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Mexico's Quest in the North American Markets

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Mexico's Quest in the North American Markets

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Submitted to the International Studies Program, Trinity College

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Abstract:

Since the 1980s Mexico has implemented various economic policies that have improved its financial system at times. All the policies have ultimately failed. Since the 1990s both Mexico and China have made progress in foreign trade with their respective trade organizations. Mexico entered the North American Free Trade Agreement (NAFTA) in 1994 and China joined the World Trade Organization (WTO) in 2001. In spite of being a part of two different trade organizations, both countries had a significant increase on their GDP and consequently a change of focus and direction towards their internal investments to enhance their production of exports. Unfortunately, these two counties have recently experienced frequent overlapping of their exports; which has increased the competition between the two countries. This thesis examines the possibilities and procedures that Mexico, along with its NAFTA

partners, must follow in order to evade the economic harm generated by the rise of the Chinese economy.

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Introduction:

The desire for economic development and stability has led countries to opt for specific financial policies to maximize output and gain advantages over other countries. Even though the Mexican government believes they have made the necessary changes in their international economic policy to be at the forefront of their potential, Mexico, along with its NAFTA partners, has not yet implemented strategies that give priority to trading among themselves without losing investment to other markets such as China. Moreover, Mexico should take advantage of its place in North America and use it as one of their economic strengths against Chinese competition. Therefore Mexico must focus on specializing in the goods that can be produced with good quality and at a faster rate. If Mexico fails to effectively implement policies that can set them apart from Chinese production, the Mexican economy will be harmed tremendously in the coming years since China and Mexico often find themselves producing similar type of goods. Furthermore, it is of utmost importance that Mexico changes and improves its economic infrastructure in several sectors of the economy.

This thesis examines the economic and historical factors that have led Mexico to choose and adopt economic policies since the international debt crisis and the peso crisis. Most of the economic policies that Mexico has implemented since the 1980's have failed due to the lack of policy planning, failure to spread the wealth among the entire population, corruption on behalf of the Mexican government, and erroneous choices that will be analyzed throughout this paper.

Mexico's economic performance before the 1980s is addressed in chapter one. The second chapter examines the two Mexican economic crises- the peso crises of 1976 and the economic debt crisis of the early '80s. Finally the third chapter is an in depth analysis of NAFTA, its strengths and weaknesses, its future, and an analysis of opportunities it should take. It is important for us to examine the economic policies implemented in the past to be able to learn from them and make changes for the future. Currently Mexico is facing the competition of China, which has been referred to as the "red demon" by several economists. China is quickly gaining territory on the same exporting products and markets around the globe, specifically in the U.S. markets. This increases the competition for Mexican producers tremendously and has clearly harmed their markets. Therefore Mexico, along with its NAFTA partners, must now act to change the direction in which their economies are heading and reorganize their infrastructure.

Chapter 1:

Import Substitution industrialization.

From the 1940s to the 1970s Mexico enjoyed rapid economic growth as a result of the strategy known as import substitution industrialization (often called ISI). This economic policy was implemented in many Latin American countries with the intention of generating local development by producing and consuming internal products. In other words, the intention was to create a self-sufficient economy with a local market and one that is less dependent on foreigners. This highly protectionist economic policy was supposed to transform Latin American countries from a rural economy to a more industrial economy. Nevertheless, this economic policy did not work favorably for the Latin American countries. For those countries with larger populations, such as Brazil and México, it worked for a little longer given that they were politically more stable and had a larger internal market. Their geographic location and population worked to their advantage in the creation of an internal market. The ISI worked for a shorter period or did not work at all those countries with a smaller population and a lack of resources, or political instability, since they were unable to create a strong local market.

Scholars have argued that although the ISI policies implemented in Mexico were "largely responsible for the economic miracle of the 1960's, they also laid the groundwork for the high rates of borrowing capital flight on the 1970s."[1] As mentioned before, the political stability in Mexico was vital for the functioning of ISI policies. President Avila Camacho (1940-1946) was one of the initiators of the idea of promoting the expansion of the economic base of the country in many sectors of the country. The aim was to create employment and rapid economic growth, but mainly to improve the standard of living via the local production and consumption of goods.

Why did ISI work for Mexico in the beginning?

The "financing of the ISI was initially facilitated by high wartime demand in the United States for Mexican mineral exports such as zinc, copper, lead, mercury and cadmium."[2] Profits were made on materials such as petroleum and rubber since they were also supplied by Mexico to the allied forces. Secondly, the *bracero* program was implemented in 1942 which allowed Mexican workers to work in the United States temporarily. This was an agreement made by the United States President Franklin D. Roosevelt and the Mexican president Manuel Avila Camacho. World War II created a

[1] Ramírez, 42
[2] Ramirez, 43

massive labor shortage in many sectors of the United States economy, especially in the agricultural sector. A third important step implemented by the Avila Camacho government was to support the creation of a development bank and industrial entrepreneurship. Therefore the expansion of *NAFINSA* (Nacional Financiera, Sociedad Anonima) in the 1940s played an indispensible role. This organization was created by the federal government in 1936 with the purpose of founding a financial society that grants capital to Mexican banks to restore liquidity and promote industry. It participated in the creation of firms and industries, offering training and technical assistance, specially financing the emergence of mid-size companies. For example "it loaned and invested from 85.4 million pesos in 1942 to 1,228.7 million pesos by the end of 1947."[3] Evidence of this is the establishment of Altos Hornos de Mexico. This is a steel mill founded in 1942 located in the north of Mexico in the state of Coahuila. Local engineers and bankers had the idea of building this industrial unit, nevertheless they did not have the economic resources and the machinery needed. NAFINSA participated in projects like these. According to Ramirez, in order "to secure the necessary financing, NAFINSA negotiated a loan with the U.S. Export-Import Bank for $6 million." [4] Next, the development bank played a crucial role in acquiring the necessary machinery and

[3] Ramirez, 44
[4] Ramirez, 44

equipment" purchasing them or obtaining them by donations mainly from the United States.

Why ISI failed to live up to its expectations.

During the Avila Camacho administration the country's "real GDP increased at an average yearly rate of 6.2 percent, while per capita product increased at an impressive 3.3 percent."[5] All the sectors of the economy registered growth rates and, more importantly, total and public investment more than tripled from the 1940s to 1952. Nevertheless, this was based on a captive market designed by the government's protectionist policies, a situation that brought as a consequence the development of firms without a solid competitiveness relative to other countries. There was a lack of development in the exporting sector of Mexico, which led to further stagnation of economic growth. This condition did not allow a truly independent and modern industrialization that could have contributed to Mexican economic development in the following years.

Presidents Avila Camacho and Miguel Aleman opted to "raise the rate of capital formation in the private sector through increases in the real profits of that sector. This

[5] Ramirez, 45

meant that increases in wages had to lag well behind increases in prices."[6] Another reason for wage reduction was the increasing migration of rural laborers to the urban sector, which was unable to absorb job seekers. The excess supply of labor in the urban sector contributed to the wage reduction. By the end of the 1960s and early 1970s there was a lack of productivity and an uneven growth of the agricultural and urban sectors. The country's exports declined relative to its imports as compared to previous years. This is what Raul Prebisch, the secretary-general of the UN Economic Commission for Latin America (ECLA) at the time, described as the deterioration of the terms of trade between the industrial and the rural sectors. This situation accelerated "inflation accompanied by growing current accounts imbalances, and an increasing reliance on foreign funds to finance the country's external and internal deficits."[7] The interconnectedness of these problems is the main reason for the political, social and economic instability that eventually caused an economic crisis in the late 1970s.

