public Policy, 1987), p188.

and non-tariff barriers) in these sectors prior to free trade.

In addition to gains in efficiency due to improvements in resource allocation, removal of trade protection to domestic industries would reduce prices and increase real income by lowering the costs of imported goods to consumers as well as producers.

Research in the late 1960s, and the 1970s, concerning Canada - U.S. labour productivity, per capita income comparisons, and scale economies, concluded that Canada's productivity and real income were substantially below U.S. levels. This was largely due to the poor productivity performance of the manufacturing sector.[44] This, in turn, was attributed to inefficient production practices, such as the use of small and inefficient plants and short production runs. The gap was seen to be a direct result of the small Canadian market. Therefore, it was argued that by opening up a much larger market and permitting Canadian producers to take advantage of scale economics and specialization, free trade with the U.S. would improve productivity, and raise real incomes in Canada. Hence the size of the potential gains in productivity and real income from a free trade agreement was viewed as depending critically on the magnitude of the prevailing Canada - U.S. productivity gap and the importance of scale economies in explaining this gap.

It is commonly argued that a small country such as Canada would benefit much more from liberalized trade through two main types of scale economies: industry size economies and rationalization of industry. "Economies of industry scale measure the response of average costs to changes in the level of industry output. The important sources of industry scale economies include: indivisabilities, economies of specialization and mass resources,

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[44]S. Magun, S. Rao, and B. Lodh. "The Impact of Canada-U.S. Free Trade on the Canadian Economy", (Ottawa: Economic Council of Canada, August 1987) p45.

superior organization of production processes, etc."[45]

In addition, free trade could significantly improve productivity by inducing changes in the structure of manufacturing industries. Close to 70% of the Canadian manufacturing industry is composed of small and suboptimal plants, operating with above average unit costs. Removal of tariff and non-tariff barriers, and increased import competition would force Canadian manufacturing firms to rationalize their operations and reduce their average costs. Increased domestic competition would reduce the number of suboptimal plants through mergers and takeovers. In other words, free trade induced restructuring would increase the average plant size in manufacturing.

"Canada - U.S. free trade, by increasing competition in the Canadian economy and providing freer access to a much larger market, could considerably reduce the manufacturing labour productivity gap and improve real income in Canada."[46] In particular, bilateral free trade with the United States should improve real wages, increase output and employment, stimulate business investment and productivity, lower prices, reduce government budget deficits, and strengthen the Canadian dollar vis-a-vis the U.S. dollar.

The removal of tariff barriers should increase both exports and imports. However, since on average Canadian trade barriers are larger than American, imports should rise more than exports, dampening some of the real income stimulus to the Canadian economy.

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[45]ibid, 45.

[46]ibid, 53.

Potential Effects on Specific Industries

In most of the industries the net impact of bilateral free trade on output and employment will be positive and significant; with primary industries, construction, and service sectors accounting for close to 85% of the gains in output and employment. For example, four service industries: retail and wholesale trade, and commercial personal and business services alone would contribute close to 65% of all the new jobs.[47] These substantial gains in service sector output and employment reflect the importance of services in the modern Canadian economy and the size of the indirect effects of free trade on the Canadian economy.

Within the manufacturing sector, durable industries would on average benefit more from bilateral free trade than the non-durable manufacturing industries. In fact, five of the six trade-negative industries, all of which are in the manufacturing sector, would be the non-durable industries, (rubber and plastics, leather, textiles, knitting mills, miscellaneous manufacturing and electronic products).[48] These industries are now highly protected in Canada, compared to the U.S., and therefore would undergo important structural adjustments.

Similarly, furniture and fixtures, metal fabricating and machinery industries also get more trade protection in Canada than in the U.S. But the indirect benefits to these industries from Canada - U.S. free trade would more than offset the negative direct effects. "Wood, primary metals, and printing and publishing would

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[47]Bruce Gates, "Fretting over the GST and free trade", Financial Post, 25 December 1989, 28.

[48]Ahmad Jaleel, "Trade Related, Sector Specific, Industrial Adjustment Policies in Canada: An Analysis of Textiles, Clothing, and Footwear Industries", (Ottawa: Economic Council of Canada, March 1988), 26.

benefit proportionally, more than the other trade-positive manufacturing industries."[49]

The printing and publishing industry would receive substantial benefits from the positive indirect effects of free trade on real incomes and consumer expenditures.

More specifically, "Canada's minerals and metals industry will derive important benefits from the agreement. Some will be immediate and other will come in the late 1990s when the effects of trade liberalization permeate the entire economy. The industry is heavily export oriented and will be able to adapt to a more vigorous free trade environment".[50]

In aggregate terms the agreement is expected to generate increases in value of output of Canada's minerals and metals industry, particularly in value-added as distinct from mine output. Exports and imports of minerals and metals are expected to increase. These increases will likely be achieved mainly through increased investment, expansion of processing facilities, and improved productivity at narrow stages of the processing chain. The biggest gains are expected to be in commodities such as aluminium, certain ferrolloys, magnesium and zinc which require large amounts of electrical energy in their production process. Benefits will also accrue to those firms and areas with specialized services related to mineral exploration and production.

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[49]"Top Performers: A Financial Review of Canada's Pulp and Paper Companies", Pulp and Paper Journal, (Maclean Hunter Ltd, 1990), 35.

[50]"The Canada-U.S. Free Trade Agreement on Minerals and Metals: An Assessment", (Ottawa: Ministry of Supply and Services, 1988), 6.

Prior to the CUFTA, the oil and gas sectors had been essentially deregulated and some liberalization of the regulatory regime for electricity, at least with respect to international trade, was under active consideration. The immediate impact of the CUFTA on the average sector will therefore, be modest; mainly effecting uranium, oil, and to a lesser extent, electricity. In the long run however, the agreement will have important "intangible and indirect impact on the energy sector. In particular, market access for energy exporters will be made more secure and the energy investment climate will be enhanced".[51]

Similarly, "the Canadian fishing industry unquestionably will benefit from the CUFTA. Economic gains will result from new investment in production facilities made in response to new opportunities for value-added processing. Demand for fish products is growing faster than the available supply and industry growth depends increasingly on securing existing markets and increasing exports".[52]

In short, the CUFTA will benefit fishermen as well as processors. A fisherman's economic viability depends on resource availability, the quality of the raw material, and good financial returns for catches. As processors secure an increased share of the American market, raw material from fishermen will be in greater demand. The greater demand in turn will mean increased returns for fish landings.

