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NAFTA AT SEVEN

Its impact on workers in all three nations

Each year since the implementation of the North American Free Trade Agreement (NAFTA) on January 1, 1994, officials in Canada, Mexico, and the United States have regularly declared the agreement to be an unqualified success. It has been promoted as an economic free lunch—a "win-win-win" for all three countries that should now be extended to the rest of the hemisphere in a Free Trade Area of the Americas agreement.

For *some* people, NAFTA clearly has been a success. This should not be a surprise inasmuch as it was designed to bring extraordinary government protections to a specific set of interests—investors and financiers in all three countries who search for cheaper labor and production costs. From that perspective, increased gross volumes of trade and financial flows in themselves testify to NAFTA's achievements.

But most citizens of North America do not support themselves on their investments. They work for a living. The overwhelming majority has less than a college education, has little leverage in bargaining with employers, and requires a certain degree of job security in order to achieve a minimal, decent level of living. NAFTA, while extending protections for investors, explicitly excluded any protections for working people in the form of labor standards, worker rights, and the maintenance of social investments. This imbalance inevitably undercut the hard-won social contract in all three nations.

As the three reports in this paper indicate, from the point of view of North American working people, NAFTA has thus far largely failed.

These reports, based in part on more comprehensive labor market surveys in all three countries,[1] show that the impact on workers in each nation has been different according to their circumstances. For example, given their respective sizes, the impact of economic integration has been inevitably greater in Canada and Mexico than in the United States. But despite this, there are striking similarities in the pattern of that impact.

In the United States, as economist Robert Scott details, NAFTA has eliminated some 766,000 job opportunities—primarily for non-college-educated workers in manufacturing. Contrary to what the American promoters of NAFTA promised U.S. workers, the agreement did not result in an increased trade surplus with Mexico, but the reverse. As manufacturing jobs disappeared, workers were downscaled to lower-paying, less-secure services jobs. Within manufacturing, the threat of employers to move production to Mexico proved a powerful weapon for undercutting workers' bargaining power.

Was U.S. workers' loss Mexican workers' gain? While production jobs did move to Mexico, they primarily moved to maquiladora areas just across the border. As Carlos Salas of La Red de Investigadores y Sindicalistas Para Estudios Laborales (RISEL) reports, these export platforms—in which wages, benefits, and workers' rights are deliberately suppressed—are isolated from the rest of the Mexican economy. They do not contribute much to the development of Mexican industry or its internal markets, which was the premise upon which NAFTA was sold to the Mexican people. It is therefore no surprise that compensation and working conditions for most Mexican workers have deteriorated. The share of stable, full-time jobs has shrunk, while the vast majority of new entrants to the labor market must survive in the insecure, poor-paying world of Mexico's "informal" sector.

As Bruce Campbell of the Canadian Centre for Policy Alternatives reports, Canada's increased market integration with the United States began in 1989 with the bilateral Free Trade Agreement, the precursor to NAFTA. While trade and investment flows increased dramatically, per capita income actually declined for the first seven years after the agreement. Moreover, as in Mexico and the United States, Canadians saw an upward redistribution of income to the richest 20% of Canadians, a decline in stable full-time employment, and the tearing of Canada's social safety net.

This continent-wide pattern of stagnant worker incomes, increased insecurity, and rising inequality has emerged at a time when economic conditions have been most favorable for the success of greater continental integration. The negative effect of increasing trade and investment flows has been obscured by the extraordinary consumer boom in the United States, especially during the period from 1996 through the summer of 2000. The boom, driven by the expansion of domestic consumer credit and a speculative bubble in the stock market, spilled over to Canada and Mexico. Their economies have now become extremely dependent on the capacity of U.S. consumers to continue to spend in excess of their incomes. As the air seeps out of that bubble, the cost of those nations' reliance on the U.S. consumer market is becoming apparent.

The current imbalanced structure of NAFTA is clearly inadequate for the creation of an economically sustainable and socially balanced continental economy. The experience suggests that any wider free trade agreement extended to the hemisphere that does not give as much priority to labor and social development as it gives to the protection of investors and financiers is not viable. Rather than attempting to spread a deeply flawed agreement to all of the Americas, the leaders of the nations of North America need to return to the drawing board and design a model of economic integration that works for the continent's working people.

