Lessons Learned from Other Blocs
The NAFTA Experience

First CAMIC Workshop
San Jose, Costa Rica
November 5-7, 2007

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Introduction
One of the main goals of international trade is to allow countries to produce and market those goods for which they have competitive and comparative advantages. The North American Free Trade Agreement (NAFTA), established in 1994 by Canada, the United States and Mexico, is an economic bloc that seeks free trade among its members. Since NAFTA’s implementation, agricultural tariffs and quotas have been gradually diminished. Today, almost all trade barriers have been eliminated, and it is expected that they will be completely lifted in 2008.

Agricultural trade among NAFTA members has grown at an extraordinary rate. According to Meilke et al. (2007), trade in the region grew at a compound annual rate of 7.8% from 1994 to 2004 and accounted for more than 39 billion dollars at the end of 2004. However, North American agriculture is characterized by a great dichotomy between the highly commercialized economies of progressive state-of-the-art production systems such as those found in Canada, the United States, and some regions of Mexico, and many small, often subsistence, non-commercial farmers struggling to meet their families’ needs (Jones et al., 2007). This represents a major challenge for an even economic development of the region.

In the development phase of CAFTA, this paper explores the accomplishments and challenges of NAFTA in order to address lessons learned from this agreement. This is accomplished mostly from a Mexico perspective.
Characteristics of NAFTA

Signed in 1993 by Presidents Mulroney (Canada), Bush (US), and Salinas (Mexico), NAFTA was implemented in January 1994. A schedule of tariff removal was set for products and commodities to be traded. Specifically for Mexico, sensitive commodities such as corn, dry beans, sugar and fluid milk were negotiated to be free traded beginning 2008.

In addition to removing trade barriers among its members, NAFTA offers a favorable environment for investment within the region. It guarantees that any member should receive equal treatment as domestic investors. In other words, each country member must grant foreign firms national treatment equal to that which domestic firms receive. Moreover, foreign firms are entitled to repatriate their capital and profits, as well as to a fair compensation in case of property compensation. Additionally, NAFTA offers a dispute settlement process in cases of evolving national antidumping and countervailing duty laws and sanitary and phytosanitary (SPS) regulations.

Although NAFTA strongly supports national treatment of foreign firms, some exceptions do apply. For example, the Mexican government had reserved the right to allow foreign investors to buy land. On the other hand, the Canadian financial system opted to remain eligible to discriminate non-Canadian credit applicants.

In the particular case of agriculture, NAFTA explicitly provides no intervention. In such way, domestic agricultural policies such as the Mexican support program, PROCAMPO; the US income and farm price programs, and the Canadian Marketing Boards for dairy, poultry and wheat, did not required modifications under NAFTA. In other words, NAFTA was established just as a free trade agreement with no policy harmonization component. In contrast, the European Union (EU) has an elaborate administrative and legislative structure that has been quite effective in harmonizing policy across its
member countries. The NAFTA countries, on the other hand, face a challenge to maximize their efficiency as a bloc since they do not count on supranational authorities or institutions to enforce conflict settlement among its members, as does the EU. While neither suggesting, nor advocating the EU structure as a strategy that NAFTA should follow, there are many opportunities for accomplishing positive institutional change within the framework of NAFTA (Knutson, 2007).

The evolution of NAFTA
Since NAFTA’s implementation in 1994, trade among the three members increased more than 100%. According to USDA (2007) data, prior to the implementation of this agreement, agricultural trade accounted for nearly 17 billion dollars. Today, agricultural trade accounts for more than 40 billion dollars in the region. Trade between the US and Canada is worth more than 22 billion dollars followed by trade between Mexico and the US, which accounts for more than 16 billion dollars. Agricultural trade between Mexico and Canada is small, it accounts for almost 1 billion dollars; however, it has been growing at a fast rate and it is expected to continue growing at an accelerated pace. Mexican agricultural trade with Canada grows at an average yearly rate of over 10%.

Trade between Canada and the United States is highly characterized by processed foods such as roasted cereals, animal feed (mainly pet food); and pastries, vegetable and fruit preparations, such as orange juice (Zahniser, 2007). The US exports to Canada have increased more than 100% since NAFTA’s inception. Today, agricultural exports account for more than 10 billion dollars annually. On the other hand, US imports from Canada increased more than 150% and total more than 12 billion dollars.

