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NAFTA: Its economic, social and political effects on U.S., Canada and Mexico

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ABSTRACT

After 20 years of its implementation, though the North American Free Trade Agreement (NAFTA) has helped to boost intraregional trade between Canada, Mexico, and the United States, but somewhere has fallen short of generating the desired amount of jobs and the deeper regional economic integration. Although with NAFTA, trade relations among these countries have broadened substantially with U.S. manufacturers creating supply chains across North America, that have not only made the companies more competitive globally but have also contributed in their respective GDP's. NAFTA has helped in stimulating the economic growth; where data show that Canada has expanded at fastest average rate and Mexico at the slowest, but economists still debate NAFTA's direct impact, given the many other economic forces at play and the possibility that trade liberalization might have happened even without the agreement. Thus, in this paper we will try to examine the social, economic and political impact of NAFTA on these three countries.

INTRODUCTION

NAFTA *i.e.* the North American Free Trade Agreement is a comprehensive agreement which sets the rules for international trade and investment between USA, Canada and Mexico. This agreement came into force in 1994 and includes eight sections, 22 chapters, and some 2,000 pages and is overseen by a number of institutions that ensure the proper interpretation and smooth implementation of the agreement's provisions. This agreement not only eliminates the tariff and non-tariff barriers to trade and investment between USA, Canada and Mexico but has also helped in creating stability and confidence for long term investment among these countries. Along with the withdrawal of import tariffs in several industries (like textiles and automobiles), agriculture was also a major focus of NAFTA. NAFTA also implemented intellectual-property protections and has established dispute-resolution mechanisms among NAFTA countries but along with all this, these three countries has also signed two side agreements: The North American Agreement on Environmental Co-operation (NAAEC) and the North American Agreement on Labour Co-operation (NAALC); where under NAAEC, USA, Canada and Mexico have committed to take certain steps to protect the environment and to work co-operatively to address regional environmental concerns, to help prevent potential trade and environmental conflicts, and to promote the effective enforcement of environmental law, among other things. However under NAALC, the three countries have agreed to co-operate on labour matters comprising of occupational safety and health, employment and job training, labour law, and workers' rights and productivity. NAFTA mainly focuses on the withdrawal of tariffs on the imported goods, *i.e.*, each NAFTA country forgoes tariffs on the imported goods from the other NAFTA country; but its rules of origin enables the custom officials to decide about the goods qualifying for the preferential treatment under NAFTA. These rules of origin have already been made very clear to the NAFTA countries so as to provide certainty and predictability to the producers, exporters and importers of the NAFTA countries.

The problem statement :

NAFTA is one of the biggest agreements for North America to streamline business between USA, Canada and Mexico. However, there are many factors like unions, labor laws, market access and government rules etc., which influence the successful implementation of this agreement. The purpose of this study is to identify factors affecting the success ofNAFTA on these countries and to see the social, economic and political affect of NAFTA on these three countries and its people.

Hypothesis :

– H_0 : NAFTA improve the three countries economy.
– H_1 : NAFTA not improve the three countries economy.

Research questions :

What is NAFTA? :

NAFTA is a trilateral agreement, which came into force on 1st January, among USA, Canada and Mexico to promote free flow of goods and services among them. The agreement has swept away many tariff and non-tariff barriers on the trade of products of several industries and has implemented intellectual property protection, dispute resolution mechanism, environmental protection and labour market co-operation among NAFTA countries.

Why is this agreement is not popular in the US and Canada?:

Because of regional liberalization and unions, both of them have harmed the trading system. The difference in the union type of both the countries explains a significant part of the variation in the levels of union activism against NAFTA in both countries, as well as differences in strategies of opposition. Furthermore, the regional differences also pose a type of hurdle for instance, for Eastern Canada, NAFTA led to large decreases in trade with the United States, Mexico, Asia, and Europe. For Central Canada, NAFTA led to large increases in trade with the rest of North America, and to a large decrease in exports to Europe. For Western Canada, NAFTA had no effect on total trade with the United States, but it did lead to large increases in trade with Mexico, and to decreases in trade with Europe and Asia. For U.S. regions, the increases in trade were spread fairly widely, with the Rocky mountain and Far West regions as exceptions.

What are the political, economic, and social impacts of the agreement? :

The North American Free Trade Agreement (NAFTA) has revolutionized trade and investment in not only North America but also in Canada and Mexico and helped these countries to unlock their region's economic potentials. NAFTA has various economic, social and political effects on these countries. There have also been various myths about NAFTA but the real fact is that NAFTA has actually helped these countries economically, socially and politically. Since it came into effect 15 years ago, all the NAFTA countries and especially North America have enjoyed an overall extended period of strong economic growth and rising prosperity.

NAFTA has not only helped in stimulating the economic growth but has also helped in creating higher-paying jobs across NAFTA countries. This agreement has actually increased the labour standards, living standards and manufacturing base (output) of all NAFTA countries and has also paved the way for greater market competition with enhanced choice and purchasing power for its consumers, families, farmers, and businesses.

Furthermore, with less government interference, NAFTA has provided North American businesses with better access to materials, technologies, investment capital, and talent available across North America, which has actually helped in making its businesses more competitive. NAFTA has proven that trade liberalization plays an important role in promoting transparency, economic growth, and legal certainty. For this, at the 2009 North American Leaders' Summit, these three countries have also agreed to "reiterate our commitment to reinvigorate our trading relationship and to ensure that the benefits of our economic relationship are widely shared and sustainable".

Some of the facts of this agreement :

Since NAFTA came into effect, merchandise trade among the NAFTA partners has more than tripled, reaching US$946.1 billion in 2008. Over that period, Canada-U.S. trade has nearly tripled, while trade between Mexico and the U.S. has more than quadrupled [C$ figure = $1.0 trillion].

Since NAFTA came into effect, the North American economy has more than doubled in size. The combined gross domestic product (GDP) for Canada, the United States, and Mexico surpassed US$17 trillion in 2008, up from US$7.6 trillion in 1993 [C$ figures = $18.2 trillion and $9.8 trillion].

In 2008, Canada and the United States' inward foreign direct investment stocks from NAFTA partner countries reached US$469.8 billion. Meanwhile, Mexico has become one of the largest recipients of foreign direct investment among emerging markets, and received US$156 billion from its NAFTA partners between 1993 and 2008.

North American employment levels have climbed nearly 23% since 1993, representing a net gain of 39.7 million jobs.

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Today, the NAFTA partners exchange about US$2.6 billion in merchandise on a daily basis with each other. That's about US$108 million per hour [C$ figures = $2.8 billion and $115 million].

Theoretical framework or model :

For this research I will be using the theory of economic growth and will show how this agreement has helped in improving the economic growth of NAFTA countries. But before doing so, let us first know about the theory of economic growth in nutshell.