Jeff Faux, Economic Policy Institute

Endnote

1. The findings in this report grew out of work done in larger studies published in all three of the countries concerned. For more information on the U.S. labor market, see Lawrence Mishel, Jared Bernstein, and John Schmitt, *State of Working America, 2000-2001*, an Economic Policy Institute Book, Ithaca, N.Y.: ILR Press, an imprint of Cornell University Press, 2001.

For a detailed analysis of the Mexican labor market, see Alcalde Arturo, Graciela Bensusán, Enrique de la Garza, Enrique Hernández Laos, Teresa Rendón, and Carlos Salas, *Trabajo y Trabajadores en el México Contemporáneo*, México, D.F.: Miguel Ángel Porrúa, 2000.

A recent analysis of the Canadian labor market can be found in Andrew Jackson and David Robinson, *Falling Behind: The State of Working Canada, 2000*, Ottawa, Ontario: Canadian Centre for Policy Alternatives, 2000.

NAFTA'S HIDDEN COSTS
Trade agreement results in job losses, growing inequality, and wage suppression for the United States

by Robert E. Scott, Economic Policy Institute

The North American Free Trade Agreement (NAFTA) eliminated 766,030 actual and potential U.S. jobs between 1994 and 2000 because of the rapid growth in the net U.S. export deficit with Mexico and Canada. The loss of these real and potential jobs[1] is just the most visible tip of NAFTA's impact on the U.S. economy. In fact, NAFTA has also contributed to rising income inequality, suppressed real wages for production workers, weakened collective bargaining powers and ability to organize unions, and reduced fringe benefits.

NAFTA's impact in the U.S., however, often has been obscured by the boom and bust cycle that has driven domestic consumption, investment, and speculation in the mid- and late 1990s. Between 1994 (when NAFTA was implemented) and 2000, total employment rose rapidly in the U.S., causing overall unemployment to fall to record low levels. Unemployment, however, began to rise early in 2001, and, if job growth dries up in the near future, the underlying problems caused by U.S. trade patterns will become much more apparent, especially in the manufacturing sector. The U.S. manufacturing sector has already lost 759,000 jobs since April 1998 (Bernstein 2001). If, as expected, U.S. trade deficits continue to rise with Mexico and Canada while job creation slows, then the job losses suffered by U.S. workers will be much larger and more apparent than if U.S. NAFTA trade were balanced or in surplus.

Growing trade deficits and job losses

NAFTA supporters have frequently touted the benefits of exports while remaining silent on the impacts of rapid import growth (Scott 2000). But any evaluation of the impact of trade on the domestic economy must include *both* imports and exports. If the United States exports 1,000 cars to Mexico, many American workers are employed in their production. If, however, the U.S. imports 1,000 foreign-made cars rather than building them domestically, then a similar number of Americans who would have otherwise been employed in the auto industry will have to find other work. Ignoring imports and counting only exports is like trying to balance a checkbook by counting only deposits but not withdrawals.

The U.S. has experienced steadily growing global trade deficits for nearly three decades, and these deficits have accelerated rapidly since NAFTA took effect on January 1, 1994. Although gross U.S. exports to its NAFTA partners have increased dramatically—with real growth of 147% to Mexico and 66% to Canada—these increases have been overshadowed by the larger growth in imports, which have gone up by 248% from Mexico and 79% from Canada, as shown in **Table 1-1**. As a result, the \$16.6 billion U.S. net export deficit with these countries in 1993 increased by 378% to \$62.8 billion by 2000 (all figures in inflation-adjusted 1992 dollars). As a result, NAFTA has led to job losses in all 50 states and the District of Columbia, as shown in **Figure 1-A**.