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[51]"The Canada-U.S. Free Trade Agreement on Energy: An Assessment", (Ottawa: Ministry of Supply and Services, 1988), 37.

[52]"The Canada-U.S. Free Trade Agreement on Fisheries: An Assessment", (Ottawa: Ministry of Supply and Services, 1988), 6.

A MEXICO - U.S. F.T.A. AND ITS CONSEQUENCES FOR CANADA

The success of a Mexico-U.S. free trade agreement that excluded Canada would leave soft sectors of the Canadian economy exposed to competition from Mexican producers, both in the U.S. and domestically, without the cushion provided by transitional arrangements. It would also deprive Canadian producers of the opportunities represented by the opening of the Mexican economy.

A Mexico-U.S. free trade agreement could modify the balance of advantages reached under the Canada-U.S. FTA and could dilute some of its benefits. For instance, it could affect the relative attractiveness of Canada as an investment location for production for the North American market. An agreement excluding Canada altogether would also limit the economies of scale that could be achieved by the addition of a new market.

A deal liberalizing trade between the U.S. and Mexico may not be consistent with some aspects of the Canada-U.S. FTA. If Canada failed to gain enlarged access to the Mexican market, it would then be penalized because it could not expand exports significantly to Mexico but would still face stiffer competition from Mexican producers. Canada would be confronted with a competitive challenge on at least four fronts.

There could be some diversion of U.S. trade away from Canada and towards Mexico. New investment in manufacturing in Mexico combined with low labour costs could give a competitive advantage to Mexican exports over Canadian exports in the U.S. market. Canada has a given share of the U.S. market in certain product lines. This share is currently protected by U.S. trade policies, primarily in the form of quotas, but also in the form of tariffs against Mexican imports. If the United States were to liberalize access, some of the market share would be lost to expanding Mexican firms.

Mexican exports to the U.S. are bearing an increasing resemblance to those from Canada. This is particularly true in the case of the automotive industry. These goods are currently the largest component of merchandise trade between the U.S. and Canada, on the one hand, and between the U.S. and Mexico on the other .

Mexico is also in varying degrees, a competitor in industrial machinery, metal fabrication, textiles, footwear, iron and steel, petrochemicals and paper products. Thus, a Mexico-U.S. FTA which excluded Canada could effect Canadian exports to the U.S. in these products.

There could be greater indirect import penetration from Mexico. The duty free provisions of the Canada-U.S. FTA do not apply to goods purchased in the U.S., if they are manufactured in another country. However, manufactured goods that have a sufficiently low proportion of intermediate content produced in a third country could qualify as U.S. or Canadian products for purposes of further manufacturing. As a consequence, if a Mexico-U.S. FTA is successfully negotiated without Canada's participation, Canada could expect more U.S. finished products, with intermediate components made in Mexico, finding their way into Canada. Further, greater Mexican import penetration into the U.S. may force American producers to shift some of their output to Canadian markets.

Labour cost and locational advantages could divert world investment flows from Canada to Mexico. The U.S. would also be a preferred investment location since it would be the only country with free access to markets in all three countries.

Machinery and transportation equipment, minerals, fuels, and lubricants are the products that will face even greater competition in the U.S. market if a Mexico-U.S. FTA takes place. Also, food,

live animal, beverage, tobacco products, and other secondary manufacturing industries will be badly hurt and possibly driven out of business. Lastly, crude materials, chemicals, and basic manufacturing products will face diminishing access and demand from the American buyers since they will buy cheaper from the Mexican producers.

As mentioned above, automotive parts are currently among Canada's largest exports to the U.S. The US$ 13.7 billion industry, which employs more than 82,000, accounted for nearly US$ 10 billion in trade last year. For the Canadian industry overall, U.S. auto companies are the single largest market, absorbing about 80% of annual production. For many years, Canada was the leading foreign source of parts for U.S. automakers. But recently, Canadian parts manufacturers have seen their market shares slip in favour of Japanese and Mexican products.[53]

The U.S. imported US$ 4.3 billion worth of auto parts from Mexico in 1989, up 80% since 1985. Meanwhile, U.S. imports of Canadian parts rose by only 8% since 1985.[54] Furthermore, for those parts with low shipping costs, limited engineering, simple technology, and few changes in design, Canadian production is very threatened.

In addition, a new Mexican trade law scheduled to take effect in November 1990, would give Mexican based automakers similar benefits to those enjoyed by the Big Three under the Canada-U.S. Auto Pact. That is, qualifying automakers will be allowed to import finished vehicles into Mexico, in proportion to the amount of domestically manufactured products they export. Clearly, Mexico wants to become more competitive in terms of quality and capacity and therefore

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[53]Laura Fowlie, "Mexico could pose threat to Canadian-made auto parts", Financial Post, 24 September 1990, 33.

[54]ibid.

wants to attract new investment to expand their industry.

Mexico suffers from low productivity, poor proximity to assembling plants, enormous inflation, and government instability. Nevertheless, low cost labour (Mexico's hourly manufacturing wage ranges between US 73 cents and US$3.08)[55] makes Mexico particularly attractive for labour intensive production of electronic devices such as wiring harnesses, clips and connectors.

With free trade, Mexico may soon be poised to erode the position of Canadian manufacturers in the U.S. At best, a Mexico-U.S. FTA would create downward pressure on Canadian wage rates for skilled and semi-skilled workers.

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[55]Clyde Farnsworth, "Bush expected to announce plans during Salina visit", New York Times, 11 June 1990, D1.