By economic growth we mean the persistent increase in the gross domestic product of a nation *i.e.*, long term expansion of the production potential of the economy. The main determinants of the economic growth are growth in the physical capital stock and human capital, growth in the labour force engaged in production, technological progress, macroeconomic stability, rising demand of goods and services produced in the economy etc. However, changes in the real exchange rates, cyclical fluctuation in national output and external trade, volatility in world prices, political instability, military conflicts, natural disasters, supply shocks and unexpected breakthrough in the state of technology may create a treat or challenge for the economic growth of an economy.

There are several growth models given by several economists in the past like Harrod Domar growth model, Solow model, Endogeneous growth theories etc. which basically shows how growth is related with some of the macro variables of the economy and how it affects the desired section of the economy.

In this paper I will also try to show through the economic growth model, how NAFTA has affected the economic growth of these three countries, using the data of national output, GDP, employment etc.

Past history and evolution NAFTA :

Prior to NAFTA, U.S and Canada has already signed a free trade agreement on October 3, 1987 which was reformed again on 1st January 1989 and eliminates all tariffs by 1998 and liberalized all financial service along with many other provisions. But while Canada and the U.S. were forging their "Free trade agreement", Mexico was planning to approach the international trade with them. The reform by Mexico was basically motivated by the oil price collapse and foreign debt crisis that Mexico experienced in the early 1980's. As a result of these crises and internal economic melancholy, the Mexican government joined the General Agreement on Tariffs and Trade (GATT) in 1986 to reduce trade barriers and comply with international trade standards during the administration of Mexican President, Miguel de la Madrid Hurtado. This orientation, along with the programme of economic reforms instituted by President Madrid's successor, Carlos Salinas de Gortari, reforms are named as "Salinastroika" and has made Mexico ready to join Canada and the U.S. in establishing a trade agreement. Then, on August 12, 1992, Canada, Mexico, and the United States announced their intention to create a free trade zone - the North American Free Trade Agreement and came up with NAFTA in 1993 and made it the largest trilateral trade agreement/relationship in the world.

Present – current – challenges :

NAFTA joined a big Third World country to the U.S. at a time when many Americans were losing their jobs and factories were heading south of the border. This economic destitution and affiliated anxiety by NAFTA created a feeling among some people about U.S. losing control over its economic destiny. At the same time, companies that have been forced to spend millions on cleanup by U.S. environmental rules started worrying about competing with Mexico, with its hit or miss environmental regulations." All of these uncertainties, coupled with defense downsizing and economic restructuring accompanying the end of the cold war, exacerbate such potential economic hardships as worker displacement, the loss of jobs, the elimination of entire industries, as well as the environmental differences between the countries.

– "Free markets and price stability: Opportunities in Mexico," Economic Commentary, Federal Reserve Bank of Cleveland, August 1, 1993, p.1.
– The term, "Salinastroika," was used by Mexican managers in conversation with the author while he was lecturing in Mexico at Universidad Popular Autonoma del Estado De Puebla in December 1992. It was used to refer to the economic reforms and openness instituted by Mexican President Salinas.
– "White House Walks the NAFTA Tightrope." *Wall Street Journal*, March 15, 1993, p. 1

Future - trends in addressing these issues :

NAFTA has been successful in addressing these issues and been able to impact NAFTA countries. With two side agreements, it has been able to stimulate investment, employment, wages, trade, stability and growth in these countries along with taking care of the environmental issues and labour laws. The trends of the same will be discussed in the later chapters of this research.

However, as far as the future of NAFTA is concerned then it has been proposed by many economists that NAFTA needs to have some changes including investing in border infrastructure, enhancing regulatory co-operation, strengthening protections for workers and the environment and promoting research and development to improve the competitiveness of North American industries, which in the recent past it has complied a bit too. Moreover, since trade remains a divisive issue in these countries, therefore new potential trade agreements, such as the Trans-Pacific Partnership (TPP)—which comprises Australia, Brunei, Canada, Chile, Malaysia, Mexico, New Zealand, Peru, Singapore, Japan, the United States, and Vietnam—are introduced which will not only bring in a set of rules that will go beyond NAFTA but will also deliver the reforms that regional negotiations haven't reached yet. Proposed TPP provisions on stronger intellectual property rights, labour and the environment, and constraints on state-owned enterprises, if agreed upon, will definitely effectively update the trade relations without reopening the treaty.

Annotated bibliography :

In the past several economists have done research on NAFTA and its counter effects. Some of them say that NAFTA has actually proved a boon for these countries whereas there are some economists who are against this view. For instance, the paper "Effect of NAFTA on US employment and policy responses" by Christopher J. O'Leary, Randall W. Eberts, and Brian M. Pittelko (2011) says that the elimination of tariffs under NAFTA has increased the volume of exports and imports between North American countries, where the consumers, producers and businesses all have gained due to the trade expansion and lowered prices. However, the transition after further trade expansion has also involved short-term adjustment costs for selected groups, affecting both employment opportunities and wage levels of some American workers. As a result, specific public policies emerged in order to address these adjustment problems and facilitate transition. This paper has focused specifically on Trade Adjustment Assistance, Self-employment Assistance and other supporting policies and showed that Trade Adjustment Assistance provided substantial income replacement to NAFTA displaced workers. However, this research also suggests that TAA retraining and re-employment assistance did not appreciably increase employment among trade impacted workers; but Self-Employment Assistance had positive effects on employment; thereby increasing the potential benefits of the geographic coverage of this measure. The authors of this paper have provided enough background on the political debate in the United States at the time of the signing of NAFTA and have outlined the dynamics of trade and employment among the NAFTA partners over the last 20 years. Then they had summarized the estimates of NAFTA's employment impact, both shortly before its implementation and afterwards and provided an overview and assessment of US employment policy responses aimed at facilitating labour-market adjustment and support of trade-displaced workers.

Romalis (2005) in his paper "NAFTA's and CUSFTA's impact on international trade" has conducted a partial equilibrium econometric analysis of demand for traded goods (at the 6-digit industry level relying on North American Industrial Classification System (NAICS) data). He provided many evidences that the reduction of tariffs under NAFTA increased Mexico's share of US imports. He found out that only a small percentage of NAICS 6-digit commodity groups had an increase in US tariff preference for Mexican goods from 1993: 389 had an increase in tariff preference (relatively lower tariffs) whereas 2 663 had no change. He also revealed that prior to NAFTA Mexico significantly liberalized its trade regime by reducing tariffs on an MFN basis and eliminated quantitative restrictions on imports. In 1965, Canada and the United States negotiated the Auto-Pact, which allowed them for duty-free trade in many automotive goods; therefore, the enactment of NAFTA did not reduce tariffs significantly for many commodities. Romalis (2005) further states that imports are sensitive to tariff reductions, and are measured by tariff preference, thus later in his study he found that for the 389 commodities for which the US tariff preference for Mexican goods had increased by at least 10 percentage points, the simple average of Mexico's share of US imports actually rose by 224 per cent between 1989 and 2000. On the other hand, for the 2 663 commodities for which Mexico's tariff preference remained unchanged, their share rose by only 23 per cent. He further found a similar response for Canada. Those commodities with at least a 10 percentage point increase in tariff preference increased their UI import share by 99 per cent; those with no change in tariff preference showed a slight decrease in share. Thus, his study concluded that the net US import increases from NAFTA partners at the expense of imports from the EU, even though Canada and the United States are high-cost producers of many of these commodities.