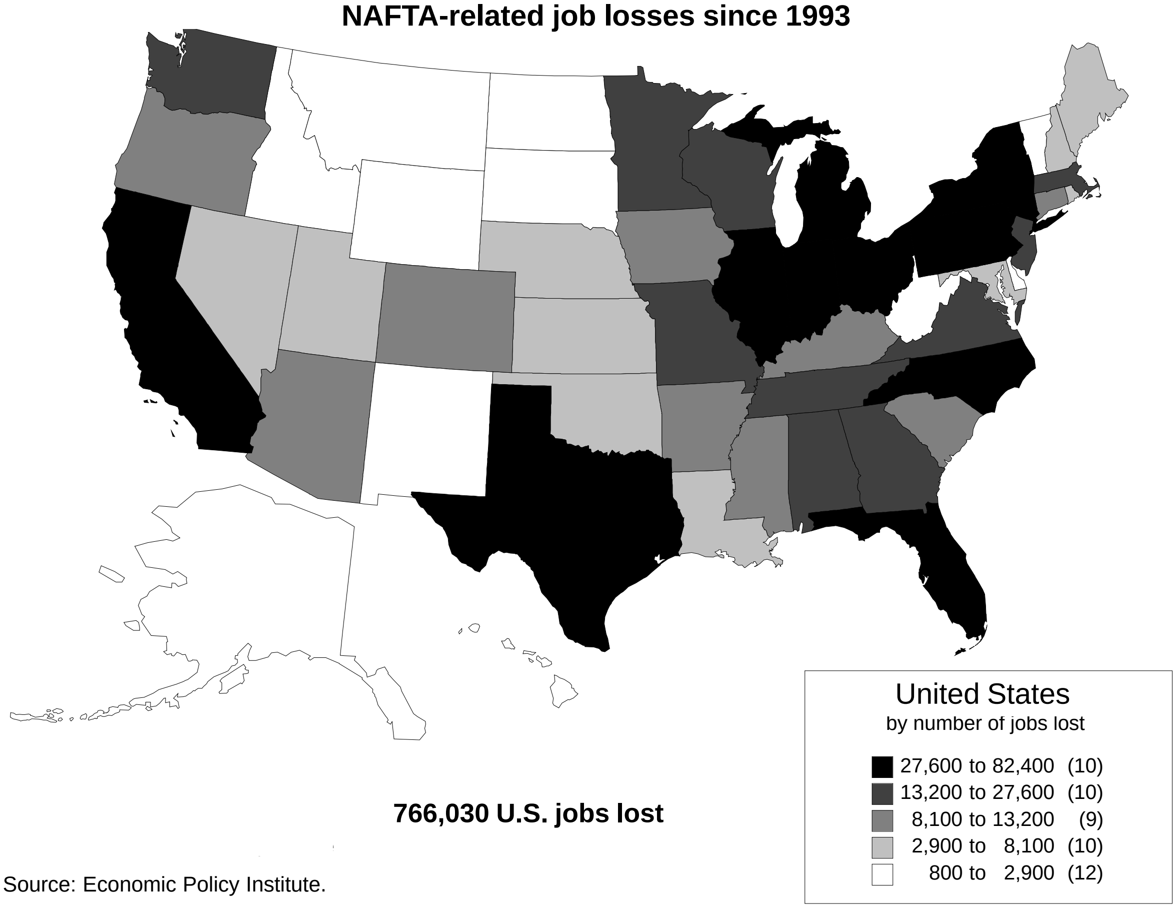
The growing U.S. trade deficit has been facilitated by substantial currency devaluations in Mexico

TABLE 1-1
U.S. trade with Canada and Mexico, 1993-2000,
totals for all commodities (millions of constant 1992 dollars)

			Change since 1993		
	1993	2000	Dollars	Percent	Jobs lost or gained
Canada					
Domestic exports	$90,018	$149,214	$59,196	66%	563,539
Imports for consumption	108,087	193,725	85,638	79	962,376
Net exports	(18,068)	(44,511)	(26,443)	146	(398,837)
Mexico					
Domestic exports	$39,530	$97,509	$57,979	147%	574,326
Imports for consumption	38,074	132,439	94,364	248	941,520
Net exports	1,456	(34,930)	(36,386)	n.a	(367,193)
Mexico and Canada					
Domestic exports	$129,549	$246,723	$117,174	90%	1,137,865
Imports for consumption	146,161	326,164	180,003	123	1,903,896
Net exports	(16,612)	(79,441)	(62,828)	378	(766,030)

FIGURE 1-A

NAFTA-related job losses since 1993



766,030 U.S. jobs lost

Source: Economic Policy Institute.

and Canada, which have made both countries' exports to the United States cheaper while making imports from the United States more expensive in those markets. These devalued currencies have also encouraged investors in Canada and Mexico to build new and expanded production capacity to export even more goods to the U.S. market.