BILATERAL TRADE BETWEEN CANADA AND MEXICO

When compared to Canada-U.S. bilateral trade of US$ 171 billion in 1989, Mexico's trade with Canada has been minimal. Bilateral trade between Canada and Mexico amounted to only US$ 2.3 billion in 1989, of which imports from Mexico totalled US$ 1.7 billion.[56] Nevertheless, Mexico is Canada's leading trading partner in Latin America with bilateral trade increasing at a rate of 17% annually since 1987.

Crude oil imports from Mexico have fallen sharply since the beginning of the 1980s when they accounted for over 80% of total imports. The bulk of Canada's imports are now made up of manufactured products; principally transportation and machinery parts, and various consumer goods.

Canadian exports to Mexico are largely composed of agricultural products, such as oil seed, fruits, grains, dairy products, eggs and honey. Transportation machinery represents the largest segment of durable goods exported.

In the area of trade in services, Mexico and Canada's links are insignificant. Exports to Mexico of a small amount of engineering services is the most important. Clearly, there is room for an increase in Canadian exports of services.

The level of bilateral direct investments between the two countries is also very limited. Mexican holdings of Canadian productive assets are virtually non-existent, while according to the Bank of Mexico, the total value of Canadian investment in Mexican manufacturing industries amounted to only US$ 371 million in 1987. But consideration must be given to Mexico's growth potential. It

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[56]Gordon Pitts, "Mexico-U.S. pact poses many questions", Financial Post, 4 April 1990, 14.

is a Latin American sleeping giant. It has a potential real GDP growth rate in excess of 6% by 1992.[57]

There are several areas in which Canadian expertise could find a market in Mexico. Agricultural and forestry products, pollution control equipment, and telecommunications represent the best opportunities for Canadian businesses. Agricultural production in Mexico is low, thus forcing Mexico to import significant amounts of basic foodstuffs. It is therefore understandable that Canada's most important exports to Mexico are presently in foodstuffs. There exists a potential for a much greater share of the Mexican market in this area.

If it is to become an important player in the international trade arena, Mexico will have to substantially revamp its economic infrastructure. This gives a great deal of potential to Canadian firms in the transportation, communications, and engineering sectors. Canada is well positioned to take advantage of Mexico's modernization drive.

Canada's Export Development Corporation has already established a line of credit of C$ 120 million for companies wishing to export to Mexico.[58] Further financial assistance for Canadian companies wishing to export to Mexico is provided by CIDA. Northern Telecom, Spar Aerospace, and Stelco are among the major Canadian companies presently operating in Mexico.

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[57]Fred Blaser, "Continent-wide trade talks favoured", Financial Post, 28 June 1990, 14.

[58]Financial Post, Editorial, 20 September 1990, 12.

THE CONSEQUENCES FOR CANADA OF A NAFTA

The creation of a North American free trade zone would add to the existing Canada-U.S. FTA. Canada, Mexico, and the U.S. have a combined population of 362 million, GNP of US$ 5.9 trillion, and total trade of US$ 225 billion.[59] With a free trade agreement the three countries would form the largest trading block in the world.

A North American common market would allow Canada further opportunities to specialize and expand economies of scale in production, distribution and marketing. In the long-term, these factors should enhance Canadian competitiveness. Benefits to Canada of a NAFTA were summarized by the Royal Bank of Canada in the November 1990 issue of Econoscope.

> "Freer trade will provide the opportunity for producers to make business decisions based on the principle of comparative advantage rather than on the basis of tariff barriers. Each country will be able to concentrate on the goods that it can produce more efficiently. Even if a country can manufacture a good as efficiently as the other country, it will still benefit the country in question to produce the commodity it has a relative advantage in producing, since specialization will lead to greater overall production and lower costs for the three nations.
>
> With its highly educated workforce, Canada is well positioned to take advantage of the growth in knowledge-based services industries. Canada enjoys a particularly enviable position in areas such as transportation machinery and equipment, telecommunications equipment, and civil engineering.
>
> A reduction in tariffs and non-tariff barriers will offer producers further opportunities to exploit economies of scale in production. Access to larger markets will allow producers to spread the total cost of doing business over larger production runs, thereby reducing average costs per unit of output.
>
> Declining trade barriers should increase competition and reduce price distortions. This should lead to price

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[59]Stephen Baker, 103.

reductions and, in the process, raise the level of real disposable income. Higher disposable income should lead to higher consumer spending which should in turn, stimulate growth in production and employment.

Greater security of access to the various markets for foreign investors as well as the higher income of consumers should lessen the risks of doing cross-border business and attract more investment into North America.

Freer North American trade will not only create job and investment opportunities, but will also expand the availability of goods to consumers and producers."

Jaime Serra, Mexico's trade minister, said the three countries would form a formidable block because they have complementary economies, geographic proximity, market potential, common business practices and together they would be more effective against other trading blocks.[60]

A NAFTA would certainly reduce the prices in Canada of many consumer goods. Mexico would probably be able to supply many of the goods Canada presently imports from the Pacific Rim countries.

A number of Canadian companies have already been active in the Mexican market. Most noticeable of them has been BCE Inc.

Winnipeg's EH Technologies recently purchased a $40 million fibre-board plant in Mexico. The plant, one of the largest in the world, will use Canadian technology, production and marketing knowledge to export its products to the southwestern U.S.[61]

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[60]Serra, 24 September 1990.

[61]John Saunders, "Trade with Mexico has winners, losers", Globe and Mail, 14 November 1990, B26.

Champion Road Machinery Ltd of Goderich, Ontario, has had a minimal presence in Mexico. With free trade it expects to sell more than $15 million of machinery.

Geni Canan of Quebec recently sold $500,000 worth of swine-breeding stock to Mexico. During the first quarter of this year, Canadian exporters shipped $552,000 worth of seed potatoes to Mexico.

Free access to the Canadian market by Mexican wine and distilled spirits should have little impact as consumer tastes would limit the market share potential of these products. However, a NAFTA could exclude beer as was done in the Canada-U.S. FTA. Like their Canadian counterparts, Mexican producers fear that in a free trade environment they could be washed away by a tidal wave of the beer imported from giant U.S. breweries.[62]

FTA rules improving access to the Canadian market for U.S. fresh fruits and vegetables could be extended to Mexico. Provisions protecting Canadian growers, for a 20 year period, from too rapid import penetration could also be included in a NAFTA. Duty free access for Mexican processed food would have little impact, since high transportation costs would prevent such products from gaining much Canadian market share.