Chapter 2:

[6] Ramirez, 62

[7] Ramirez, 71

The economic crisis

By 1972 president Luis Echeverria faced a critical situation in which the economic and social future of Mexico hung in the balance. The President had two options: either to continue to promote industrialization or begin to redistribute the country growing wealth.

> *The Echeverria administration decided to do both at the expense of monetary and financial stability; it embarked upon a populist program designed to raise the state's provision of collective consumption goods, such as subsidized health and housing, and to accelerate the process of import substitution in the capital goods sector.*[8]

With the first action the Echeverria administration was attempting to reduce the social tensions that had arisen as a consequence of the government's poor performance. The second action was aimed at generating rapid economic growth, profits, and jobs, while reestablishing the confidence of the private sector. To accomplish these goals the Echeverria administration implemented two policies. One was to increase government spending and the second one was to postpone necessary tax reforms at the time. These polices did not work as expected. From the beginning of the implementation of these policies until 1976, the public sector deficit as well as the money supply had at least tripled. Inflation also quadrupled during the same period.[9] You need to cite other sources besides Ramirez to support your claims.

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[8] Ramirez, 82

[9] Ramirez, 83 (Table)

By the end of Echeverria's governance the economic situation had worsened, inflation increased while real GDP declined. This caused many local and foreign investors to lose confidence in the peso which led to capital flight to the United States to place their wealth in a more stable economy. According to Mexican economist Solis, the growing uncertainty among private investors caused Mexico around 4 billion pesos in investment to flee the country in 1976.[10]

The IMF in Mexico and why its policies failed.

President Lopez Portillo established an agreement with the International Monetary Fund promising to reduce the public deficit, decrease the money supply and public investment, begin trade agreements with other countries, and limit the amount of labor compensations.

The IMF has provided financial capital and designed programs for economic recovery in many countries. According to Pastor, the Fund has the right to advice countries experiencing economic difficulties on how to strategically stabilize their economies and generate economic recovery. On the other hand, the IMF also has the power to obstruct crucial financing that can potentially come from other private creditors. Despite this power, Peru and Jamaica tried to obtain payments directly from

[10] Francisco J. Alejo, 16

private creditors in the 1970s. "Although these were ultimately unsuccessful, the fact that countries even attempted to reject the Fund's financing and advice in favor of private credit and stabilization programs indicated a general weakening of the Fund's institutional power."[11] The debt crisis came in the 1980s and soon three-quarters of Latin American countries were operating under some IMF stabilization program that was accompanied by a high degree of conditionality.

The Latin American countries were responsible for meeting the goals laid out in the stabilization programs in order to receive help from the Fund. The Fund would also withhold credit to problem debtors unless there was a fresh influx of capital from the bankers as well. By setting these harsh conditions the IMF had a monopoly over lending in Latin America and used its power to determine the economic policies of Latin America. The Fund maintained a "case by case approach that blamed the crisis on various domestic mistakes and maintained separated negotiations between itself and individual countries."[12]

Some of the economic policies that the IMF recommended for the Latin American countries were a devaluation of the currency, a reduction of the fiscal deficit, a decrease in real wages, and a relaxation in the terms of trade by reducing tariffs and subsidies to

[11] Pastor, 296

[12] Pastor, 297

make exports more attractive to foreigners. All these policies were problematic. For instance, since all these policies were recommended to all Latin American countries, if every country devalued its currency at the same time, then no one would gain an advantage over the other. That is, the growth rate of their exports would simply decrease. Also, at the time these policies were implemented, the world economy was in recession and foreign countries did not have the income to buy goods from the countries which devalued their currencies. Lowering domestic wages decreased the demand for domestic goods and since foreigners and domestic consumers had little or no income to purchase products, the Latin economy as a whole was hurt.

In the case of Mexico, the IMF forced the country to decrease its rate of inflation. Therefore, the Mexican government decided to reduce wages so that the rate of growth of the money supply could be reduced. These actions by the government came too little too late and in 1978 home and car prices increased alarmingly.

Rising inflation and external debt are the two main reasons why the IMF program did not work in Mexico. First of all, as the government was trying to pay its external debt through the profits generated from the new found oil reserves, it undermined the poor sector of its population. The government fixed nominal wages for unskilled labor while there was extreme inflation in the country. The poor were slowly forgotten, and there were price increases for everything even the most common foods for this part of the population. The cost of the *tortilla* and the *bolillo* (a certain kind of bread that many construction workers eat) more than doubled in price. Gas and domestic gas also doubled in price. During this period the gap between the rich and the poor widened extremely as Mexico did not restrict its domestic investors from sending their money overseas. Secondly, the Mexican government, with the oil market boom made a bad effort diversifying its exports. It could have used its labor and capital to produce other types of goods such as footwear, clothing, electrical machinery, construction services and the like. This could have helped relieve the pressures from the IMF and led the country to recover faster. The modernization of Mexico's industrial sector and the promotion and diversification of its exports along with the liberalization of the national economy were the most plausible options open to the Mexico in order to stabilize its economy. With these fiscal and economic reforms Mexico experienced economic growth.

Chapter 3:

Mexico and NAFTA

The past two chapters have covered the economic policies that several Mexican governments have implemented for the development of the country. These polices have gone through three different periods. First, from a protectionist and regulatory regime to an economy controlled by an international organization such as the IMF. The current stage of the Mexican economy is one which is associated with pursuit of market-base, outward-oriented policies, such as the North American Free Trade Agreement (NAFTA).

The North American Free Trade Agreement (NAFTA) is a treaty that was signed by Canada, Mexico and the United States and created the world's largest free trade area, which now links 450 million people producing $17 trillion worth of goods and services. It is the largest free trade area and the richest market in the world in terms of combined GDP. NAFTA's ultimate goal is to eliminate taxes among the three North American on all goods is not possible. Moreover, there was an immediate elimination of tariffs on more than half of Mexican exports and one third of U.S. exports. The rest of the tariffs were scheduled to be eliminated in the next ten to fifteen years.

It has been argued that Mexico's main interest in entering NAFTA was not necessarily to have access to the North American particularly U.S. market. Rather its main motivation was to provide incentives to increase foreign direct investment (FDI) in to the country. Although NAFTA has generated economic growth by increasing Foreign Direct Investment and trade between North America and Mexico, it has also been limited to the manufacturing sector and unfortunately it has had relatively little impact on other sectors of the Mexican economy. Structural reforms in the financial, energy and other domestic sectors have lagged behind those in the manufacturing sector over the last few decades.

During president Salina's government, Mexico was in need of financial resources. Foreigners did not find it safe to invest in Mexico due to "erratic policy shifts, 'Mexicanization' laws, and the bank expropriations."[13] Salina's reforms failed to convince domestic and foreign investors to put money into the Mexican economy. Instead, domestic investors would rather put their money overseas, which hurt the Mexican economy tremendously. It is estimated that $20 billion dollars of assets owned by Mexican investors are being held offshore.[14] With the increasing outflows of money and the investors' low confidence in the Mexican economy, president Salinas decided to propose the NAFTA in order not only to increase trade, but mainly to regain domestic and foreign investors' confidence.