The Mexican peso was highly overvalued in 1994 when NAFTA took effect (Blecker 1997). The peso lost about 31% of its real, inflation-adjusted value between 1994 and 1995, after the Mexican financial crisis. The peso has gained real value (appreciated) recently because inflation in Mexico has remained well above levels in the U.S. As prices in Mexico rose, its exports become less competitive with goods produced in the U.S. and other countries because the peso's market exchange rate was unchanged between 1998 and 2000. High inflation in Mexico also made imports cheaper, relative to goods purchased in the U.S.

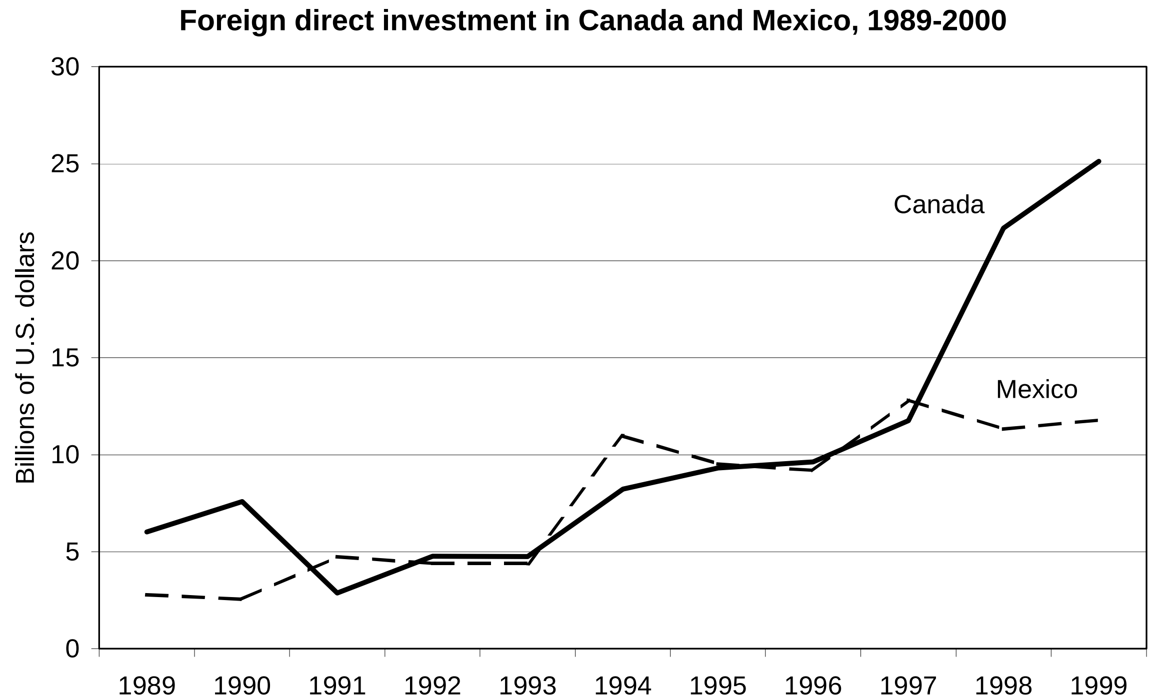
By 2000 the peso's real value had risen to roughly the pre-crisis levels of 1994.[2] Thus, the peso was as overvalued in 2000 as it was when NAFTA took effect. As a result, Mexico's trade and current account balances worsened substantially in 1998-2000, as imports from other countries surged, despite the fact that Mexico's trade surplus with the U.S. continued to improve through 2000. Given Mexico's large overall trade deficits, and the rising value of the peso, pressures are building for another peso crisis in the near future.