Trade in the automotive sector will be the key item for negotiation. The machinery and mechanical apparatus industry could face a challenge. Even without free trade Canada imports 46.3% of total industry demand from Mexico.[63] Finally, the Canadian textile and footwear industries, which are labour intensive, would be the hardest hit by a NAFTA.

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[62]William Watson, "Imports from Mexico not what we expected", Financial Post, 26 October 1990, 9.

[63]ibid.

SUMMARY

Certainly, any change in trading patterns as dramatic and extensive as would result from the creation of a North American free trade zone would have many winners and losers. The potential benefits to Canada have been outlined above. However, at least in the short run, most of these benefits would be enjoyed by large corporations, skilled and semi-skilled workers, and Canadian consumers. Unquestionably, there will be many losers in Canada: jobs will be lost in labour intensive manufacturing industries, there will be downward pressure on wages, painful restructuring in some industries, and a loss of power for organized labour.

Undeniably, the opposition to a NAFTA in Canada will be significant. The Mexicans realize this and fear that Canadian opposition to an agreement could jeopardize their country's chances of successfully negotiating a deal with the Americans. Alfredo Phillips, Mexico's ambassador to Canada, recently told a meeting of the Canada-U.S. Business Association that reluctance in Canada "about a deal with Mexico has soured his country's business community on Canada". He went on to state: "'We are going to have an agreement with the United States. We would like to have a similar agreement with Canada. But it takes two to tango or, in this case, it may take three.'"[64]

Clearly, successfully negotiating an agreement with Canada is a secondary objective of the Mexican government. It will not allow indecision in Canada to frustrate a potential deal with the Americans.

Canada has a great deal at stake in the event of a bilateral Mexico-U.S. agreement. It would be foolish to not at least

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[64]Bob Papoe, "Mexican envoy chides Canada over doubts about free trade", Toronto Star, 21 November 1990, F3.

participate in the negotiations to ensure an adequate input for Canadian concerns. However, politics is the art of achieving the possible. Given the present disillusionment with the Mulroney government and the Canada-U.S. FTA, it is unlikely that the ruling Conservatives could convince Canadians to support a NAFTA. It is unlikely an agreement will be completed prior to 1992. By then Canada would be in a pre-election period and certainly the opposition in Parliament would stall approval of a NAFTA until after the next election - an election few expect the free trade Conservative to win.

Yet, Canadian participation in the negotiating process is important if only to serve as a means of exposing the Canadian public to the pros and cons of North American free trade and the potential consequences to Canada of a Mexican-American bilateral agreement.

Finally, Canadian business leaders should be wary of political instability in Mexico. Major investments in that country in plants and equipment could turn to major losses if the ruling PRI is unable to contain growing opposition. It may be profitable for many Canadian businesses to increase their trade with Mexico; but this should not necessarily include massive amount of direct investment in that country until it has been proven that Salinas' reforms are to form the basis of a permanent restructuring of the Mexican economy.

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The Emerging Continental Market
Canadian Business Opportunities in Mexico
(Jointly sponsored by The Canadian Manufacturers' Association and The Canadian Council for the Americas, Toronto, 24 September 1990)
Guest Speakers:

Dr. Herminio Blanco. Deputy Secretary of Foreign Trade for Mexico

Fred Blaser. Chairman: Mexico-Canada Business Committee

Luis Carcoba. President: Confederation of Industrial Chamber of Mexico

Louise Frechette. Assistant Deputy Minister: External Affairs

Claudio X Gonzalez. Chairman - Kimberly Clark de Mexico
Special Advisor to Pres. Salinas

Alfredo Phillips. Mexican Ambassador to Canada

Roberto Sanchez. President, Mexico's National Chamber of Processing Industries

H.E. Dr. Jaime Serra. Minister of Commerce and Industry Mexico

Dr. Humberto Soto. President, National Foreign Trade Bank of Mexico
President, Association of Mexican Banks