Mexico was considered a great exporter with the exception of agricultural and textile products. Nevertheless, the Salinas administration realized that by implementing the free trade agreement investors would be more willing to invest in Mexico so as to have easier access to the North American markets. Secondly, Mexico "wanted NAFTA in order to guarantee foreign investors that their property rights would be protected."[15] This was the Salinas administration's main goal because by protecting investors' rights

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[13] Maurer, 10
[14] Maurer, 10
[15] Maurer, 11

he hoped that more capital would flow to Mexico. His goal was to raise Mexican productivity through foreign investments and by raising the level of competition with local companies, forcing them indirectly to be more competitive, thus increasing their productivity and causing the economy to grow as a whole.

Foreigners that invested assets in Mexico after 1994 "did so in order to use Mexico as an export platform to the United States," which, in essence, was also part of Salina's goal because it would bring FDI into Mexico.[16] However, after the peso crash in 1994-95, foreigners were hesitant to invest in non-financial non-export industries. The foreigners' motivation to invest only on the export sector is due to the fact that they earned revenue in dollars compared to the other sectors that earned revenue in Mexican pesos. Since the peso had been frequently devalued and had recently crashed, it was not convenient to be earning revenue in pesos. Therefore, it was far less risky for investors to keep the U.S. dollar as their currency. On the other hand, export industries benefited when the peso lost value, since their revenue in dollars was not affected and "many of their costs especially wages dropped in dollar terms."[17] It was painless for the export sector, they were earning in dollars and spending in pesos, earning on a more expensive currency and spending on a weaker one.

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[16] Mauer, 11
[17] Mauer, 11

Wages and Living standards under NAFTA

During the 1980s and the early 1990s, real wages of unskilled workers fell due to Mexico's initial trade opening. By 1987, Mexico joined the General Agreement on Tariffs and Trade (GATT) that forced the lowering of prices of textiles, furniture, and shoes in order for these industries to be more competitive among other countries that had joined the treaty. Lowering of prices brought as a consequence the lowering of wages of the unskilled labor that worked in the manufacturing sectors mentioned above.

Once NAFTA went into effect, the wage gap between the unskilled and skilled labor narrowed. This time the "skill-intensive" industries such as automobile and auto parts companies were the ones most affected by having to lower wages.[18] The textile industry in Mexico was one of the most benefited by NAFTA: it was in high demand and had a privilege over other countries' textiles industries. Since this industry was in high demand the real wages for the textile industry in Mexico rose while wages for the automobile and auto parts fell. The closing of the wage gap happened in 1994 and 1995.

The economic improvements at the beginning of the 1990s under NAFTA were not spread evenly throughout Mexico for several reasons. Mexico has a better transportation and telecommunications infrastructure in the Northern part of its territory, which in fact contains the better educated population in the area. The

[18] Maurer, 19

maquiladora industry is also located in northern Mexico along the border with the U.S. which facilitates the transportation and delivery of goods to the U.S.

On the other hand, the southern part of México has not experienced the improvements in infrastructure that the North has experienced. In Mexico since "1993, per capita GDP has fallen at an annual rate of 1 percent in the southern states."[19] One of the reasons is the South's specialization in agricultural production and the lack of entrepreneur companies in the area, in contrast to the north. Another reason is that due to the distance of Southern Mexico and North America, the North part of Mexico enjoys a lot more FDI from the United States since its closer and therefore it is easier and faster to transport goods. As the author Maurer suggests; the Mexican government has to improve its economic development in the South of its territory to equalize growth, or else there will be continues migration to the north of México and the United States from southern states.

The improvements in the North of Mexico took place before China joined the World Trade Organization (WTO) which is the successor of GATT. China's entry to the WTO has drastically influence Mexico's advantage of trade with North America in the low skilled sector of the economy. Mexico's competition increases dramatically with China on the radar, given the fact that China is known for its massive labor supply, low

[19] OCED 2002

production costs and large quantities of production. Therefore, Mexico must change its economic focus and localize the areas where it can be superior to China and other competitors to specialize on those sectors. With China as a trade adversary, it is going to be challenging for Mexico's unskilled sector to continue to be as profitable as it has been in the North of México.

Bottlenecks that Mexico faces

There are several bottlenecks that Mexico currently faces. First, in Mexico only 3.3 percent of electricity is privately generated. This is a serious problem since electricity constitutes a very substantial cost for many of Mexico's industries. There is an "increasing demand for electricity in Mexico, in fact, prices have risen 50 percent in the last five years" and the cost in Northwest Mexico, are now "more than twice the level in Arizona".[20] Consequently many factories close to the U.S. border are considering moving their operations to the U.S. This is one more reason that discourages investors of putting their money in Mexican factories.

Second, the petroleum sector remains nearly completely closed from private investment. Mexico made the energy and petroleum sectors government's property which prohibits private investments and exploration. Private investors "are forbidden

[20] Maurer, 16

from participating in either drilling or basic refining."[21]This consequently has a negative result on the development of the petroleum sector because it slows down the potential growth rate of a major booming industry. It has even hurt Mexico to the extent that it imports petroleum when it has enough quantities of oil to be self-sufficient on petroleum terms. The government is not doing enough to promote and explode this industry; it instead is wasting time and not taking advantage of its natural resources to generate economic growth.

Third, the telecommunications and internet connections' rates are very high in Mexico because the government has allowed the company Telmex to create a monopoly on telecommunications. Other companies have tried to compete with Telmex's monopoly and attempted to enter the telecommunications markets but Telmex has been able to fight out all its competitors. Telmex currently controls two thirds of Mexican telecommunications and it has expanded to the U.S., Argentina, Colombia Brazil and other Latin American countries. The result is that "Mexico remains deficient in telecommunication services, and charges remain high by international standards."[22] Part of this is the government's fault for allowing one single telecommunication's firm to take control of most of the sector, and in addition allowing this company to charge high prices for a service.

[21] Maurer, 16
[22] Maurer, 16

Fourth, Mexico also suffers a tax-collecting problem; in 2003 Mexico collected 18 percent of its GDP in taxes while the U.S. collected 28 percent. With a population larger than 150 million people, only 5 percent pay taxes. Moreover the wealthy avoid most of their tax payments through corrupt transfers, benefiting individually, but hurting the country's economy. Others avoid taxes by shopping in the large informal sector that exists in Mexico. As a result of the low tax income, the Mexican government struggles to find capital to invest and be able to expand education, health and other social needs of the populations.

While many blame the government and complain about the low quality of these services, its both the people's fault for evading tax payments and the corruption within the government who keeps much of the tax money collected. As a consequence, Mexico has seen a decline in its education system due to low investment in public schooling. "Mexico's per-student expenditures are only 30 percent of Greece's, 18 percent of Japan's, and 16 percent of the USA's." [23] This shows the lack of investment in education that brings many negative consequences to the Mexican people and the country itself. Less skilled labor, increase in crime and lower wages for the people among others.