The Canadian dollar has depreciated over the past few years. The Canada-U.S. Free Trade Agreement—a precursor to NAFTA—took effect in 1989. Initially, the Canadian dollar rose 4.1% in real terms between 1989 and 1991, as Canada's Central Bank tightened interest rates. During this period, Canada maintained short-term interest rates that averaged 2.25 percentage points above those in the U.S. (1989 to 1994), which caused the initial appreciation in its currency. Canada then began to reduce real interest rates in the mid-1990s. Between 1995 and 2000, short-term interest rates in Canada were 0.75 percentage points *below* U.S. rates, a net swing of 3.0 percentage points. The Canadian dollar began to depreciate in the mid-1990s, as interest rates were reduced, relative to the U.S. Overall, between 1989 and 2000, the Canadian dollar *lost* 27% of its real value against the U.S. dollar.[3]

NAFTA and the devaluation of currencies in Mexico and Canada resulted in a surge of foreign direct investment (FDI) in these countries, as shown in **Figure 1-B**. Between 1993 and 1999 (the most recent period for which data have been published), FDI in Mexico increased by 169%. It grew rapidly between 1993 and 1997, following the peso crisis, and then declined slightly afterwards, because of the steady appreciation of Mexico's real exchange rate between 1995 and 2000.

FDI in Canada more than quadrupled between 1993 and 1999, an increase of 429%, largely as a result of the falling value of the Canadian dollar in this period. Inflows of FDI, along with bank loans and other types of foreign financing, have funded the construction of thousands of Mexican and Canadian factories that produce goods for export to the United States. Canada and Mexico have absorbed more than $151 billion in FDI from all sources since 1993. One result is that the U.S. absorbed an astounding 96% of Mexico's total exports in 1999.[4] The growth of imports to the U.S. from these factories has contributed substantially to the growing U.S. trade deficit and the related job losses. The growth of foreign production capacity has played a major role in the rapid growth in exports to the U.S.

FIGURE 1-B



Source: Economic Policy Institute.

NAFTA costs jobs in every state

All 50 states and the District of Columbia have experienced a net loss of jobs under NAFTA (**Table 1-2**). Exports from every state have been offset by faster-rising imports. Net job loss figures range from a low of 395 in Alaska to a high of 82,354 in California. Other hard-hit states include Michigan, New York, Texas, Ohio, Illinois, Pennsylvania, North Carolina, Indiana, Florida, Tennessee, and Georgia, each with more than 20,000 jobs lost. These states all have high concentrations of industries (such as motor vehicles, textiles and apparel, computers, and electrical appliances) where a large number of plants have moved to Mexico.

While job losses in most states are modest relative to the size of the economy, it is important to remember that the promise of new jobs was the principal justification for NAFTA. According to its promoters, the new jobs would compensate for the increased environmental degradation, economic instability, and public health dangers that NAFTA brings (Lee 1995, 10-11). If NAFTA does not deliver net new jobs, it can't provide enough benefits to offset the costs it imposes on the American public.

Long-term stagnation and growing inequality

NAFTA has also contributed to growing income inequality and to the declining wages of U.S. production workers, who make up about 70% of the workforce. NAFTA, however, is but one contributor to a larger globalization process that has led to growing structural trade deficits and has shaped the U.S. economy and society over the last few decades.[5] Rapid growth in U.S. trade and foreign investment, as a share of

TABLE 1-2
NAFTA job loss by state, 1993-2000

State	Net NAFTA job loss*
U.S. total	766,030
Alabama	16,826
Alaska	809
Arizona	8,493
Arkansas	9,615
California	82,354
Colorado	8,172
Connecticut	9,262
Delaware	1,355
District of Columbia	1,635
Florida	27,631
Georgia	22,918
Hawaii	1,565
Idaho	2,768
Illinois	37,422
Indiana	31,110
Iowa	8,378
Kansas	6,582
Kentucky	13,128
Louisiana	6,613
Maine	3,326
Maryland	8,089
Massachusetts	16,998
Michigan	46,817
Minnesota	13,202
Mississippi	11,469