David Winfield. Canadian Ambassador to Mexico

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APPENDICES

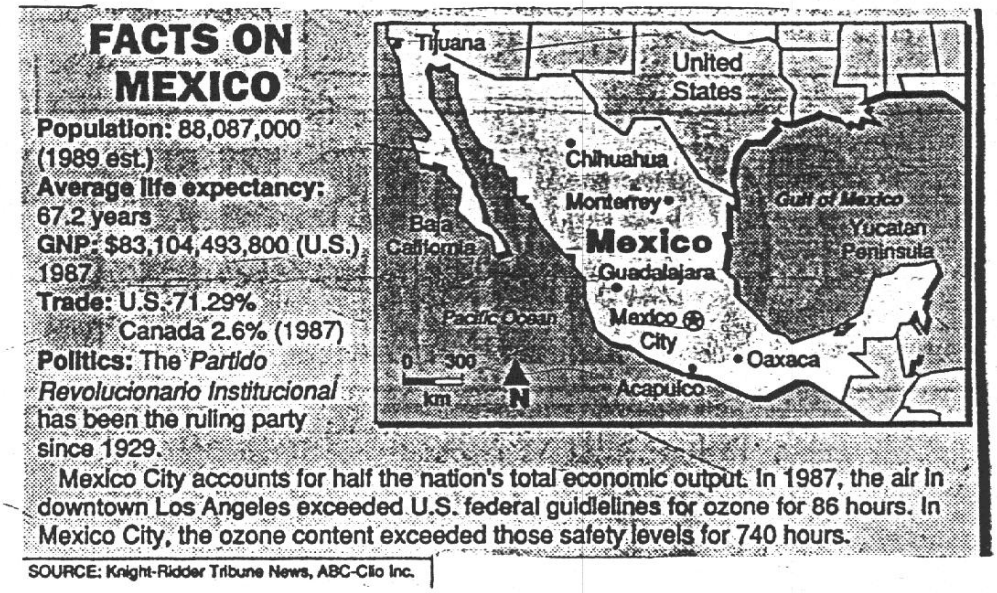


Figure 1: Mexico at a glance

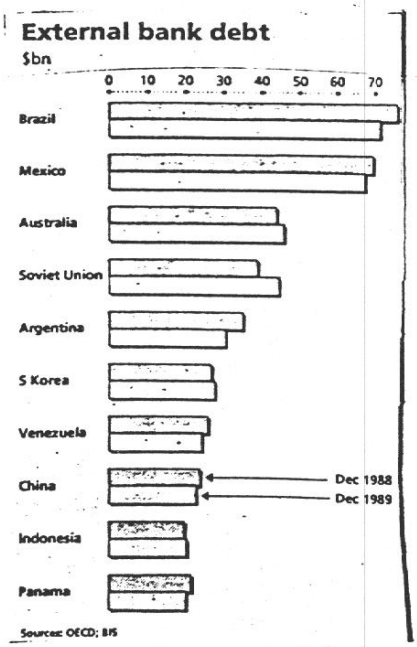


Figure 2: Mexico's external bank debt

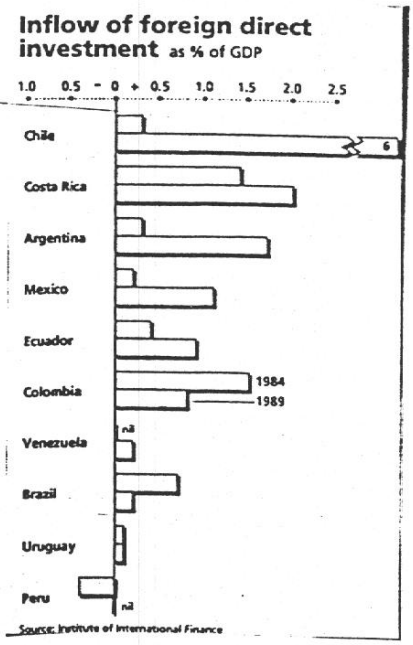


Figure 3: Mexico's inflow of foreign direct investment

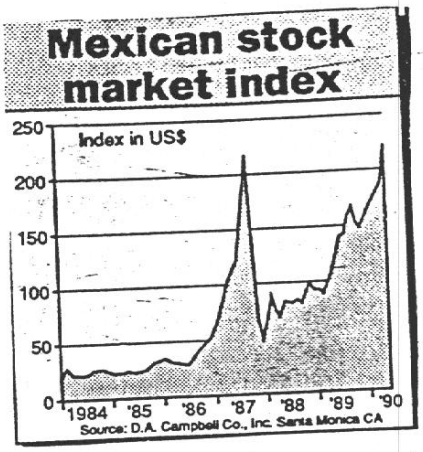


Figure 4: The upward Mexican market stock index

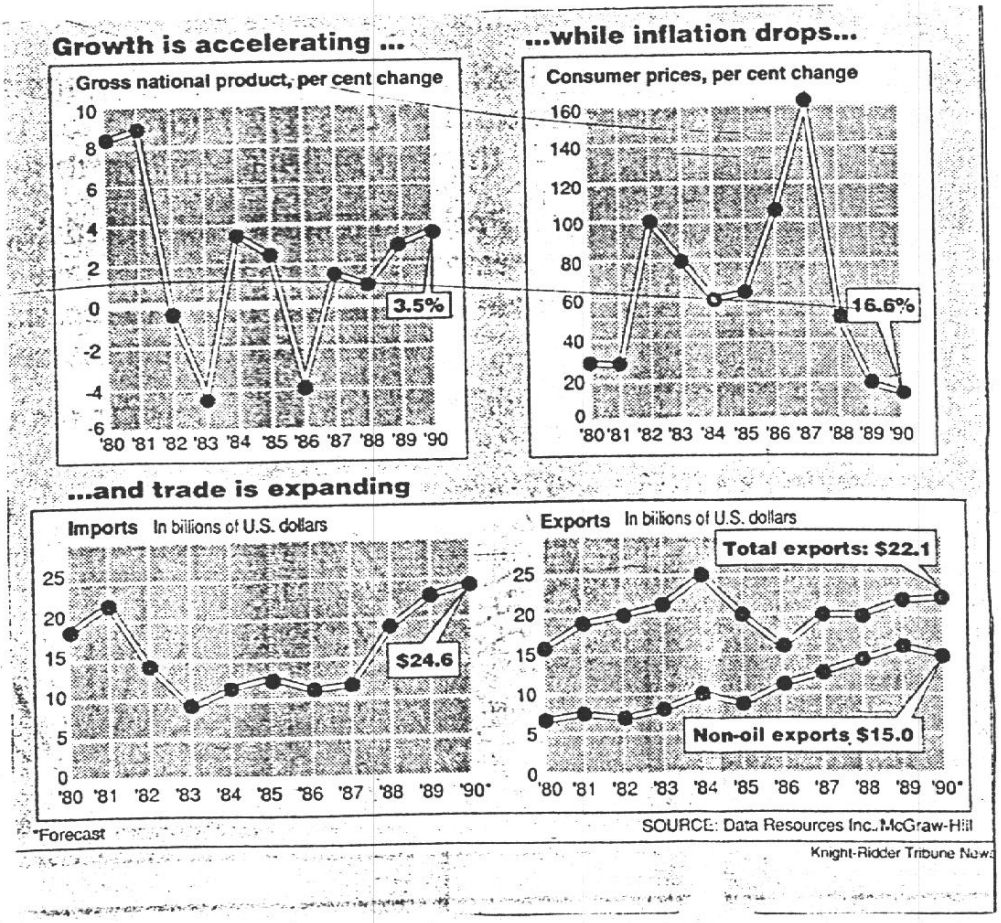


Figure 5: Mexico's economy at a glance

Since 1938, when the government nationalized the oil industry, Mexico's oil production has been rising steadily, but never as dramatically as between 1973 and 1982, when it soared nearly 600 percent. Along with its bountiful oil supplies, it has abundant natural gas; in 1984 alone it produced 1.37 trillion cubic feet. In the mid-1980s, the country's proven reserves of oil and natural gas stood at 72 billion barrels — ranking Mexico second only to Saudi Arabia in reserves. This chart taps into the nation's average daily petroleum production.