Agama and McDaniel (2002), in their paper "The NAFTA preference and U.S.-Mexico trade" examined whether other factors could baffle the response of trade to tariff reductions. They used an econometric model to estimate the separate effects of various other factors, including GDP and tariff changes prior to NAFTA and found that an increase in tariff preferences increases trade. Mathematically his study showed that on average, a one percentage point increase in the tariff preference corresponds to somewhere between an 11.2 per cent and 16.5 per cent increase in US import demand for Mexican goods. However, on the export side, a one percentage point increase in the NAFTA tariff preference corresponds to an increase in Mexico's demand for US goods of between 5.1 per cent and 6.7 per cent. Furthermore, an important issue addressed by Agama and McDaniel (2002) study is the effect of more permanent tariff reductions offered by NAFTA versus the more temporary ones put in place before NAFTA was implemented and their results suggest that the responsiveness of tariff preferences were larger during the period in which NAFTA was in effect than beforehand. Thus, their study shows the permanency of NAFTA trade liberalization had a positive effect on trade.

The above stated studies suggest that NAFTA affected the level and pattern of trade between the United States and Canada & Mexico, where significant increases in tariff preferences *i.e.*, relative reductions in tariffs, were associated with increased shares of US imports. Furthermore, since changes in tariff preferences differed across commodities, the expectation was that NAFTA would affect the import shares of different commodities differently, leading to a reallocation across industry sectors. These studies also shed some light on the different responses between Mexico and Canada to these tariff changes. For instance, Mexico appeared to be more sensitive to an increase in tariff preference than Canada—a 224 per cent increase for Mexico versus a 99 per cent increase for Canada. Moreover, these studies shed some light on some factors other than tariff preferences that affect import penetration, and Mexico's exports to the United States appear to be more sensitive to these factors than do Canada's exports. This difference is evident in the commodities with no change in tariff preference, as Mexico's share of US imports increased by 24 per cent whereas Canada's share did not increase.

Feenstra and Hanson (1997), in their paper "Foreign direct investment and relative wages: evidence from Mexico's maquiladoras" found that in Mexico labour demand by incoming foreign firms is skewed towards skilled workers. Another study found that the level of protection is in fact correlated with the labour-intensity of a sector (Hanson and Harrison, 1999). This implies that trade liberalization would disproportionally affect less skilled workers, who were previously enjoying the benefits of tariff protection.

Hanson (2003) has examined, in his paper "What has happened to the wages in Mexico since NAFTA", the impacts of trade and investment liberalization on the wage structure of Mexico. One part of this paper examined the Mexico's policy reforms which have raised the demand for skill in the country, reduced rents in industries that prior to reform paid their workers high wages, and raised the premium paid to workers in states along the U.S. border and have resulted in an increase in wage dispersion in the country. The second part of the paper examines the changes in Mexico's wage structure during the 1990's and concluded that in the last decade, Mexico has experienced rising returns to skill labour, like the wage movements in the United States, though there is little evidence of wage convergence between the two countries. Furthermore, this paper has also explained the regional wage differentials in Mexico that have widened and is explained largely by variation in regional access to foreign trade and investment and in regional opportunities for migration to the United States. Lastly the paper ends with the discussion of the implications of Mexico's experience for the rest of Latin America in the event a Free Trade Agreement of the Americas is enacted.

Wall (2002) in his paper "NAFTA and the geography of North American trade", has demonstrated that at the regional level the effects of NAFTA have been much more complicated than what normally should happen. This paper concluded that NAFTA just meant three things; (i) less trade between Eastern Canada and the United States and Mexico, (ii) more trade between Central Canada and the United States and Mexico, and (iii) more trade between Western Canada and Mexico, but no change in the volume of trade between Western Canada and the United States. The author also found out that NAFTA has decreased trade between Canadian regions and both Europe and Asia, while increasing Mexico's trade with Asia.

Krueger (1999) in her paper "Trade creation and trade diversion under NAFTA" has used the Aggregate and more micro data on trade between the U.S., Canada, and Mexico to assess the early effects of Mexican entry into NAFTA and found that although the fraction of Mexican trade with the U.S. and Canada has risen sharply, but this is because of a number of other factors like Mexican reduction of tariffs and quantitative restrictions and the Mexican alteration of exchange rate policy at the end of l994. Thus for her, the impact of NAFTA over its first three year does not appear to have been large relative to the effects of these other events.

Another research by Rock-Antoine Mehanna and Hannaraong Shamsub (2002) titled who is benefiting the most from NAFTA? An intervention time series analysis has examined the forecasted trade values and investigates the impact of NAFTA on both bilateral trade and income of each NAFTA country by using historical data. This paper has covered time series data before and after NAFTA was formed, from 1980 to 1999 and considered NAFTA as a prolonged impulse function in international trade activities among the three trading partners by employing an intervention-function model. The paper findings revealed that NAFTA increases bilateral trade between US-Canada and US-Mexico, and in terms of income, NAFTA benefits mostly to Canada. To substantiate these findings, this paper has employed Granger causality analysis, which in turn has supported their intervention-function results. Thus, keeping in view the viewpoint of the other economist's researches, this paper will analyze the economic, social and political effect on NAFTA on the NAFTA countries using the relevant data.

MATERIAL AND METHODS

Population, data sources and analysis techniques :

The study pertains to the analysis of growth and trade trends of three NAFTA partners United States, Mexico and Canada, observed during the period 1993-2012. Secondary data were collected from the websites of the World Bank, IMF, NAFTA, U.S. International Trade Commission's Interactive Tariff and Trade Data, U.S. Bureau of the Census. Data, Bureau of Economic Analysis.

The analysis involves the comparison of data from the time NAFTA was implemented *i.e.* in 1994 to the current period

2012-2013, (latest available data) and how the countries have performed in terms of growth rates, trade trends and employment.

OBSERVATIONS AND ANALYSIS

NAFTA in 1994 opened up the North American economies of Mexico, Canada and the US to each other catering to the market of 400 million people and accounting for one-third of the world's output of more than $1 trillion per year. One of the major objectives of NAFTA was promotion and safeguard of foreign direct investment between the partner countries and thus promoting employment through trade.