State	Net NAFTA job loss*
Missouri	16,773
Montana	1,730
Nebraska	4,352
Nevada	4,374
New Hampshire	2,970
New Jersey	19,169
New Mexico	2,859
New York	46,210
North Carolina	31,909
North Dakota	1,288
Ohio	37,694
Oklahoma	7,009
Oregon	10,986
Pennsylvania	35,262
Rhode Island	7,021
South Carolina	10,835
South Dakota	2,032
Tennessee	25,419
Texas	41,067
Utah	5,243
Vermont	1,611
Virginia	16,758
Washington	14,071
West Virginia	2,624
Wisconsin	19,362
Wyoming	864

* Excluding effects on wholesale and retail trade and advertising.

Source: EPI analysis of Bureau of Labor Statistics and Census Bureau data.

U.S. gross domestic product, has played a large role in the growth of inequality in income distribution in the last 20 years. NAFTA has continued and accelerated international economic integration, and thus contributed to the growing tradeoffs this integration requires.

The growth in U.S. trade and trade deficits has put downward pressure on the wages of “unskilled” (i.e., non-college-educated) workers in the U.S., especially those with no more than a high school degree. This group represents 72.7% of the total U.S. workforce and includes most middle- and low-wage workers. These U.S. workers bear the brunt of the costs and pressures of globalization (Mishel et al. 2001, 157, 172-79).

A large and growing body of research has demonstrated that expanding trade has reduced the price of import-competing products and thus reduced the real wages of workers engaged in producing those goods. Trade, however, is also expected to increase the wages of the workers producing exports, but growing trade deficits have meant that the number of workers hurt by imports has exceeded the number who have benefited through increased exports. Because the United States tends to import goods that make intensive use of less-skilled and less-educated workers in production, it is not surprising to find that the increasing openness of the U.S. economy to trade has reduced the wages of less-skilled workers relative to other workers in the United States.[6]

Globalization has reduced the wages of "unskilled" workers for at least three reasons. First, the steady growth in U.S. trade deficits over the past two decades has eliminated millions of manufacturing jobs and job opportunities in this country. Most displaced workers find jobs in other sectors where wages are much lower, which in turn leads to lower *average* wages for all U.S. workers. Recent surveys have shown that, even when displaced workers are able to find new jobs in the U.S., they face a reduction in wages, with earnings declining by an average of over 13% (Mishel et al. 2001, 24). These displaced workers' new jobs are likely to be in the service industry, the source of 99% of net new jobs created in the United States since 1989, and a sector in which average compensation is only 77% of the manufacturing sector's average (Mishel et al. 2001, 169). This competition also extends to export sectors, where pressures to cut product prices are often intense.

Second, the effects of growing U.S. trade and trade deficits on wages go beyond just those workers exposed directly to foreign competition. As the trade deficit limits jobs in the manufacturing sector, the new supply of workers to the service sector (displaced workers and new labor market entrants not able to find manufacturing jobs) depresses the wages of those already holding service jobs.

Finally, the increased import competition and capital mobility resulting from globalization has increased the "threat effects" in bargaining between employers and workers, further contributing to stagnant and falling wages in the U.S. (Bronfenbrenner 1997a). Employers' credible threats to relocate plants, to outsource portions of their operations, and to purchase intermediate goods and services directly from foreign producers can have a substantial impact on workers' bargaining positions. The use of these kinds of threats is widespread. A *Wall Street Journal* survey in 1992 reported that one-fourth of almost 500 American corporate executives polled admitted that they were "very likely" or "somewhat likely" to use NAFTA as a bargaining chip to hold down wages (Tonelson 2000, 47). A unique study of union organizing drives in 1993-95 found that over 50% of all employers made threats to close all or part of their plants during organizing drives (Bronfenbrenner 1997b). This study also found that strike threats in National Labor Relations Board union-certification elections nearly doubled following the implementation of the NAFTA agreement, and that threat rates were substantially higher in mobile industries in which employers can credibly threaten to shut down or move their operations in response to union activity.