Not surprisingly, oil has become Mexico's leading export. More than half the oil pumped is shipped abroad, much of it to the United States.

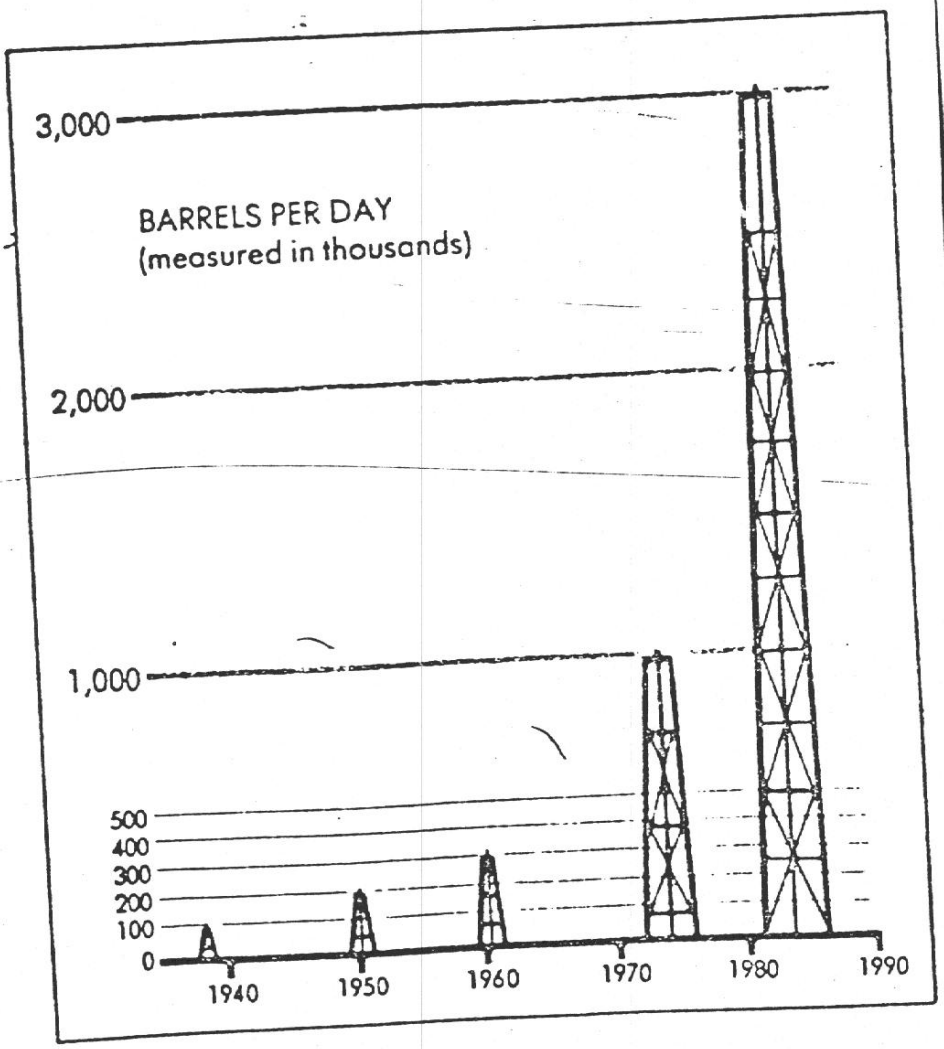


Figure 6: Mexico's oil production

A DRAMATIC SHIFT IN THE WORK FORCE

Industrialization and a growth in the service area of the economy have proceeded rapidly in Mexico since midcentury *(graph at right)*. This has produced a significant shift in the distribution of the labor force, reflecting the transition from a rural, agriculturally based economy to an urban, industrialized and service-oriented one typical of developed nations. As unemployed countryfolk have fled to the cities in search of jobs, the rural proportion of the population has shrunk. In 1950 farm workers accounted for 62.4 percent of the labor force; in 1980 they were 37.4 percent; and by the turn of the century they should make up only 17.8 percent.

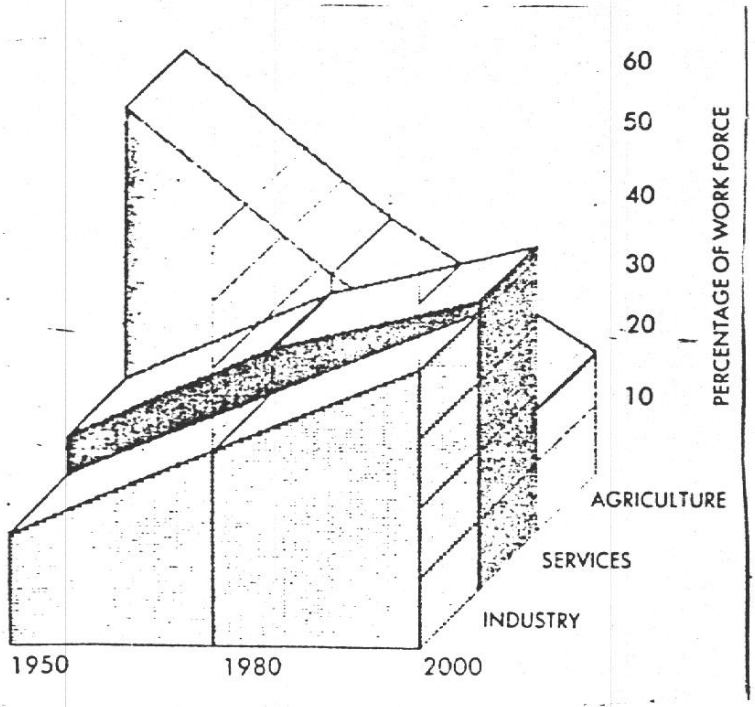


Figure 7: Employment by sector in Mexico since 1950

Made in Mexico

THE FOLLOWING table shows the number of cars produced in Mexico.