The major sectors covered by NAFTA are health-care management, engineering, construction, accounting, advertising, consulting, architecture, auto, commercial education, and tourism. The key NAFTA provisions were designed to promote tariff and non-tariff trade liberalization and also included were cultural exemption, transportation services and investment, rules of origin, services trade, foreign investment, intellectual property rights protection, government procurement, and dispute resolution, trade remedies, agricultural supply management etc. The trade and non-tariff trade liberalization provisions of the agreement required elimination of all tariffs and most non-tariff barriers on goods produced and traded between the three economies over a period of fifteen years after it entered into force in 1994. Some tariffs were eliminated immediately, while others were phased out in various phases of five to fifteen years. All tariffs and quotas were eliminated on U.S. exports to Canada and Mexico by January 1, 2008. All existing drawback programmes were terminated by January, 2001. NAFTA became the world's largest free trade area, linking 454 million people, 33.3 million of whom live in Canada, 304.1 million in the US, and 106.7 million in Mexico. Over $17.2 trillion worth of goods and services were produced in 2010.It provided the option of accelerating tariff reductions, speeding up the process of export product inspection and certification, also included were safeguard provisions for the domestic producers against increased imports from another NAFTA partner in which it increases tariffs, or imposes quotas in some cases, on imports during a transition period. NAFTA provided "national goods" status to products imported from other NAFTA countries. The state or the local governments could not impose taxes or tariffs on those goods. Separate NAFTA side agreements were prepared to take care of labour and environmental provisions. Under those agreements, the countries agreed to establish commissions who had the power to impose steep fines against any of the three governments that failed to impose its laws consistently.

Trade between US and Canada was already duty free under the provisions of CUFTA. Thus, most of the market opening measures resulted in the elimination of US trade barriers applied to imports from Mexico, and Mexican tariffs and quotas applied to imports from the United States and Canada. At the time that NAFTA went into effect, about 40 per cent of US imports from Mexico became duty-free and the remainder faced duties of up to 35 per cent. The agreement also included opening the US Mexico border and interior of Mexico to US truckers and streamlining border processing and licensing requirement.

In 2012, Canada was the largest US trade partner and Mexico was ranked third. They both together accounted for 32 per cent and 26 per cent of US exports and imports, respectively. US accounted for 74.5 per cent and 78 per cent of Canadian and Mexican trade, respectively. Between 1993 and 2012, US trade with Canada increased by 192 per cent while with Mexico it increased by 506 per cent (Table 1).

In 1993, trade within the NAFTA region as measured in terms of a country's import from other partners was over US $285 billion while in 2012 it passed the $1 trillion mark. The North American economy has more than doubled in size since 1994, reflecting the prosperity and development of the region. The combined gross domestic product (GDP) for Canada, the U.S., and Mexico was US$19.2 trillion in 2012 up from US$7.7 trillion in 1993. US's export to Mexico increased from $41.6 billion in 1993 to $216.3 billion in 2012 and US imports from Mexico increased by 596 per cent over the same period. In 1994 US was a running a merchandise trade surplus of 1,349.8$ million whereas by 2013 it was - 54,302.6$ million. US export of services to Mexico increased by 142 per cent and services imports from Mexico increased by 85 per cent during the period 1993-2012.

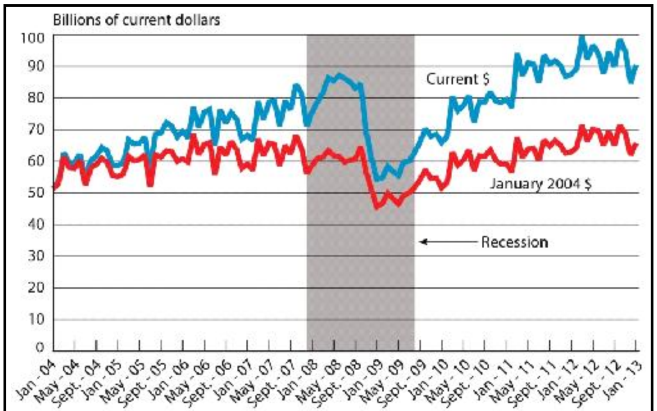
Approximately 75.7 per cent of Canada's total merchandise exports were destined to NAFTA partners in 2012. Total trade in goods between Canada and the US more than doubled between 1993 and 2012. Canada was the main destination for US goods exports in 2012, second largest source of merchandise imports into the United States and largest market for US service export. US exports to Canada increased from $100 billion in 1993 to $292 billion in 2012. Canada's goods exports to the US

Table 1 : Total merchandise trade between NAFTA countries during 2008-2012

Flow	2008	2009	2010	2011	2012
Exports	1012507	767892	956683	1102276	1150722
Imports	965464	717481	899595	1034688	1078829

Source : The World Bank
Unit : US dollar at current prices.

grew at an annual rate of 4.4 per cent between 1993 and 2012. In 2012, total trade between the two nations amounted to 41 per cent of Canada's GDP. Mexico and Canada are the main foreign suppliers of energy to United States. Canada's merchandise trade with Mexico was around $31 billion in 2012. Between 1993 and 2012, Mexico-Canada merchandise trade grew seven folds to over $30 billion in 2012, growing at an average annual growth rate of over 10.6 per cent (Fig. 1).



Source : Bureau of transportation statistics

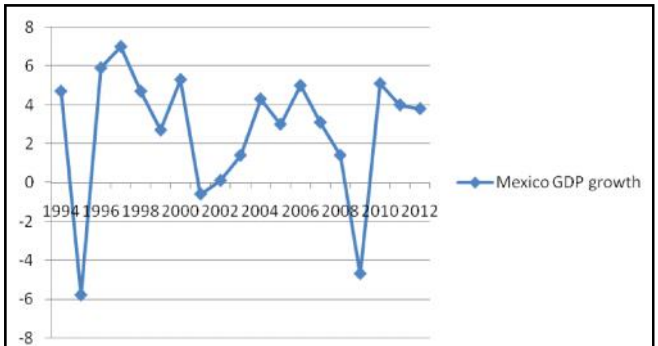
Fig. 1 : Trade between the US and NAFTA partners

Services trade between Canada-Mexico increased five times to $2.9 billion in 2011. In 2012, Mexico was Canada's third largest trade partner, third largest supplier and fifth largest export market for merchandise trade. One in five jobs in Canada is related to trade reflecting how the enhanced economic activity and production in the region have contributed to job creation. With the addition of more than 4.7 million net new jobs during the period from 1993-2014, Canada's unemployment rate decreased from 11.4 per cent (1993) to 7.2 per cent (2012).

Effect on Mexico :

Mexico's main motivation in entering a free trade agreement with Canada and United States was to stabilize the Mexican economy which was facing tough economic conditions during 80s and early 90s, thereby promoting economic development through increasing exports and job creation by attracting foreign direct investment. It was expected that NAFTA would help to improve investor confidence in Mexico, increase export diversification, create high skilled jobs, increase wage rates, and reduce poverty. Higher economic activity would help to narrow the income differentials between Mexico and the United States and Canada. A number of economic studies predicted and supported that the agreement would have a positive economic effect by narrowing the gap in prices of goods and services and the differential in real wages between US and Mexico.

Between 1960 and 1980, the Mexican economy grew at an average annual rate of over 6.5 per cent, leading to significant improvements in per capita GDP and living standards. During the debt crisis of 1982, poverty deepened and productivity growth declined .The government's economic reforms in the latter part of the 1980s helped stimulate economic growth and GDP growth averaged 3.8 per cent between 1990 and 1994. During 1994-2000, it grew at an average rate of 3 per cent p.a. After 2001, economic conditions in the United States improved, which helped economic growth in the Mexican economy. Real GDP growth in 2004 was 4.0 per cent, up from 0.8 per cent during 2001-03. In 2006, GDP grew by 5 per cent but decreased to 3.1 per cent in 2007. The 2009 global financial crisis had a strong adverse effect on the Mexican economy, and the GDP growth rate contracted by 6.6 per cent (Fig. 2).