With respect to the agricultural trade between Mexico and its northern neighbors, domestic demand for each country seems to be complemented by the production of other NAFTA members. Mexico has been able to maximize fresh produce exports to the US and Canada where climate does not allow year-round production. On the other hand, Mexico has fulfilled its domestic grain demand through imports from the US and
Canada. Currently, Mexico´s agricultural trade with its NAFTA members accounts for more than 15 billion US dollars.

After NAFTA was established in 1994, Mexican agricultural trade increased 150%. Although Mexican exports to the United States account for more than 80% of the total international trade, exports to Canada are expected to increase at a faster pace in the near future. Mexican agrifood exports to Canada increased 35% last year from 672 million dollars to 906 million dollars, (World Trade Atlas, 2007). This year, Mexican exports to Canada are expected to increase in more than 10%.

Most of the Mexican agrifood exports to Canada are composed of fresh fruits, vegetables and nuts (Jones et al., 2007). This pattern is similar to the agricultural trade between Mexico and the European Union: it is low but is growing at an accelerated pace. Last year, Mexican agricultural exports to the EU grew almost 40%, reaching a total of 45 million dollars.

Today, an important goal for NAFTA farmers should be not to compete against each other, but to produce what foreign markets demands. NAFTA countries have benefited from trading not only in economic terms, but also in providing consumers access to products that would otherwise be impossible due to climate or economic constraints. For example, consumers that live in non-favorable climates for agriculture, such a those with long winters and cold temperatures, are able to fulfill their demand for agricultural products through imports. About 75% of Mexican agricultural exports to the United States relate to vegetables, fruits, and beer. On the other hand, Mexico has been able to fulfill its grain demand such as yellow corn, to sustain its growing livestock industry.

Mexico has been successful in expanding vegetable and fruit markets, since its weather allows the production of almost any type of fresh produce. Besides climate attributes, Mexico maintains an economic advantage in producing these commodities. Harvesting products such as strawberries, broccoli, avocados and green onions is labor intensive,
and the cost of labor is highly competitive in Mexico. Mexico grows fresh produce on around 4% of its agricultural land, and approximately 20% of the production is exported, Huang et al. (2007). Today, Mexico is the seventh fresh produce exporter of the world and the main supplier to the United States.

Mexico’s position in the global arena has been achieved through NAFTA and the sanitary and phytosanitary requirements necessary to incur into international markets. Mexican fresh produce exports to the US have almost quadrupled since 1990. Fruit exports to the US rose from around 200 million dollars in 1990 to more than 900 million dollars in 2006. At the same time, Mexican vegetable exports to the US increased from 775 million to 2.5 billion dollars (Huang et al., 2007).

On the other hand, according to Zahniser (2007), foreign direct investment (FDI) has increased significantly among the bloc members since NAFTA’s inception. Mexican FDI in the United States’ agrifood industry is around one US billion dollars while the US FDI in Mexico and Canada is around 3 billion dollars to each of these countries.

**The experience of NAFTA at a sector level**

At a sector level, NAFTA has produced mixed results. Some countries have increased their market share in foreign markets, while others have seen their share decreased. Kennedy et al. (2002) evaluated the evolution of certain sectors to assess winners and losers within NAFTA. The methodology used in this paper is simple but straightforward. It analyzes the market share growth for sensible sectors such as sugar, corn, beef, and wheat. The US sugar market share decreased 50 and 82% for Canada and Mexico, respectively. On the other hand, the Mexican market share in the US increased 35% and it is expected to continue increasing.

Another commodity that has experienced important changes is corn. The US has significantly increased its share in the Mexican market. Beef is another sector that has experienced structural changes. Prior to the BSE outbreak, Canada had increased its
market share in the US by 129%. Similarly, the US beef market share in Mexico had increased by almost 100%. All these market trends were reversed once the presence of BSE in the region was confirmed. What it used to be an example of market integration in North America, is now a segmented market afflicted by SPS issues with serious effect on industry competitiveness.