	1989	1988	% change
Chrysler	102,734	77,323	+32.85
Ford	87,169	98,815	-11.79
General Motors	63,061	51,477	+22.50
Nissan	86,749	73,045	+18.76
Volkswagen	98,928	53,114	+86.26
TOTAL	438,641	353,783	+23.99

Source: Automotive News 1990 Market Data Book Issue

Figure 8: Car production in Mexico

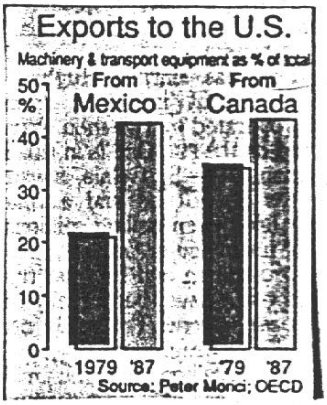


Figure 9: What Canada and Mexico export to the USA

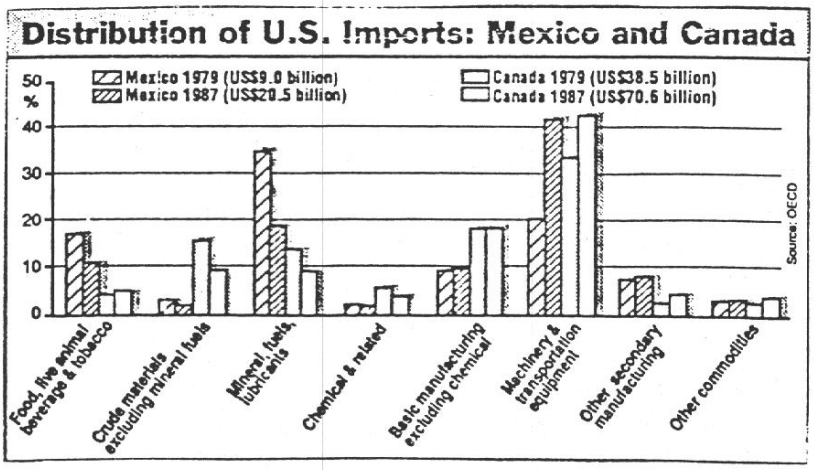


Figure 10: What Canada and Mexico export to the USA, sector by sector

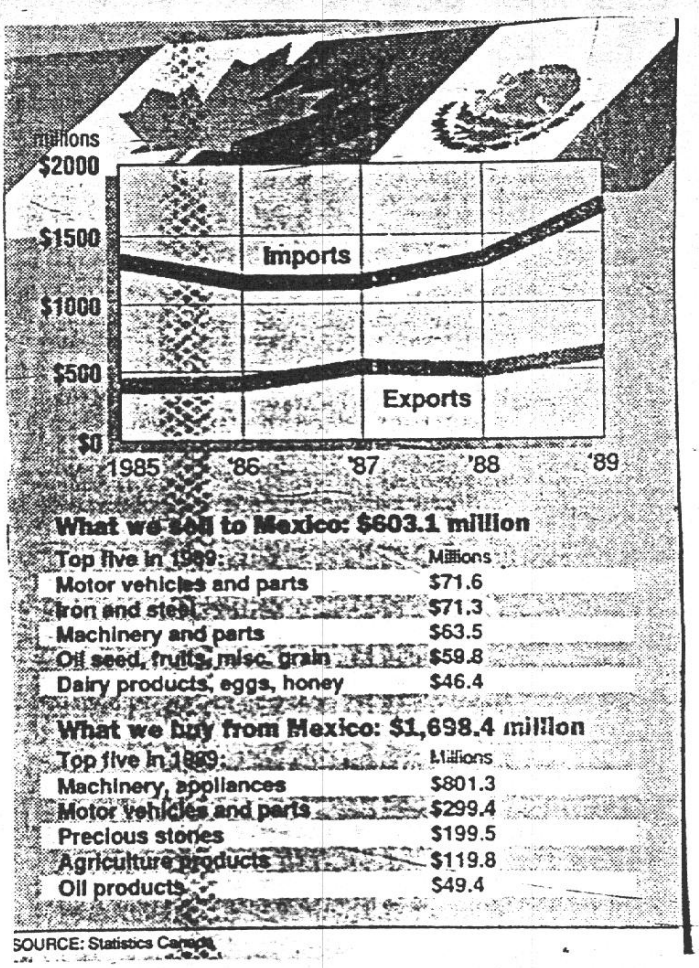


Figure 11: Canada-Mexico trade

Mexican firms ripe for investment

Company Name	Industry	Shares outstanding	Exchange
Grupo Industrial Alfa	Petrochemicals and steel	117 million	Bolsa
Cementos Mexicanos	Cement	330 million	Bolsa
CIFRA	Retail: apparel and food	787 million	OTC
Grupo Condumex	Electrics, auto, plastic	80 million	Bolsa
Teleindustria Ericcson	Telecommunications	300 million	Bolsa
Real Turisma	Luxury hotel operator	264 million	Bolsa
Grupo Sidek	Steel, tourism, real estate	201 million	NASDAQ
Telefonos de Mexico	Monopoly telephone operator	4 billion	NASDAQ
Tubos de Acero de Mexico	Seamless steel pipe	49 million	AMEX
Grupo Vitro	Glass and plastic	51 million	Bolsa

Source: D.A. Campbell Co. Inc., Santa Monica, Calif.

Figure 12: Some opportunities for Canadian in Mexico

Where Canada stacks up

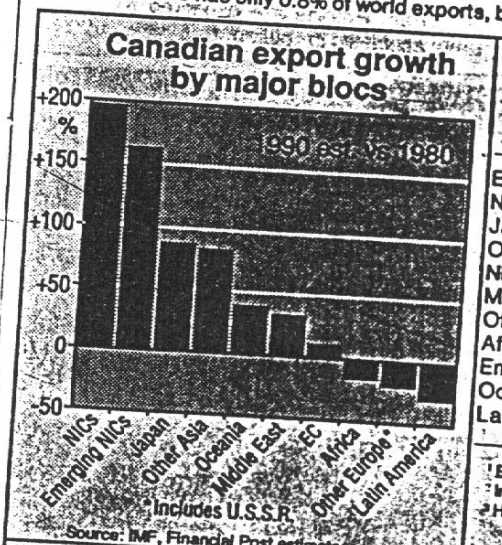
INTERNATIONAL trade is big business in Canada, with exports of goods, services, investment-income receipts and transfers from abroad equivalent to about 25% of gross domestic product.