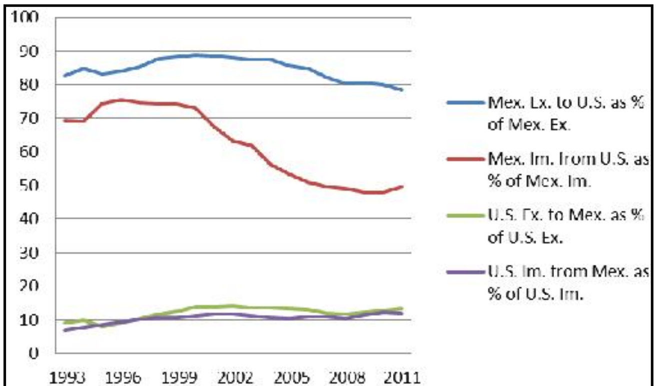
Source : The World Bank

Fig. 2 : Mexico GDP growth

A number of studies have found that NAFTA has brought overall economic and social benefits to the Mexican economy, but the benefits were not evenly distributed throughout the country. A 2005 World Bank study assessing some of the economic impacts from NAFTA on Mexico concluded that NAFTA helped Mexico to close the development gaps with United States and Canada. Several economists have noted that it is likely that NAFTA contributed to Mexico's economic recovery after the 1995 exchange rate crisis. Mexican manufacturers were able to adopt US technological innovations more quickly and thus improve productivity and quality of jobs. A World Bank study states that NAFTA had positive impact employment, reduced economic volatility, enabled easy adaptability to US technological innovations. Since NAFTA, Business cycles in Mexico, the United States, and Canada are more closely correlated and synchronized. NAFTA has reinforced the high sensitivity of Mexican economic sectors to developments in the US. Mexico implemented a strong economic adjustment programme and also by fully adhered to its NAFTA obligations to liberalize trade with the other NAFTA partners. NAFTA may have supported the resolve of the Mexican government to continue with the course of market-based economic reforms, resulting in increasing investor confidence in Mexico. The World Bank study estimates that FDI in Mexico would have been approximately 40 per cent lower without NAFTA.

U.S.-Mexico trade :

Since 1994, Mexico's trade with the United States has grown tremendously. It had a trade deficit of $1.3 billion with the United States in 1994 which shifted to a surplus as exports to the United States increased subsequently. While imports from the United States also increased after NAFTA, the rate of growth was not as high. Much of the increase in US-Mexico trade since 1994 could be attributable to NAFTA, but, as stated previously, exchange rates and economic conditions have also been a factor. The devaluation of the Mexican peso against the dollar in 1995 limited the purchasing power and also made products from Mexico less expensive for the US market. Trade with US rose steadily as economic conditions in Mexico improved in the late 1990s until 2001 when the downturn in the U.S. economy caused trade to slow down. However, since 2002, Mexico's share of the US market has lost ground. China has surpassed Mexico as the second leading supplier of US imports and Mexico's leading source of imports. The United States is also losing market share of Mexico's import market. Between 1993 and 2011, the US share of Mexico's total imports decreased from 69 per cent to 50 per cent (Fig. 3).



Source : IMF international financial statistic.

Fig. 3 : Mexico–US trade shares

US- Mexico foreign direct investment :

The flow of foreign direct investment has increased many folds between the two countries since the inception of NAFTA. The United States is the largest source of FDI in Mexico. In 2012, 58.5 per cent of FDI in Mexico came from the US. The flow of U.S. FDI in Mexico increased from $15.2 billion in 1993 to $92 billion in 2012, a more than 500 per cent increase. From 2000 through 2012, U.S. foreign direct investment in Mexico totalled $291.7 billion (51.4%), concentrated largely in the manufacturing and finance and insurance sectors. Mexican FDI in US was $13.8 billion in 2011, increased by more than 1000 per cent since 1993 from the level of $1.2 billion. It was largely concentrated in the manufacturing and wholesale trade sectors. Sales of services in Mexico by U.S.-owned affiliates were $34.4 billion in 2010, while sales of services in the United States by majority Mexico-owned firms were $4.8 billion (Table 2).

Table 2 : U.S.- Mexican foreign direct Investment positions: 1994-2011 (U.S. $ in millions)

Year	Mexican FDI in the U.S.	U.S. FDI in Mexico
1994	2,069	16,968
1995	1,850	16,873
1996	1,641	19,351
1997	3,100	24,050
1998	2,055	26,657
1999	1,999	37,151
2000	7,462	39,352
2001	6,645	52,544
2002	7,829	56,303
2003	9,022	56,851
2004	7,592	63,384
2005	3,595	73,687
2006	5,310	82,965
2007	8,478	91,046
2008	8,420	87,443
2009	11,492	89,419
2010	12,591	90,304
2011	13,800	91,402

Source: U.S. Department of Commerce, Bureau of Economic Analysis.

The flows of FDI have been affected by other factors over the years, with higher growth during the period of high economic growth during the late 1990s, and slower growth during the 2008 global financial crisis. Yet, we can say that NAFTA provisions on foreign investment may have helped to increase investor confidence and provision of protection to the US and Canadian investors in the country (Table 2).

Income disparity :

At the time of proposal of NAFTA, it expected that was it would improve economic conditions in Mexico and narrow the income disparity between the three countries.

However, it has been pointed out in many of the studies that economic convergence in North America has failed to materialize. The income disparities continued between the two nations. This may be due to lack of regional integration or co-operation between them. Per capita income in Mexico increased from $ 5,710 in 1994 to $ 9,749 in 2012, slower than Latin American countries such as Brazil, Chile and Peru (Table 3).

Mexican wages rose steadily from the early 1980s until

Table 3 : Per capita GDP (Current US$)

Year	Mexico	US
1994	5,710	27,776
1996	4,133	30,068
1998	5,046	32,949
2000	6,664	36,467
2002	7,032	38,175
2004	7,083	41,929
2006	8,618	46,444
2008	9,560	48,407
2010	8,855	48,358
2012	9,749	51,749

Source: The World Bank

1996. During the currency crisis of 1996, average real wages declined by 15.5 per cent, thereafter real wages increased at the rate of 11.8 per cent until 2000, since then they have varied slightly. Wage differential between the skilled and unskilled workers within the country increased even though NAFTA had a positive impact on wages and employment in some Mexican states as pointed out by the World Bank study. Wages were found to be higher in states with higher level of foreign direct investment and states with less developed infrastructure lagged behind. Thus, NAFTA itself was not sufficient to ensure a narrowing of the wage gap between Mexico and the United States.