To assess competitiveness, observers often refer to changes in market share, exports, and profitability. But ultimately, the competitiveness of a nation’s product is rooted not in any single outward measure, but in the quantity and quality of the country’s productive resources (Dohlman et. al., 2003). In other words, a more appropriate discussion of competitiveness would center on specific industry groups within a nation and the factors that drive their success.

Advantages and disadvantages of NAFTA

NAFTA represents a market of 430 million consumers. Each of the member countries is ranked among the top economies of the world. Canada has more than 33 million consumers with a per capita income of 39,000 dollars; the US has more than 300 million consumers with per capita income of 44,000 dollars, and Mexico has more than 100 million consumers with a per capita income of over 8,000 dollars.

NAFTA has allowed its members to achieve a more dynamic and a faster economic growth. Zahniser (2007) argues that NAFTA agricultural trade supports around 270,000 jobs in the US. Similarly, according to the World Bank, Mexico’s global exports would be 25% lower and the FDI would be 40% lower without NAFTA. In addition, Mexico’s technological innovation has increased twice as fast after the implementation of the agreement.

NAFTA, as any other trade agreement, has implications for aggregate macroeconomic fluctuations, cycles, and growth. The more economic integration within the bloc, the more synchronized the development of the region. Mexico’s macroeconomic volatility
has changed after NAFTA. It has became more stable, but has a higher level of
dependence with the US and Canadian cycles. However, up to certain extent, this
behavior reduces risk and, thus, promotes investment. On the other hand, one of the
major disadvantages of NAFTA is that small producers are not able to achieve the
economies of scale as large domestic and international producers, resulting in rural
farm displacements. Krugman (1990) argued that neither industries nor countries, but
individual firms compete for both domestic and foreign markets. However, in order for
firms to compete successfully, they must present at least some competitive advantages;
either in cost and/or in the quality of their products.

A shortcoming of NAFTA is that there is no supranational authority that solves disputes
among members, and sometimes conflicts are solved unilaterally. Josling (1997) argues
that under this scenario, domestic groups can lead a country to change NAFTA
arrangements, at least during a particular period of time, instead of making internal or
domestic changes.

In addition, agricultural policy has not been able to be harmonized among its members.
Having different regulations among each country will make trade complex. Knutson and
Ochoa (2007) argue that policy convergence is a condition to efficiently solve trade
disputes, enhancing market integration. However, policy convergence requires close
and constant communication among policy makers in order for them to understand their
own and their counterparts’ policy goals.

What to focus on
Important strides have been achieved under NAFTA. However, further steps are
needed to achieve a greater level of integration. Up to this point, the NAFTA experience
has proven successful. However, a greater effort from the three member countries is
needed to solve the existing and future conditions. One of the cases where the NAFTA
mechanisms have been successful, it is preventing SPS issues to further extend into
the economic bloc. However, once these issues have been resolved, it has been
difficult to resume trade at the original levels. In other words, it has been easy to close the borders due to SPS incidents, but it has been difficult to re-establish trade once the issue has been resolved.

Protecting against animal and plant diseases is an issue on which governments have great concerns. However, in order to improve animal and food trade in the region, governments should work on developing programs at a regional level. That is, the health and food safety issues concerning one country must be an issue for the rest of the partners.

It is important for countries to develop common regulatory animal and plant programs. Otherwise, the presence of animal or plant health hazards becomes itself a sanitary frontier within the supposedly free trade zone. Similar to the BSE restrictions in Canada and the US, another example is the presence of Avian Influenza and Newcastle in poultry, or Swine Fever and Aujesky Disease in swine in some regions in Mexico. (Figures 1-4). This represents a sanitary frontier that impedes the movement of these products across not only within the country, but across the trading bloc.