These bottlenecks are some of the reasons for Mexico's failure on being able to develop its economy better with the goal to catch up with the first world economies. On the one hand investment clearly remains below the normal to develop an infrastructure

[23] Maurer, 17

that can possibly bring economic growth. On the other hand the Mexican government allows companies such as Telmex to charge absurdly high rates. Instead, the government should control companies like Telmex in the way they charge to provide their service and collect more money in tax form to increase government spending and build a stronger infrastructure that benefits everyone and not just a few. Ironically, the Mexican government does not allow private companies to invest in Pemex. Private investment in Pemex can certainly help boost and expand its production, as well as increase its competitiveness worldwide. Privatization of Pemex can also help reduce corruption within the firm, and take its production more seriously. Being a government owned firm, companies often find themselves subject to corruption since the Mexican government currently has high levels of fraud and dishonesty. The fact that the government controls Pemex has caused stagnation on the company's oil search, the government has become too passive in their domestic oil exploitation to the extent that they had to import oil from abroad having their own petroleum plants. If Pemex was a private company it could get loans for oil expeditions, and if a member of the corporation is not contributing anything to the firm, the company can make quick changes on their employee force and be more productive under less corruption. Finally Mexico has clearly failed to collect sufficient tax to build a solid infrastructure able to spend in education, security and health among other public services.

Maquiladoras in the Mexican Economy

As I have mentioned before, most of the FDI went to the manufacture sector, specifically to the maquiladoras. The maquiladoras are factories usually located in the northern part of Mexico close to the United States where plants import material, equipment and capital on a tariff free basis mainly from North America for assembling, processing and manufacturing goods. The "number of maquilas in Mexico has jumped from 2000 in 1994 to 3,333 in 1999."[24] Most of the firms in this area are owned by the U.S. companies "with well-known names such as American Home Products, Beatrice Foods, Caterpillar, Eastman Kodak, Frito-Lay, Ford, GM, IBM, Levi-Strauss, Mattel, Motorola, Pepsico, Siemans, Sony, Wrangler, and Maiden form, to name just a few."[25] Once the product is finished it's shipped out to markets around the world, especially to the United States under the NAFTA treaty in order to avoid tariffs. Maquiladoras have a significant contribution to Mexico's GDP. In 2002, "maquiladora exports made up

[24] Ramirez (2003), 7
[25] Ramirez (2003), 7

roughly half of all exports. Their production was roughly 17 percent of Mexico's GDP."[26]

On the other hand, NAFTA has helped Mexico's economy in its export industry because most of its goods are consumed by the U.S. However, whenever the U.S. economy is struggling or going through a recession, Mexico's economy is deeply affected since as noted above its exports are a large component of Mexico's GDP and the U.S. consumes a little more than ninety percent of these goods. This is evidence by how "Mexico has been dragged into a severe recession by the faltering U. S. economy in the past two years."[27] The U.S. recessions in the past decade consequently lead to hundreds of plant closings in the north of Mexico. In less than a year "240,000 maquiladora workers had lost their jobs, 19% percent of total Maquiladora employment."[28] This figures show the dependency from Mexico to the U.S economy. Indeed this dependency can be dangerous for Mexico's prosperity from two different views. First, if the U.S. happened to find a market that is more convenient for them and they decide to stop importing from Mexico. On the other hand if Mexico for some reason finds itself not producing the goods that the U.S is used to consume then the U.S will have to look for another exporter.

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[26] Mauer, 14
[27] Ramirez (2003), 8
[28] Ramirez (2003), 8

Unfortunately, productivity across the Mexican economy has not grown evenly. One of the reasons is because domestic and foreign investments have gone primarily to the manufacturing sector, which constitutes only one fifth of the Mexican economy. This sector reached its peak in the year 2000 producing 20 percent of Mexico's GDP; however it has steadily declined since. In order to increase "domestic investment, the Mexican government needs to reform energy petroleum, telecoms, tax system, infrastructure and education, but the country had made very little progress on any of this fronts.

NAFTA in the present and the emergence of the Chinese economy

The rise of China involves opportunities as well as obstacles for many countries in south Asia and Latin America. Their abundant low labor cost, prosperous foreign investments and an increasing skilled labor among other reasons have given them the opportunity to expand their markets at the expense of others. As a result NAFTA has been highly affected due to the emergence of China, specifically Mexico since it is increasingly in competition with Chinese manufactures. Therefore if countries like Mexico want to rescue their economy they must change their export structure; first by upgrading the value added of their exports, secondly, by focusing on issues such as distance and time costs that can work for their advantage and lastly implementing a new and competitive infrastructure with the help of their NAFTA counterparts.

In the paper by Wise, the NAFTA members are compared and contrasted with one another. She mentions that although Mexico has double the growth of its GDP per capita from 1995 to 2000, "the rise of real income in Mexico has hit a virtual plateau"[29]. Wise says that one of the reasons for this stagnation in the Mexican economy was due to the lack of success of Mexico to reduce inflation and interest rates that had already been achieved by its other two NAFTA partners. Canada and the US were engaged in a free trade agreement implemented in 1989 known as CUSFTA, five years before the North American free trade agreement would include Mexico. According to Wise, this gave Canada an advantage compared to Mexico since it had been engaged in free trade with the US for longer and had settled markets with high demand, such as the commodities market. However, Canada did not hold to this trading advantage for long.

In few years after the creation of NAFTA, Mexico caught up quickly and eventually "tripled its GDP outpacing Canada's improvement. The number of patents granted to Mexico increased at a faster rate than did those of the US, while Canadian patents decreased".[30] Without NAFTA Mexico's "global exports would have been 50 percent lower and foreign direct investment would have been about forty percent

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[29] Wise, 12

[30] Wise, 16

lower."[31] Clearly, the Mexican economy was benefited by NAFTA. It increased its GDP per capita every year, it enhanced Mexico's competitiveness, it increasing its productivity, it diversified Mexican exports to be less dependent in oil and NAFTA also increased foreign direct Investment in Mexico. These advancements in the Mexican economy were significant but certainly not enough, they were unsustainable and they did not reach the expectations of the NAFTA engineers.

Changes of the Mexican economy under the influence of China

One of the Mexican government's goals to implement NAFTA was to stimulate exports of the manufacturing sector. In the early years of NAFTA before China had a big influence in the U.S. market, Mexico succeeded in attracting FDI in the automotive and electronics sector. Yet Mexico has failed to maintain the same rate of growth experienced in the earlier years. Furthermore, not only Mexico but the three countries, Canada, Mexico and the U. S have been losing ground in the world trade of manufactures to other economies. In fact since the formation of NAFTA in 1994 to 2000 the three countries were deeply integrated into the manufacturing global market all three countries increased employment in this sector, "by 8.4% in the region, 1.4 percent in the U.S., 23.4 percent in Canada, and 39.2 percent in México."[32]

[31] Wise, 16
[32] Gallagher, 34

Contrary to the period from 2000 to 2009, where the NAFTA "region together lost 6.3 million jobs in manufacturing, or 27 percent of total employment in the sector."[33] This signifies that since 2000 to the present the general integration of these three countries has deteriorated. This situation has only worsened after the global crises of 2008.

Mexico's economy has struggled since the 1940s with the lack of appropriate domestic investment reforms. Mexico boosted its economy throughout the late nineteen's with FDI but it did not helped set on a base for long-term economic growth. For example from 1980 to 2007 "Mexico's per Capita GDP growth rate was one tenth that of China."[34] Several specific events have strongly affected NAFTA and the economic relationship between Mexico and North America. Recently, Mexico's manufacturing sector has been one of the most affected by the emergence of China. By the end of 2009 more than half of its labor force went unemployed due to the lack of demand of Mexican goods throughout the early 2000s and the economic crisis of 2008. This was also caused by the relocation of maquiladora's operations to "lower wage countries in Central America and Asia, particularly China."[35] Secondly the trade integration between Mexico and the United States has declined steadily. In the manufacturing sector, the drop has been more evident with Mexico's "share of U.S.