The study points out that those domestic policies along with geographic and demographic differences, contribute to the continuing disparities in income between the two countries. It argues that Mexico failed to adopt complementary policies such as those related to education, industrial, and transportation infrastructure after NAFTA that could have promoted a more successful regional integration effort. Moreover, the government failed to make reforms in the areas of fiscal policy, labor law reforms etc and hence lacked the proper institutional and regulatory framework to properly implement privatization and trade liberalization efforts.

Impact on agriculture sector :

The *Economist* has pointed out that despite increased competition, Mexican farm exports to the United States have tripled sinceNAFTA's implementation because of reduced tariffs on maize.

After NAFTA, Mexican prices of basic crops such as maize dropped but production increased by more than 41 per cent during 1994-2001. Between 1990 and 2003, corn production increased by 44 per cent compared to 27 per cent rate of growth of US corn production during the same time period.

From 1993 to 2003, Mexican exports to the US in agricultural products such as sugar and related products, beverages, grains and feeds etc grew from $2.7 billion in 1993 to $6.3 billion in 2003, while Mexican exports to Canada increased from $136 million to $409 million. Mexican imports from the US increased from $3.6 billion in 1993 to $7.9 billion in 2003. US foreign direct investment in the Mexican food processing industry has more than doubled.

It has been criticized that NAFTA has had negative impact on Mexican agriculture prospects by opening competition to the heavily subsidized U.S. farm industry. It has caused a higher amount of worker displacement in this sector than in other economic sectors as Mexico began to import lower priced products from the United States. Another study states that the employment in rural agriculture declined from 8 million to 6.8 million and that the value added in agriculture dropped from about $32 billion in 1993 to $25 billion in 2003. It has been raised that NAFTA's agricultural policies did not benefit subsistence farmers, while it provided larger commercial farmers with adequate support.

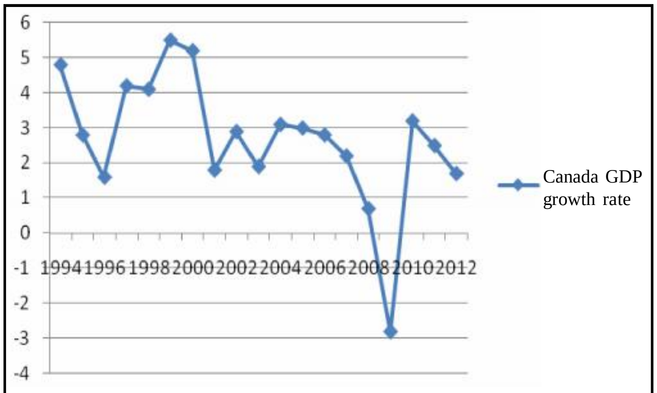
Experts say trade NAFTA has had positive consequences for Mexican private businesses as the deal has led to reduction in Mexican prices for clothes, televisions, and food, which helps offset slow income growth. An estimate suggests that the cost of basic household goods in Mexico has halved since NAFTA's implementation. It has helped to expand the country's manufacturing base. Liberalization of trade has allowed the prices of tradable goods to converge with those in partner countries and thus led to reduction in deficits.

Effect of Canada :

Prior to NAFTA, Canada-US Free Trade Agreement (CUSTA) was signed in 1988 between US and Canada. It aimed at phasing out of a wide range of trade restrictions in stages over a ten-year period, and resulted in a great increase in commerce between the two countries value of US$116 billion in 1985 to more than US$ 240 billion by 2002. All duties covered under the provision of NAFTA were eliminated by 1998. US and Canada undertook number of projects related to biological diversity, conservation etc under the co-operative work programs. The trade flows between US and Canada are the largest between any two countries in the world.

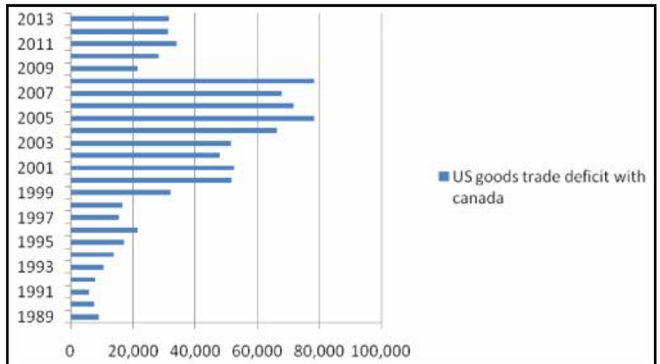
From 1994 to 2000, the Canadian economy grew around average rate of 4 per cent per annum. Since then it has been growing sluggishly at average rate of 1.91 per centp.a similar to the US economy which grew at the average rate of 1.76 per cent over the period 2001-2012. The combined gross domestic product for Canada, the U.S., and Mexico increased from $7.7 trillion in 1993 to $19.2 trillion in 2012 (Fig. 4).

Since NAFTA came into force in 1994, Canada's annual GDP has risen by nearly $1.2 trillion and employment has risen by 4.7 million. Canadian trilateral trade in goods with the United States and Mexico has increased four folds from $ 289 billion in 1993 to nearly $1.1 trillion in 2012. It is the top export destination for the US states. As per an estimate nearly $1.8billion worth of



Source : The World Bank

Fig. 4 : Canada GDP growth rate



Source : United States census bureau

Figures are in $ million on nominal basis.

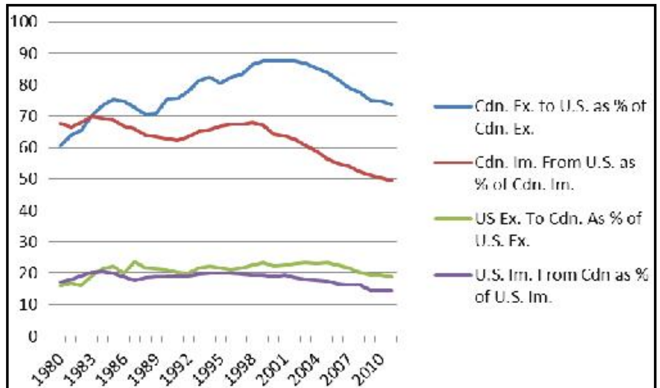
Fig. 5 : U.S. goods trade deficit with Canada

goods and services are traded between US and Canada every day. Productivity has increased by 14 per cent and over 2 million Canadian jobs are now depended on trade with US.

US- Canada trade shares :

Canada's goods exports to the US grew at an annualized rate of 4.4 per cent between 1993 and 2012 and Canada's bilateral merchandise trade with Mexico was around $31 billion in 2012. Approximately 75.7 per cent of Canada's total merchandise exports were destined to US and Mexico. Total merchandise trade between Canada and the United States became more than doubled between 1993 and 2012. Trade between Canada and Mexico has increased by almost 7-fold over the same period. Trade in goods and services between the two nations in 2012 was close to $740 billion or 41 per cent of Canada's GDP. It is the largest market for US services exports with Canada US services trade amounting to $107.6 B in 2012, a 167.3 per cent increase. In 2012, it was the main destination for United States merchandise exports and the second largest source of merchandise imports into the United States. It is the second largest importer of US agriculture products. Its export of private commercial services was $280 billion in 2012, 208 per cent up from pre NAFTA levels. Canada is the main foreign supplier of energy to United States, and is the 4th largest cumulative source of foreign direct investment (FDI) into the United States. The US trade deficit with Canada has steadily increased since NAFTA reaching a high of $78 billion in 2008. The US good trade deficit was $31 billion in 2013 accounting for 4.5 per cent of overall US goods trade deficit (Fig. 5).