Bronfenbrenner updated her earlier study with a new survey of threat effects in 1998-99, five years after NAFTA took effect (Bronfenbrenner 2000). The updated study found that most employers continue to threaten to close all or part of their operations during organizing drives, despite the fact that, in the last five years, unions have shifted their organizing activity away from industries most affected by trade deficits and capital flight (e.g., apparel and textile, electronics components, food processing, and metal fabrication). According to the updated study, the threat rate increased from 62% to 68% in mobile industries such as manufacturing, communications, and wholesale distribution. Meanwhile, in 18% of campaigns with threats, the employer directly threatened to move to another country, usually Mexico, if the union succeeded in winning the election.

The new study also found that these threats were simply one more extremely effective tactic in employers' diverse arsenal for thwarting worker efforts to unionize. At 38%, the election win rate associated with organizing campaigns in which employers made threats was significantly lower than the 51% win rate where there were no threats. Win rates were lowest—32% on average—when threats were made during organizing campaigns involving more mobile industries, such as manufacturing, communications, and wholesale distribution. Among this last group, companies targeted for organizing are much likelier than they were in 1993-95 to be subsidiaries of large multinational parent companies with foreign operations, customers, and suppliers. The 30% win rate for organizing campaigns with these global multinational companies suggests that the existence of other sites in Latin America, Asia, or Africa serves as an unspoken threat of plant closing for many U.S. workers.

Bronfenbrenner (2000) described the impact of these threats in testimony to the U.S. Trade Deficit Review Commission:

> Under the cover of NAFTA and other trade agreements, employers use the threat of plant closure and capital flight at the bargaining table, in organizing drives, and in wage negotiations with individual workers. What they say to workers, either directly or indirectly, is if you ask for too much or don't give concessions or try to organize, strike, or fight for good jobs with good benefits, we'll close, we'll move across the border just like other plants have done before.[7]

In the context of ongoing U.S. trade deficits and rising levels of trade liberalization, the pervasiveness of employer threats to close or relocate plants may conceivably have a greater impact on real wage growth for production workers than does actual import competition. There are no empirical studies of the effects of such threats on U.S. wages, so such costs simply have been ignored by other studies of NAFTA.

NAFTA, globalization, and the U.S. economy

The U.S. economy created 20.7 million jobs between 1992 and 1999. All of those gains are explained by growth in domestic consumption, investment, and government spending. The growth in the overall U.S. trade deficit eliminated 3.2 million jobs in the same period (Scott 2000). Thus, NAFTA and other sources of growing trade deficits were responsible for a change in the composition of employment, shifting workers from manufacturing to other sectors and, frequently, from good jobs to low-quality, low-pay work.

Trade-displaced workers will not be so lucky during the next economic downturn. If unemployment begins to rise in the U.S., then those who lose their jobs due to globalization and growing trade deficits could face longer unemployment spells, and they will find it much more difficult to get new jobs.

When trying to tease apart the various contributing causes behind trends like the disappearance of manufacturing jobs, the rise in income inequality, and the decline in wages in the U.S., NAFTA and growing trade deficits provide only part of the answer. Other major causes include deregulation and privatization, declining rates of unionization, sustained high levels of unemployment, and technological change. While each of these factors has played some role, a large body of economic research has concluded that trade is responsible for at least 15-25% of the growth in wage inequality in the U.S. (U.S. Trade Deficit Review Commission 2000, 110-18). In addition, trade has also had an indirect effect by contributing to many of these other causes. For example, the decline of the manufacturing sector attributable to increased globalization has resulted in a reduction in unionization rates, since unions represent a larger share of the workforce in this sector than in other sectors of the economy.

So, although NAFTA is not solely responsible for all of the labor market problems discussed in this report, it has made a significant contribution to these problems, both directly and indirectly. Without major changes in the current NAFTA agreement, continued integration of North American markets will threaten the prosperity of a growing share of the U.S. workforce while producing no compensatory benefits to non-U.S. workers. Expansion of a NAFTA-style agreement—such as the proposed Free Trade Area of the Americas—will only worsen these problems. If the U.S. economy enters into a downturn or recession under these conditions, prospects for American workers will be further diminished.