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[33] Gallagher, 28
[34] Gallagher, 28
[35] Ramirez (2003), 9

manufacturing imports dropping from levels above 80 percent in 1990's to 45 percent in November 2008. [36]These figures clearly represent the decreasing economic integration between the two countries. Thirdly, the high dependency on the U.S. trade and economy affects Mexico both positively and negatively. For example, in the economic crisis of 2008 the demand for many goods such as automobiles fell tremendously. Mexico is the largest supplier of auto parts and automobiles for American companies such as GM, Chrysler and Ford providing more than half of the autos to these companies. Since the demand for automobiles decline in many countries during the economic crisis of 2008, Mexico's auto manufacturing sector was negatively affected tremendously. Finally the last key issue to fully understand Mexico's decline in manufacturing is the emergence of new competitors for the U.S. market. Recently Mexico drop from being the largest exporter to the U.S to be second after China. The low cost of Chinese imports have made Mexican imports look expensive and unattractive for U.S. companies.

Obstacles for Mexico under the rise of China

Wise identifies three obstacles that impede Mexico's development. The first obstacles that she identifies are corruption and institutional modernization. The lack of

[36] Gallagher, 29

government effectiveness and political stability clearly affects Mexico's economic progress as it makes economic policies harder to execute. It also diverts domestic and foreign direct investment towards other countries due to the lack of investors' confidence to invest their assets in an unstable country.

The second obstacle that Wise develops is the divided government in Mexico. In previous years the executive branch in Mexico had enough power to implement economic and political policies more handily, nevertheless due to the strengthening of the legislative power in recent years it has diminished its strict power to conduct economic policies and therefore left Mexico at a disadvantage in perusing economic policies such as NAFTA.

The third obstacle that Wise identifies is the idea of geographical proximity. Mexicans thought they did not have to worry about competition, but in recent years China has made huge inroads increasing its exports to the US "23 per cent in 2004 versus 3 per cent in 1990.[37]" Some of the causes of China's rapid advancement are their lower cost of production, much greater labor force, more tax incentives, their investments abroad and their investment in the educational infrastructure "turning out some 600,000 engineers and thousands of other qualified professionals each year.[38]" These are some of the predominant reasons that show China's solid economic, political

[37] Wise, 25

[38] Wise, 25

and social infrastructure that will keep their economy highly competitive and with a concrete foundation.

Both essays by Lidoy and Hogenboom present substantial evidence of how China's trade impact in the world has benefited some countries but has also harmed others. For example in the essay by Lidoy he mentions that "in 1988, nearly 60% of United States shoe imports came from South Korea compared to a meager 2% from China. By 2005 China's share was more than 70% while United States imports from South Korea and Taiwan had dwindled.[39]" This is one of the examples of China's impact in the global markets and how it gains territory in foreign markets at expense of others. After China joined the WTO in 2001 its exports and imports increased immensely. Between 1990 and 2002 Chinese exports had "increase 425%, this implies, by definition that other countries are losing market shares" and China is simply replacing them and making vast profits.[40] Chinese goods compete with other emerging economies in South Asia and in Latin America. Currently any country whose export structures are similar to that of China is being greatly affected by the rapid expansion of the cheap and abundant Chinese production of goods; such is the case of Mexico. On the other hand countries with opposite export structures are more likely to be benefitting from the emergence of China such as Argentina, Chile and Brazil (to some

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[39] Lidoy, 18
[40] Lidoy, 19

extent). Those countries like Argentina that export mainly commodities face lower competition, given the fact that China does not export commodities, but rather imports them, they often find themselves being trading partners and as a consequence benefitting each other. Chile was one of the countries that highly supported China's entry to the WTO because they "aimed to achieve foreign direct investment from China, particularly to the mining sector".[41] Brazil is another country that has been profiting from rising commodity exports and Chinese investment. Although in recent years the trade between China and Brazil has turned a bit hostile since China has persistently tried to force Brazilian exports to remain fixed, benefiting China and harming Brazil. China has also increasingly sought for foreign investment abroad in Latin America and Africa to secure their supply of commodities and other necessary goods for their economy and production. The development of this solid infrastructure stabilizes and strengthens their long term economic expansion, securing the supply of resources necessary for their long-term economic development.

Moreover those countries such as Mexico, that specialize in information and technology, electronics, clothing and low value added goods will find themselves in high competition with China. "While 90 percent of the PCs produced in Mexico go to the US, China is increasingly replacing Mexico in this market"[42]. Therefore the economic

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[41] Hogenboom, 143
[42] Hogenboom, 148

approach by all the affected countries such as Mexico must change otherwise China will soon devastate their markets.

What are the modifications that Mexico and NAFTA have to consider in order to improve?

For Hogeboom there are three main tasks that Mexico should change. First, he mentions there should be "regional cooperation and integration in Latin America and make sure that the returns of the commodity boom are invested in economic modernization for the long-term" in the countries.[43] Similar to what China is doing securing their long-term economic growth. Secondly there should be a "regional infrastructure that invests time and money in political, institutional and social integration" as well as construction of roads and pipelines for a better transportation of their goods.[44] Thirdly, recognize the situation that these countries are facing to be able to "develop a new model" of their economic strategies. [45] For example Lidoy mentions that in order for Mexico to become more competitive it should change their export structure "by upgrading the value added of their exports" to make them more competitive. Another aspect that Lidoy suggests is that Mexico should focus on those

[43] Hogenboom, 150
[44] Hogenboom, 151
[45] Hogenboom, 151

goods where “time costs are both a quantitatively and a quality” important.[46] This will allow Mexican goods to be more competitive and effective than Chinese goods when exporting them to the US markets. Time costs for the production of certain goods really matter and if Mexico is more capable of delivering a better good at a faster rate than China is, then most likely the US will take the Mexican goods. Wise also suggests that in order for Mexico to be more competitive there has to be a “technological guidance, and development assistance from its NAFTA partners “to formulate a better infrastructure for a superior trade with North America. [47] Lidoy, Hogeboom and Wise all suggest that Mexico should invest “more vigorously in infrastructure, technology transfer” and work with the US to reduce the time at the border for security checks to reduce the time costs even more. [48]

The emergence of the Chinese market as mentioned before is clearly benefitting but also harming other markets. In order for the disadvantaged countries to overcome China’s threat they most make the necessary adjustments.

Reforming the Investment policy

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[46] Lidoy , 26
[47] Wise, 14
[48] Wise, 33

In order for Mexico to aim for long term economic growth it should change its investment regime. Mexico should promote and protect domestic investment, while ensuring that foreign investors are not privileged over domestic investors. Make long term investments that create jobs and help the country develop a sustainable economy.

Moreover, the NAFTA laws should go under review since foreign investors have shown that they would challenge any government measure that is on their way of achieving success. For example "NAFTA has to date been used to challenge: measures to control gasoline content and protect groundwater resources; a legislative ban on the export of hazardous resources; the creation of an ecological park; the regulation of open-pit mining near Native American scared sites and most recently the implementation of safety standards for foreign trucks."[49] NAFTA was created to encourage investment but many foreign investors have clearly gone out of proportion with their demands. In other words lawyers have the ability to sue governments for any situation that investors disagree or are unhappy with. They use NAFTA laws as a way of protecting their business in case of failure. This is also difficult for the government's, since it gives an opportunity to unhappy investors to threaten countries with expensive fines.