Since 2008, the relative importance of value of US- Canada trade has been falling. The US share of Canada's total import has dropped to low of 49.5 per cent in 2011 from peak of 70 per cent in 1983. As a share of U.S. total trade, trade with Canada dropped from 20 per cent-15 per cent since 2003. Trade with the US fell from 74 per cent to 63 per cent of Canada's global trade in the same period. Over the past few years, China has become the largest supplier of US imports.



Source : IMF international financial statistics

Fig. 6 : US-Canada trade shares

US- CANADA foreign direct investment :

The two way investment, both in terms of stock and flow has increased markedly since 1994. The provisions under NAFTA ensure greater stability and certainty for investment decisions and have contributed to enhancing Canada's attractiveness for foreign investors and at the same time providing more opportunities for Canadians to invest in NAFTA partners' economies. US is the largest investor in Canada with a stock of $318.9 billion FDI into Canada in 2011, up from a stock of $69.9 billion in 1993, increasing at an average of $13.9 billion during 1995-2013. It is nearly 54 per cent of the total FDI in Canada. It is equal to 19 per cent of Canada's GDP compared to just 1 per cent in 1994. U.S.

Approximately 40 per cent of Canadian FDI is invested in US. The stock of Canadian FDI in US increased from $27 billion to $211 billion in 2011. Canadian FDI flows into the US increased at an annual average of $1.8 billion during CUFTA to an annual average of $9.7 billion from 1995 to 2011 (Table 4). These direct investments in the US and Canada is led by the finance/

insurance, banking, and manufacturing sectors.

Table 4 : U.S. Foreign direct investment positions with Canada: 1994-2011 (U.S. $ in millions)

Year	Canadian FDI in US	U.S. FDI in Canada
1994	41,219	74,221
1995	45,618	83,498
1996	54,836	89,592
1997	65,175	96,626
1998	72,696	98,200
1999	90,559	98,200
2000	1,14,309	1,32,472
2001	92,420	1,52,601
2002	92,529	1,66,473
2003	95,707	1,87,953
2004	1,25,276	2,14,931
2005	1,65,667	2,31,836
2006	1,65,281	2,05,134
2007	2,01,924	2,50,642
2008	1,68,746	2,46,483
2009	1,88,943	2,65,326
2010	1,88,943	2,89,535
2011	2,10,864	3,18,964

Source : U.S. Department of Commerce, Bureau of Economic Analysis

Job losses and labour flexibility :

Between 1988 and 1994, Canada lost 334,000 manufacturing jobs, equivalent to 17 per cent of total manufacturing employment in the year 1987. During NAFTA's first nine years, employment in Canada grew by 2.7 million. But more than half these new jobs were part-time, insecure jobs with fewer benefits. Canada's official unemployment rate rose from an average of 7.8 per cent in 1988-90 to 11 per cent during 1991-93. A study on labour market conditions in Canada under NAFTA found that "part-time workers-most of them women-earn just two-thirds the wages of equivalent full-time workers, and less than 20 per cent receive benefits from their employers."

Effect on U.S. :

The trade in goods and services with both Mexico and Canada was equal to less than 5 per cent of US GDP before NAFTA. The US trade with the NAFTA partners was already growing prior to NAFTA, Hence, it would be difficult to assess the likely impact of agreement on the US economy and separate it from the other factors. Some studies suggest that the overall net effect of NAFTA on the US economy has been relatively small. A 2003 report by the Congressional Budget Office estimated that NAFTA likely increased the annual US GDP by a very small amount- a few billion dollars. In some sectors such as textile, apparel, automotive, and agriculture industries, trade-related effects have been more significant as they were more exposed to trade liberalization efforts. Its agriculture exports to Mexico and Canada were more than compared to the next six largest markets combined. It reduced oil and grocery prices as dependence on Middle East was reduced. Overall, it has been pointed out in several studies that there was a positive, even though small, impact of NAFTA on the US economy. Its trade with NAFTA partners increased more rapidly than with the rest of the world. Its sectors such as automobiles, textiles, chemicals etc benefitted from the agreement through wider reach and became more competitive. It bought greater product choices to US producers and consumers. The Peterson institute for international economics estimates a gain of $10000 annual income per household. It registered a trade surplus of $2.6 billion with its NAFTA partners in 2011.

NAFTA has been credited with making US manufacturing industries especially auto more competitive and productive through development of supply chains. Supply chains were able to benefit from economies of scale as they could cross national boundaries. The backward and forward linkages reduction in tariff in a given sector not only affect prices in that sector but also in other sectors related to it. Over the period of time, the importance of US Mexico border region as production site increased as flow of intermediate goods produced in US and exported in Mexico and return flow of finished goods from Mexico to US increased. According to one report 40 per cent of US imports from Mexico and 25 per cent of imports from Canada are of US origin.

The most significant impact of the agreement was felt on the North American auto industry. NAFTA provisions allowed removal of Mexico's restrictive trade and investment policies and elimination of US tariffs on auto and auto parts. As a result, US auto trade increased more rapidly. US to auto export to Mexico increased 232 per cent and imports increased by 480 per cent. In 2011, Mexico was the leading supplier of automotive goods for the US. Canada ranked second with 22 per cent of the US market share (Table 5).

Over the years NAFTA has been credited for massive

Table 5 : US trade in Auto with Mexico and Canada, 1993 and 2011

Country	1993		2011		Percentage change	
	Export	Import	Export	Import	Export	Import
Mexico	7.5	11.1	24.9	64.4	232 %	480 %
Canada	26.4	37	52.1	55	97 %	49 %

Source : U.S. Department of Commerce

increase in North American trade and creating job growth in the US. Economist and other groups take it as an engine to further improve trade relations and economic integration with the region. However, over the years, especially the labor and consumer groups have argued that NAFTA has had negative effects. It has been criticized for increasing outsourcing of jobs and lower wages. The following paragraph discusses some of the points against NAFTA from the perspective of the three partners :

NAFTA was touted as a boon to the labour market that would create million jobs in the first five years of its impact. However, the agreement has been accused of rapid job losses. US firms relocated production to Mexico to take advantage of lower wages. US trade deficit worsened with both Mexico and Canada as imports rose. It led to approximate one million job losses in US by 2004. Around 850,000 US workers who lost their jobs in manufacturing sector have been certified for trade adjustment.

There was downward pressure on US wages contributing to income inequality. According to the U.S. Bureau of Labour Statistics, two out of every three displaced manufacturing workers who were rehired in 2012 experienced wage reductions up to 20 per cent.