Common regulatory programs such as inspection and traceability should be implemented along the entire region. In addition, there are other mechanisms that could foster trade within the region by adopting common sanitary and phytosanitary standards and measures (Jones et al., 2007). The Hazard Analysis and Critical Control Points (HACCP) system offers a number of advantages over the current system. Most importantly, it focuses on identifying and preventing hazards fromcontaminating food. In addition, it is based on science, permits more efficient and effective government oversight, and appropriately places responsibility for ensuring food safety on the food manufacturer and distributor. Finally, HACCP helps food companies more effectively compete in the world market, and it should be a scientific mechanism to reduce technical barriers to international trade.
Other important SPS issue is Traceback. The International Organization for Standardization (ISO) defines traceability as the “ability” to trace the history, application, or location of that which is under consideration. Firms determine the necessary breath, depth and precision of their traceability systems depending on three objectives: 1) improve supply management; 2) facilitate traceback for food safety and quality; and 3) differentiate and market foods with subtle or undetectable quality attributes (Golan et. Al, 2004). In the food industry where margins are thin, supply management, including traceability, is an increasing area of competition. A firm’s traceability system is key to finding the most efficient ways to produce, assemble, warehouse and distribute products. Golan et. al (2000) conclude that labeling might be an appropriate policy tool in the following circumstances: 1) Consumer’s preferences differ; 2) information is clear and concise; 3) information on product use enhances efficiency; 4) costs and benefits of consumption are borne by the consumer; 5) standards, testing, certification and enforcement services can be established; and 6) no political consensus on regulation exists.

Grades and standards are important issues in securing and maintaining trade flows. In the area of food safety and quality, the program commonly referred to as Agrifood Armor emphasized the establishment of a quality certification program for agrifood products (“Inspección de calidad agropecuaria”). This voluntary program is intended to minimize disputes among buyers and sellers and to ensure that the sales price reflects the quality of the product.

NAFTA-wide risk assessment laboratories should be of common interest for the NAFTA member countries. The region’s security must be seen as a common interest and priority. Domestic security will hardly be accomplished if regional security is not achieved. Animal, plant health, food safety, control and diagnosis of diseases must be addressed and treated as a regional bloc.

Investment in education and outreach should be a priority under NAFTA. Assuring the next generation of science power and knowledge for regional agricultural security will be
achieved only by investing in education. However, this effort must be carried out through regional educational programs developed by NAFTA members and according to the needs of the bloc.

**Closer coordination issues**

It is fundamental to promote common technical and scientific regulatory mechanisms across the NAFTA countries. Active collaboration on programs related to surveillance, testing and tracing disease and pest issues that affect production in each of the NAFTA countries must be commonly addressed. The development and application of common SPS standards for animal and plant products should be a priority.

Finally, uniformity in policy analysis is crucial to develop a common ground to proactively address the current and future issues and disputes. The creation of common analytical models would allow the decision-makers to understand the implications of their policy decisions across the entire bloc.

**Conclusions**

The underlying objective of free trade agreements is to allow products and services to flow under the same terms and conditions across countries as it is within each country. Despite its shortcomings, NAFTA has proven positive for economic development through enhanced trade in North America.

One of the main lessons from NAFTA is that benefits are maximized when countries produce and trade the commodities for which they have competitive and comparative advantages. By specializing in products where the countries have a competitive advantage, producers’ income may increase and the economic asymmetries across countries should be diminished.

There may exist asymmetries on the legal and political level that make trade inefficient. It has been proven that regulations are very efficient in closing borders when sanitary
and phytosanitary issues arise. However, the re-establishment of trade flows has been proven much more difficult. Science-based decision should promote faster and more rational solutions to SPS issues. Regulations among members should be consistent.

A supranational institution should help in resolving disputes among the trading partners. It is recommended that there should be, at least, one official government representative in charge to voice and resolve multilateral issues. In addition, enhancing integration should go beyond politics and laws. Joint collaboration on scientific and technical research should be promoted.

Finally, countries should not wait until the last minute to start making changes and adapting to the new trade environment. Similar to the tariff elimination, it is necessary to establish and closely follow a sector adjustment program. This program should not only include measures to adapt those subsectors that are going to be able to compete in a more open environment, but to provide some remedy for those subsectors and players, such as small producers and firms that, because of their inability to reach economies of scale, will hardly be able to endure the new trading environment.
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Figure 1. Swine Fever Eradication Program

Figure 2. Aujeszky Disease Eradication Program

Figure 3. Avian Influenza Eradication Program

Figure 4. Newcastle Eradication Program