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[49] Van Harten, 44

For these reasons the three countries should come together to make the appropriate modifications to NAFTA's laws. Otherwise one of them could be facing a situation close to the one Argentina is facing. This country has received approximately 46 claims for its reforms in the face of the country's economic crises of 2001. These claims brought by foreign companies have cost Argentina billions of dollars and have had an important impact on its economy. This is an example from which the three North American countries should learn and take action before it's too late.

Investment treaties should allow governments to be better protected and be able to take action against foreign investors that threaten governments with senseless claims. There should be a balance in the regulation of these laws, one where the governments does not target and discriminate foreign investors under particular circumstances and at the same time investors do not bring unnecessary claims. For any kind of disputes, NAFTA should offer an independent and fair process separate from both the investors and the country in case consistent with NAFTA laws and principals. Another sector that needs an urgent change is the manufacture sector or maquiladora industry.

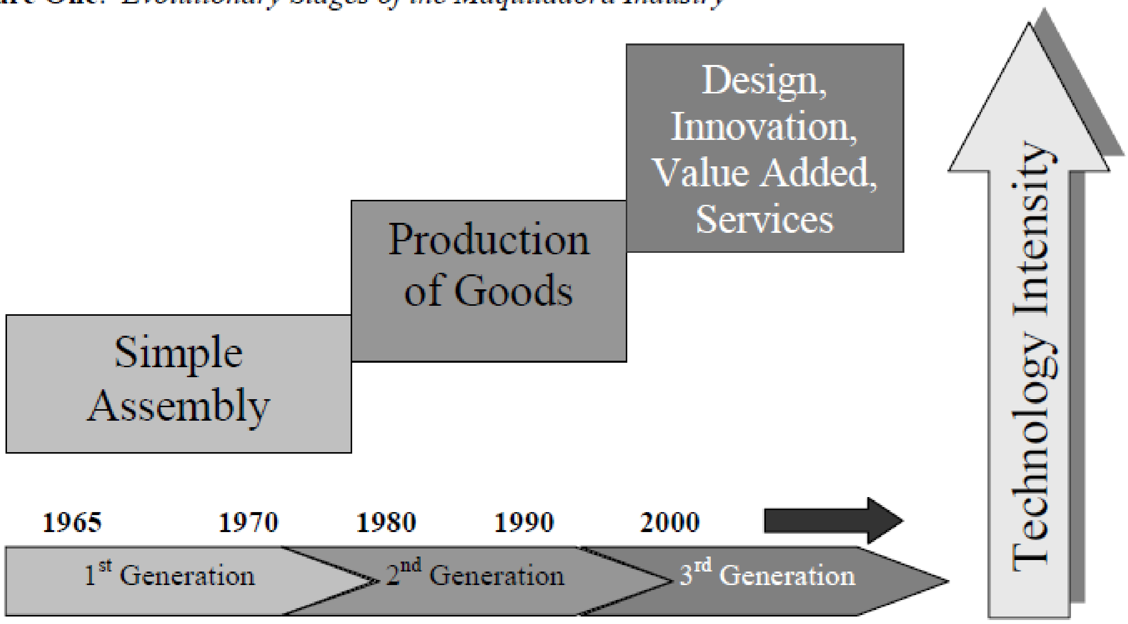
Mexico's maquiladora industry includes auto parts, medical products, electronics, and items for aerospace. Scholars have decided to classify the maquilas into three different types or generations to show the differences between these factories. The first generation plants perform the simplest assembly tasks. The second generation plants produce more refined manufacturing products and the third generation utilize technological intensive production to assembly high quality goods. The maquiladoras are the producers of most of the export that go to the U.S. Before the rise of the Chinese economy, the U.S imported 90 percent of Mexican exports. In the last decades Chinese competition has caused a reduction of the maquiladora plan. The difference in compensation rates is very significant, it is estimated that Chinese labor is one third to one half cheaper than Mexican labor. Therefore, this represents a problem to the maquiladora industry since its production is more expensive than in China. From 67 of the maquilas in Monterrey Mexico only 37 percent of the maquilas survived in 1994. Few maquilas producing apparel "23 percent, furniture zero percent, or leather zero percent were still active while 60 percent of the electronics and 68 percent of auto part producers remained."[50]These shocking figures show the influence of Chinese production and how fast its production is taking over markets of other countries.

Scholars such as Lidoy argue that Mexico should not try to regain low wage assembly jobs but as an alternative develop the higher value added and technology intensive sectors. Mexico has already started to develop this sector and many maquiladoras have already made the transition from the first and second generation to the third, upgrading its products on the foundations of advanced technology. This shift has helped saved a few more maquiladoras from losing to the Chinese competition.

[50] Sargent, 7

Mexican policy makers argue that by shifting from the first generation production systems to a higher value added with a more technology intensive model the maquiladoras have experienced better results in their exports to the U.S. As mentioned before some goods produced in the maquiladoras such as the auto parts are still great exports from Mexico that have slightly increased their demand of labor from 2000 to 2005 while maquiladoras specialized in other sectors have completely vanished. Figure one demonstrates the approach that the Mexican maquiladoras are trying to achieve.

Figure One: *Evolutionary Stages of the Maquiladora Industry*



Source - Presentation made by María de Rocio Ruiz Chávez, Subsecretaria de Industria y Comercio, Secretaría de Economía, entitled *Visión Global de la Industria Manufacturera de Exportación* at the National Maquiladora Convention, October 27th, 2005.

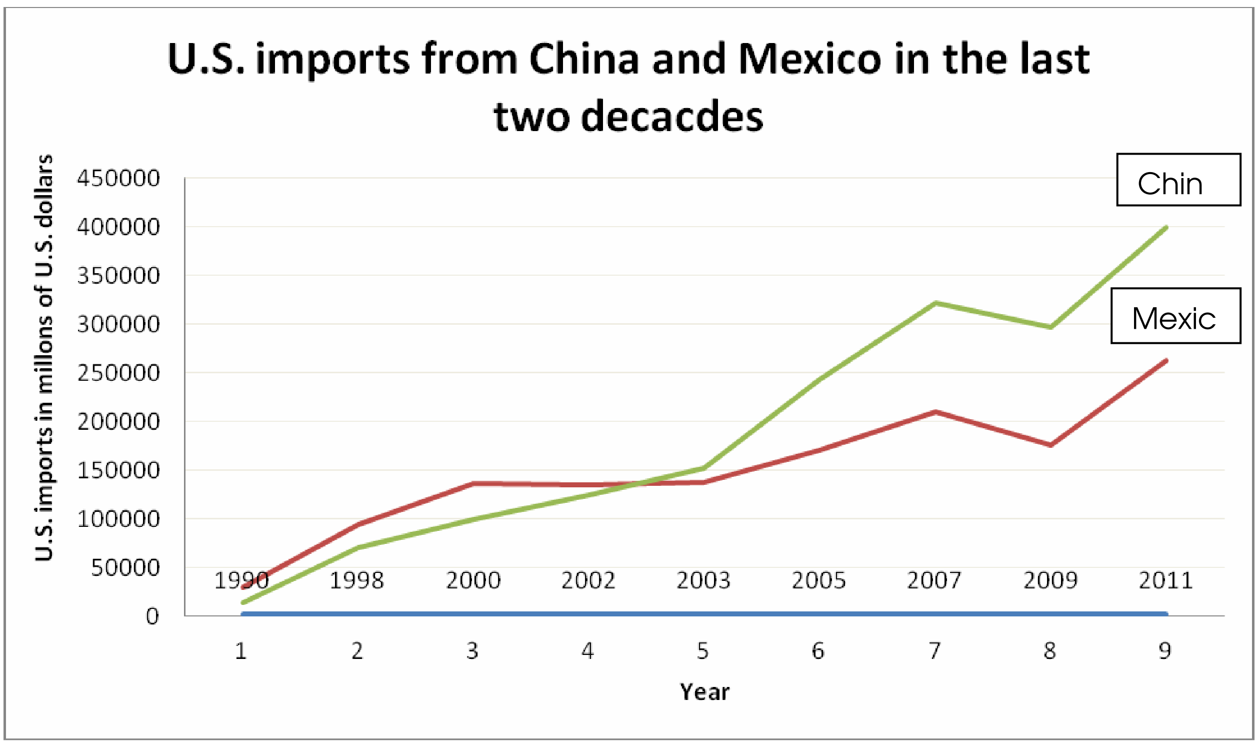
Nevertheless, there is evidence that China has also targeted high technology sectors such as the auto parts production, and has seen a profitable opportunity that they are rapidly developing.