It was assumed that NAFTA would bring prosperity to Mexico people, that it would provide access to cheaper imported products. However, real wages have fallen significantly below the pre NAFTA levels. Wage increase has fallen short of increase in price of basic consumer goods. The cost of consumer goods has risen by seven times and minimum wages have risen by only four times the pre NAFTA level. Facing falling employment levels, rising prices and stagnant wages, more than half the Mexican population, and more than 60 per cent of the rural population, still falls below the poverty line.

AT the time of proposing NAFTA, it was argued that agreement would allow greater market access to the US farmers and in turn lead to farm income stability. However, the average annual U.S. agricultural trade deficit with Mexico and Canada under NAFTA is $800 million, more than twice the pre-NAFTA level. US beef imports from other two nations have risen by 130 per cent since NAFTA. Despite more than 180 per cent rise in food imports from Canada and Mexico under NAFTA, the average price of food in the US has increased by 65 per cent since inception of NAFTA.

The reductions in consumer goods prices have not been sufficient to offset the reduction in wages under NAFTA. Even after taking into account for gains from cheaper goods, it is expected that US workers without college degrees have lost a net amount equal to 12.2 per cent of their wages due to NAFTA trade. This net loss is equivalent to a loss of more than 3,300 per year for a worker earning the median annual wage of 27,500.

The export of subsidized US corn increased after NAFTA, leading to loss of the livelihoods of more than one million Mexican corn farmers and about 1.4 million additional Mexican workers whose livelihoods depended on agriculture.

NAFTA expanded the maquiladora area program in which Mexican workers were employed by the US owned company to cheaply assemble products for export to the US. The migration of those displaced from Mexico's rural economy pushed down wages in this border factory zone. It also contributed to doubling of Mexican immigration to the United States following NAFTA's implementation. These workers had neither labour rights nor health protection.

The economic rationale behind NAFTA was that it would push the Canada's disappointing rate of economic growth which in eight years prior to the FTA had averaged around only 1.9 per cent per capita per year. The GDP growth rose after NAFTA but real GDP growth per capita was negative during the first five years of NAFTA.

The rationale for free trade is that it would boost productivity and lead to higher wages. A comparison of A comparison of productivity increases and labour costs in the key manufacturing sector in the U.S., Canada and Mexico from 1993 to June 2002 showed that the cumulative increase in Canadian output per hour was only 14.52 per cent, while the increase in the U.S. was 51.98 per cent, and in Mexico 53 per cent. Labour costs, measured in U.S. dollars. In the years prior to CUFTA, manufacturing productivity in Canada was 83 per cent of the US level and by 2000, it was 65 per cent. So, the productivity gap widened rather than narrowed. One of the reasons for the widening productivity gap is the dominance of foreign transnational corporations in Canadian manufacturing.

NAFTA has been blamed for rising income inequalities among different group of workers. The US and Canada has witnessed trend of rising relative wages for the relatively more skilled workers. In Mexico, regional inequality increased as fall in real wages was relatively less in northern border region than in the rest of the country.

Conclusion :

Highlights :

The above analysis and discussion suggests that NAFTA over the last two decades was able to promote North American trade and investment flows. Large multinational corporations have benefitted from increasing competition and wider market reach. Consumers and producers of final good gained as a result of lower prices due to trade expansion and integration. NAFTA was basically designed to improve trade and as the analysis suggests that trade volume among the three nations increased tremendously, touching $1.139 trillion in 2013. Cross border investment as data shows surged. Since 1994, US, Canadian and Mexican GDP have grown by 63, 66 and 65 per cent, respectively. This is better than 53per cent composite growth registered by the OECD countries since 1994. However, it is difficult to isolate the effect on innumerable other factors affecting the growth rate, available estimates and several studies suggest that agreement had a positive impact. It yielded a greater impact on exports than imports. Despite dramatic rise in trade deficit, for example with Mexico from trade surplus of $4 billion in 1993 to the deficit of $54 billion in 2012, the corporate profit margins have risen during the same period. Recently, with acceleration in exports the US trade deficit with Mexico and Canada has contracted. Moreover, there has been a shift of factory employment towards India and China who have emerged as favored destination due to relaxed labor laws and lower wage requirement. Amongst the three partners, Canada seemed to have benefitted from the agreement. There has been increase in bilateral agricultural flows. Though it is difficult to attribute it entirely to NAFTA, given the fact Canada and USA already had a free trade agreement.

A recent poll survey showed that people of US still prefer the idea of free trade with Mexico and Canada compared to trade with countries such as India and China. Similar is the preference in both Mexico and Canada.

NAFTA was expected to provide stimulus to growth and development of the Mexican economy which was facing tough economic conditions before the enactment of NAFTA. However, it failed to bring promised development to the Mexican economy. Approximately 4-5 million people migrated to US during the 90s and now there are around 12 million Mexican born people living in the US. Even though, NAFTA was not directly responsible for such huge migration but it failed to generate adequate employment to restrict it. Income and productivity gap continues to hold back the Mexican economy and attractive U.S and Canadian job markets continue as a pull for the Mexican people.

The general consensus that seems to emerge from the study is that agreement turned out to be a mixed bag for the three nations. It has led to greater economic integration between them with complementary interests, both economic and geopolitical. The business cycles of Mexico and Canada are more closely correlated to that of US. On the other hand despite removal of trade barriers and opening up of markets, it benefitted various special interests. It strongly protected private investor's rights. It did not abolish antidumping and countervailing duties for member countries. NAFTA failed to address labor market issues to significant extent. It loosely adhered to internationally accepted labor rights and standards.

Acceptance or rejection of hypothesis :

Thus based on the above discussion I accept the hypothesis HO and state that as per this study NAFTA improved the three countries economy. Though the magnitude of the improvement is a mixed answer but yes it does improve the U.S., Canada and Mexican economy and their respective trade, investment and growth.

Lessons from the study :

The way ahead :

As data showed, Mexico has lagged behind its two trade partners. It failed to close the "development gap" with Canada and US as its internal economic and social policies reforms lagged behind. It needs more public investment in education and infrastructure, reforms in fiscal and monetary policies to move up the industrial ladder. Thereby, it can attract more skill intensive industries with greater spillover benefits.

The North American states need to focus their attention towards greater co-operation in other policy areas beyond trade. Further deepening of economic relations and greater integration will help to promote economic growth and common trade agenda. Exchange rates should be managed effectively to prevent excessive trade imbalances. Policies should focus on strengthening institutions to protect the environment protection, labour rights and improving corporate and democratic governance. These can be achieved by promoting trade in intermediate goods and supply chains, creating more efforts to close the income gaps within the region, promoting research and development to enhance the global competiveness of North American industries improving border infrastructure, increasing regulatory co-operation.

Limitations of the study :

It is difficult to measure the overall economic impact of NAFTA as trade and investment trends are also affected by variables such as economic growth, exchange rate fluctuation, inflation etc. These variables are known to have far greater impact on aggregate employment and wage levels compared to changes caused by trade liberalization. Mexico and Canada are more dependent on US economy than before. Thus, it is difficult to separate the effect of NAFTA from other factors affecting the growth and development of an economy.

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