Canada relies on a surplus in goods trade to help offset its deficit in investment income — where this year we're paying out $23 billion more than we're likely to receive. The reason is large government borrowing and high foreign ownership of Canadian industry. We have a $8-billion deficit in services, and surpluses of $8 billion for goods and $5 billion for transfers.

Despite Canada's reliance on trade, we're just a bit player on the world scene, with only 4.2% of world exports of goods (excluding the Soviet Union) in 1989. That's why we signed the Free Trade Agreement with the U.S. — which has 12.6% of the world pie — and are now talking about a new deal including Mexico. Mexico has only 0.8% of world exports, but with 85 million people, it has big potential.

If we negotiate a three-country trade agreement, North America would be the second-biggest trading block. Last year, this area accounted for 17.5% of world trade vs the European Community's 39.2%. Unlike the EC, North America has been losing market share over the years; it accounted for 21.2% of world exports in 1970. The big winners have been the booming economies of Asia, whose export success has pushed their share to about 24% of world exports vs 15.5% in 1980 and 12.6% in 1970.

Canada has had its strongest export growth over the past decade with Asian countries and the U.S. Exports to the EC have grown just 11% since 1980 vs an average 109% to Asia and 100% to the U.S. Exports to Mexico have been weak, up just 45%. Canada has a considerable surplus in trade with the U.S., about $13 billion this year, and a deficit of around $1 billion with Mexico.



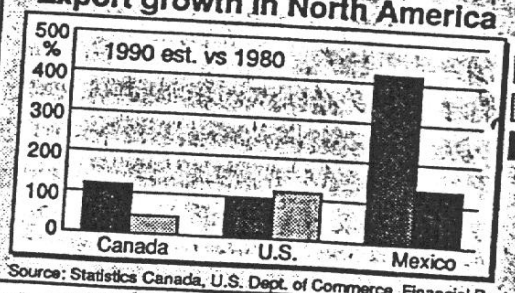
Source: IMF, Financial Post estimates

World export leaders

	World exports % distribution 1970	1980	1989	Export growth 1980-89
EC [1]	40.2%	36.4%	39.2%	+64%
North America [2]	21.2%	16.3%	17.5%	+64%
Japan	6.7%	6.9%	9.5%	+110%
Other Europe	10.1%	8.4%	8.6%	+222%
NICs [3]	2.2%	4.0%	8.5%	+56%
Middle East	4.7%	12.6%	4.3%	-48%
Other Asia	2.1%	2.1%	2.9%	+105%
Africa	4.0%	4.7%	2.1%	-33%
Emerging NICs [4]	1.6%	2.5%	2.6%	+60%
Oceania	2.1%	1.4%	1.6%	+70%
Latin America [5]	5.2%	4.6%	3.2%	+5%

[1] Exports for all countries in the EC at present
[2] Includes Mexico
[3] Hong Kong, South Korea, Singapore, Taiwan
[4] Indonesia, Malaysia, the Philippines, Thailand
[5] Excludes Mexico
Note: Total excludes Soviet Union

Source: International Monetary Fund, Financial Post estimates



Source: Statistics Canada, U.S. Dept. of Commerce, Financial Post estimates

Figure 13: Canada's position in a North American Free Trade environment

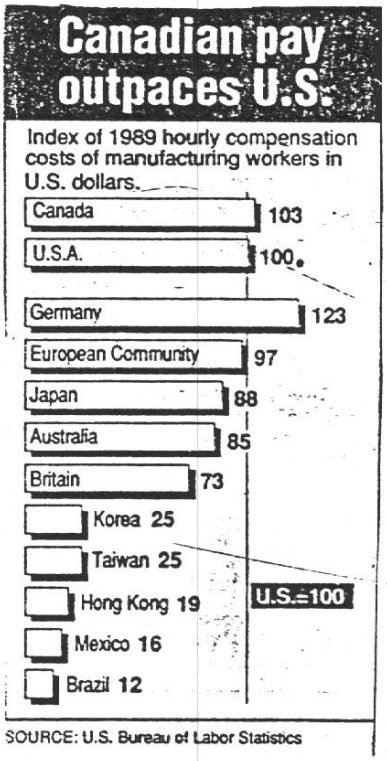


Figure 14: Hourly wage comparisons for selected countries

A tale of three countries

Hourly labor costs, including fringe benefits, for production workers in manufacturing

	$ Cdn.	$ U.S.		
Year	Canada	Canada	United States	Mexico
1989	$17.43	$14.72	$14.31	$2.32
1988	16.65	13.53	13.85	1.99
1987	15.85	11.95	13.40	1.57
1986	15.28	11.00	13.21	1.50
1985	14.75	10.80	12.96	2.09

Source: U.S. Bureau of Labor Statistics

Cheap labor in Mexico's Maquiladora sector

Customs-bonded assembly plants along the U.S. border handle labor-intensive work for U.S. manufacturers. Workers in such plants appear to earn roughly half as much as Mexican manufacturing workers in general.

Hourly labor costs, 1988, in U.S. dollars, for Maquiladora production workers.

Industry	Wages	Benefits	Total
Total food and related products	$0.62	$0.13	$0.75
Apparel and textiles	0.60	0.16	0.76
Footwear and leather	0.68	0.21	0.89
Chemicals, chemical products	0.78	0.20	0.98
Furniture and fixtures	0.77	0.24	1.01
Electrical and electronic	0.75	0.27	1.02
Transportation equipment	0.84	0.25	1.09
Toys and sporting goods	0.81	0.31	1.12
Machinery and equipment	0.93	0.22	1.15
Maquiladora average	**0.74**	**0.24**	**0.98**

Source: U.S. Bureau of Labor Statistics

Figure 15: Mexico's competitive advantage through cheap labour