Mexico has found few ways were they can still be ahead of China in their exports. However, "the rapid increase in Chinese exports to the US, the stagnation and/or fall in Mexican exports to the US in several of these same sectors, the loss of close to 300,000 maquila jobs from late 2000 to December, 2003, reports of widespread enterprise migration from Mexico to China, and a growing number of studies from agencies such as the World Bank and the Inter-American Development Bank provide clear evidence China represents a direct threat to Mexico."[51] Therefore in order to be successful, Mexico and other countries should focus on sectors where they do not face Chinese competition directly.

The next graph shows a comparison in the growth rate of the U.S. imports from China and México in the last two decades. Mexico's export share to the U.S. is shown in red while China is represented in green. The United Census Bureau website provides yearly information of U.S imports from every country in the world among other information. In the graph we can see that from the 1990 to 2001 there is a noticeable difference between the two trends. In the year 2002 the U.S. imported 134,600 million dollars worth of goods from Mexico and 125,100 million dollars worth of goods from China. By the next year in 2003 China would surpass Mexico while exporting 152,400 million dollars and México 138,000 million dollars worth of exports to the U.S. only. The graph shows when the two trends merge for a few months and then the Chinese trend spikes upwardly while the Mexican trend keeps growing but at an evident lower rate. The next graph also shows that by the end of the year 2011 the Chinese exports to the

[51] Sargent, 23

U.S were 399,000 million dollars while the Mexican exports were 263,000 million dollars. China's exporting rate as of 2011 is one third higher compared to the one from Mexico.



It is astonishing the way China is substituting for Mexico in the U.S. market. We have examine different policies that the Mexican government should impose with the manufacturing and transportation sectors. On the other hand there other sectors where the Mexican government can find a way to improve its situation, perhaps in the agricultural sector.

Agriculture under NAFTA and proposals for reform

Among these countries agriculture has been a controversial theme and has affected people particularly in Mexico. Mexico has the advantage of being able to produce off-season fruits and vegetables and have profitable market selling them to North America when they are not able to produces these goods. The U.S. also has a vast agricultural sector. Corn is a good example to demonstrate the emergence of a successful American product taking over the Mexican domestic production. For geographical and technological issues, the U.S. is able to produce at least two thirds or more corn than Mexican producers. After NAFTA was established the high production of corn in the U.S. quickly swamped the Mexican markets. This caused a drop of more than “25 percent” in the Mexican agricultural sector, an average of “two million people” left the corn fields."[52] The little agriculture that remained in the production of corn experienced high competitively against the U.S imports and a larger supply of fruits and vegetables in the Mexican market, hence a drop in prices of more than fifty percent. As a chain reaction this situation caused agricultures to migrate looking for seasonal jobs in the U.S. or permanent jobs in other states of Mexico.

It is vital that both governments come together to solve this problem because people have not been finding jobs and poverty remains high. Mexico has experienced an increasing food dependency on cheap U.S. foods. It should be unacceptable for a developing country such as Mexico to be dependent upon other countries on their food supply; this is supposed to be one of the country's stronger sectors of the economy where it should be exporting rather than importing food. If Mexico finds itself importing food, not being successful in its manufacturing sector, not creating jobs, with a deficient domestic investment policy, and more issues mentioned previously, México will struggle in the upcoming decades. The three NAFTA countries should find a way in which they regulate their exportations between one another in a way that they do not harm each others' sectors. NAFTA should be an instrument that helps the three economies develop and not a system that destroys them.

There are several ways the Mexican government can help develop and at a certain level protect its agricultural sector. In order to achieve these changes there has to

[52] Wise, 35

be political motivation and the government's desire to execute adjustments. First of all the U.S. can "expand its own government support for smallholders, since subsided are not restricted under NAFTA and Mexico's current support levels remain billions of dollars below the county's allowable limits under NAFTA."[53] Secondly, utilize its involvement in the "Cartagena protocol on Biosafety" to restrict imports from the United States because many of them are genetically modified and "Cartagena recognizes the precautionary principal".[54] This issue is of high importance because genetically affecting products violates NAFTA's environmental regime. Thirdly justify protective tariffs to shield part of the agricultural sector in México specially the production of corn and beans. In this theme México can bring the issue of constant illegal migration of Mexicans to the U.S. prompt by the loose of jobs in the agricultural sector.

To implement changes in the NAFTA reforms the Mexican government should also relay on organizations such as the Doha Development Agenda (DDA) which is the current trade negotiation round of the WTO. Under the DDA, countries are allowed to implement policies to protect the asymmetries in development between trading partners. One of the policies is to establish goods under the "special group category within NAFTA , with clear and agreed criteria for its use consistent with emerging

[53] Wise, 37
[54] Wise, 38

WTO Disciplines." [55] This would by itself concentrate on many issues over the shocks of NAFTA in the agricultural sector. Currently there was a proposal aimed at developing countries to declare up to 12 percent of tariff on agricultural products that would fall under the special product criteria. Many of the Mexican agricultural products especially corn and beans fall into this criteria, but until 2010 the Mexican government had not petitioned the WTO for the special products status of its corn and beans production.

In addition of the propositions that the Mexican government could petition for, they could also relay upon the North American Development Bank (NADBANK) for public investment. The NADBANK involvement with Mexico has not been advantageous nor helpful. Mexican "researchers have shown that Mexico could more than double the country's maize production using existing technologies if there were public investment in communications, infrastructure, irrigation, credit and agricultural extension."[56] Therefore it is critical that Mexico increases its public investment to help grow the agriculture sector.

On the other hand increasing investment on the corn production, Mexico can counter the negative agricultural impact that NAFTA has brought by entering a new international coffee agreement. NAFTA forbids Mexico from exporting its coffee to other parts of the world. Such measurements should not exist when North America is

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[55] Wise, 38
[56] Wise, 39

the only one benefiting from the corn exportation to Mexico for instance. As mentioned before NAFTA should be used to help develop all three economies and by restricting Mexico's exportation of coffee Mexico is not developing its coffee sector and its corn sector is ruined by it so-called trading partner.

Due to this unbalanced trade, there have been social and economic consequences that have to be addressed. Mexico joined NAFTA with a lack of preparation on its technology and transportation infrastructures. Therefore it is hard for México to compete against North America's production nowadays and day by day it is harder to close the gap with the other North American economies. If these issues were not addressed before the implementation of NAFTA they should be addressed now.

What should the three NAFTA countries do?

First and foremost, in order to face the challenges that the three NAFTA counties are encountering, regional representatives have to get together to work on renewal reforms for NAFTA. The equal cooperation among the countries is of great importance, as it was since the establishment of the treaty. It is imperative to begin working on a framework that strengthens the integration of the regions economically, socially and ideologically for the same purpose. Secondly they should address their challenges facing each country's priority sectors. For instance, from the Mexican standpoint, there are issues with agriculture, energy, transportation, migration, automobile industry and the financial and banking sectors, among others. Lastly they should concentrate on ways to enhance commerce and trade among the three countries to get the most profits out of it. They should attempt to increase trade amongst themselves and find ways to invest in each other's economies rather than looking to settle business overseas. This is an effort to reduce the competiveness vis a vis other countries that might offer tempting business opportunities to the NAFTA countries. Currently the three countries face similar situations with Asia and in particular with China. Not only in respect of increasing Chinese trade and investment, but also in regard of the substantial current account deficit. Therefore the NAFTA countries should structure reforms that constitute a new relationship with Asia.

One of the main weak points of NAFTA has been the lack of financing to develop. There is a financial institution that was establish in 1994 called North American Development Bank (NADB) governed equally by the United States and Mexico for the purpose of financing regional projects. This institution still exists but its command and thrive has significantly reduced. These types of institutions raise initiatives such as supporting small and medium businesses, as well as the financing of technology, venture projects and research to improve development. Therefore both countries should bring more attention to NADB and ensure that it fulfills its duties.

Conclusion:

This paper has evaluated the economic development of Mexico since the late 1940s with a much larger focus in the last two decades when NAFAT was implemented. The evidence shows that even though NAFTA has not been a complete success, Mexico would have been a lot poorer without entering this treaty and Mexico would have not been an attractive country for FDI.

However, this analysis clearly shows that Mexico is not the undeniable winner of NAFTA, contrary to the general view of this treaty. Mexico on the one hand got FDI, increased trade, exports quadrupled but it certainly did not develop the economic growth that Mexico needed.

As mentioned before Mexico only grew at a rate of 1.6 percent per year during the NAFTA period, which is very low compared to the standards of other developing countries and even compared with its own economic growth. In previous years Mexico has had an increase of 6 percent in GDP almost four times of the current growth. More importantly, the economic growth is very slow by the standards Mexico needs for job creation. This is probably the most shocking result of NAFTA, even in manufacturing there were only a limited number of jobs created. Employment in "the manufacturing sector fell dramatically after the peso crisis, and remains stagnant as we enter the 21st century."[57]

In the agricultural sector the flood of grains and meets coming in from the United States cost over two million people to lose their jobs. The percentage of people in the informal sector increased by almost ten percent and the migration to the United States from Mexico doubled. FDI into Mexico indeed increased, but ironically the foreign companies came and eliminated many of their domestic counterparts and the government was not able to fix the imbalances. So while FDI increased, total investment in Mexico decreased, and it was only 17 percent of Mexico's GDP. While it has been argued that a country needs at least a total of 25 percent of GDP in total investment in order to grow. In contrast, other Asian countries are in the low 30s while China gets 40 percent of GDP total investment. Therefore the free trade agreements between the countries need to be fixed in order for them to be able to absorb the benefits of foreign investment and make the economy develop.

There are several reasons why NAFTA has not accomplished what was expected. First, the increasing domestic and foreign direct investments went directly towards the manufacturing sector, leaving the rest of the sectors out of funds to develop. Second, major bottlenecks to future growth were not addressed by the trade

[57] Ramirez (2003), 19

pact, notably transportation, education, energy, agriculture, manufacturing and the financial system. Mexico should also address the problem of social inequality. The gap between the poor and the rich has just widened and it does not seem like it will get better unless the government intervenes and fixes the sectors where people are losing jobs. Lastly Mexico should find a way to redistribute wealth among the population since the money is highly concentrated on the wealthy.

Some specific reforms that need to be changed in the treaty are the following. First, as mentioned before there should be an independent organization that balances out the disputes from foreign companies and governments. In the past Mexico has experienced that the rights of the foreign companies are elevated over the government's power and many take advantage of them, bringing governments to a tribunal at the World Bank that does not have much transparency and foreign companies end up suing them for millions of dollars.

Second, make foreign investment help the larger economy by joining together local and foreign companies where workers from both countries work alongside learning the technics. In this way local engineers can later expand their acquired knowledge to other local engineers and let the benefits spill over the rest of the economy. NAFTA does not allow this kind of learning, which does not let local engineers to spread the new technology and knowledge across the country.

Third, Mexico should not rely on foreign investment so heavily. It should encourage domestic investment and set restrictions for domestic investors to avoid capital outflow. They should form committees that investigate the competitiveness agenda of manufacturing in the NAFTA region compared to other places in the world. Committees that are able to decipher the most convenient procedure for the three countries. One example of this investigation can be whether or not to allow more companies such as Pemex to go private to allow them to develop on their own. On the other hand this committees should also create some restrictions or boundaries in case they allow companies like Pemex to go private, or in the case of current private companies such as Telmex to make sure they do not create monopolies that can harm the population and their basic needs.

Although this paper examines economic policies implemented in the past, it is of extreme importance to address the current challenge that Mexico is facing with NAFTA.

> *Mexico's exports were worth 31, 540 Million USD in March of 2012. Mexico is the biggest exporter in Latin America. Mexico's major exports are: manufactured goods, oil and oil products, silver, fruits, vegetables, coffee and cotton. Mexican trade is fully integrated with that of its North American partners: 82% of Mexican exports are with the United States.*[58]

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[58] Trading Economics. http://www.tradingeconomics.com/mexico/exports

The fact that the exports as a percent of GDP in Mexico comprise "26.6 %" of Mexico's total GDP as of 2009 is alarming. [59] More than four fifths of Mexican exports go to the United States only, and more than one forth of the Mexican economy is comprised by its exports. This is exactly the reason why it is imperative and urgent to address the problems that NFTA is facing. Otherwise, a large piece of wealth will be lost by Mexico and overtaken by China. Approximately 22 percent of Mexico's total GDP could be lost if Mexico and its NAFTA partners do not compromise and come to an agreement.

Moreover, as mentioned before, Mexico should stabilize its government, which will enhance production, and increase safety to attract FDI. Mexico should pursue an economic infrastructure with better highways and transportation that will benefit trade, making it easier to transport goods. In addition, as mentioned in the beginning of this thesis, Mexico must work alongside with its NAFTA counterparts to come to agreements that will benefit all three nations. For instance, the border control between the U.S. and Mexico must develop faster and more effective security checks . This will convey a more effective trade in less time from which both countries benefit. These are some of the situations that countries like Mexico should address as soon as possible before it is too late to shift to a new economic model of development. If Mexico fails to

[59] Global Finance. http://www.gfmag.com/gdp-data-country-reports/220-mexico-gdp-country-report.html#axzz1tfNeIlMb

tackle these issues soon enough, the country's political, social and economic situation will be in danger.

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