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Methodology used for job-loss estimates

This study uses the model developed in Rothstein and Scott (1997a and 1997b). This approach solves four problems that are prevalent in previous research on the employment impacts of trade. Some studies look only at the effects of exports and ignore imports. Some studies include foreign exports (transshipments) — goods produced outside North America and shipped through the United States to Mexico or Canada — as U.S. exports. Trade data used in many studies are usually not adjusted for inflation. Finally, a single employment multiplier is applied to all industries, despite differences in labor productivity and utilization.[8]

The model used here is based on the Bureau of Labor Statistics' 192-sector employment requirements table, which was derived from the 1992 U.S. input-output table and adjusted to 1998 price and productivity levels (BLS 2001a). This model is used to estimate the direct and indirect effects of changes in goods trade flows in each of these 192 industries. This study updates the 1987 input employment requirements table used in earlier reports in this series (Rothstein and Scott 1997a and 1997b; Scott 1996).

We use three-digit, SIC-based industry trade data (Bureau of the Census 1994 and 2001), deflated with industry-specific, chain-weighted price indices (BLS 2001b). These data are concorded from HS to SIC (1987) classifications using conversion tables on the Census CDs. The SIC data are then concorded into the BLS sectors using sector-plans from the BLS (2001a). State-level employment effects are calculated by allocating imports and exports to the states on the basis of their share of three-digit, industry-level employment (BLS 1997).

Endnotes

1. Potential jobs, or job opportunities, are positions that would have been created if the trade deficit with Mexico and Canada had remained constant, in real terms (and holding everything else in the economy constant). The total number of jobs and job opportunities is a measure of what employment in trade-related industries would have been if the U.S. NAFTA trade balance remained constant between 1993 and 2000, holding everything else constant.

2. EPI calculations and International Monetary Fund (IMF) (2001).

3. IMF (2001) and EPI calculations. This analysis compares overnight money market rates in Canada (annual averages) with the comparable federal funds rate for the U.S.

4. Bureau of the Census (2000) and EPI calculations.

5. Globalization includes rapid growth in imports, exports, and the share of trade in the world economy, and even more rapid growth in the international flows of foreign investment around the world. The term is also used to refer to the international convergence of rules, regulations, and even the social structure and role of government in many countries. This process is often viewed as a "race-to-the-bottom" in global environmental standards, wages, and working conditions.

6. See U. S. Trade Deficit Review Commission (2000, 110-18) for more extensive reviews of theoretical models and empirical evidence regarding the impacts of globalization on income inequality in the U.S.

7. Bronfenbrenner (1999).

8. Other studies—see California State World Trade Commission (1997), which finds 47,600 jobs created in California from increased trade with Canada alone—have allocated all employment effects to the state of the exporting company. This is problematic, because the production—along with any attendant job effects—need not have taken place in the exporter's state. If a California dealer buys cars from Chrysler and sells them to Mexico, these studies will find job creation in California. However, the cars are not made in California; so the employment effects should instead be attributed to Michigan and other states with high levels of auto industry production. Likewise, if the same firm buys auto parts from Mexico, the loss of employment will occur in auto-industry states, not in California.

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THE IMPACT OF NAFTA ON WAGES AND INCOMES IN MEXICO

By Carlos Salas, La Red de Investigadores y Sindicalistas Para Estudios Laborales (RISEL)

Mexico is much changed in the seven years since NAFTA was implemented in 1994. Although Mexico now has a large trade surplus with the U.S., Mexico has also developed a large and growing overall trade deficit with the rest of the world. In fact, Mexico's net imports from the rest of the world now substantially exceed its net exports to the United States. Official unemployment levels in Mexico are lower now than before NAFTA, but this decline in the official rate simply reflects the absence of unemployment insurance in Mexico. In fact, underemployment and work in low-pay, low-productivity jobs (e.g., unpaid work in family enterprises) actually has grown rapidly since the early 1990s. Furthermore, the normal process of rural-to-urban migration that is typical of developing economies has reversed since the adoption of NAFTA. The rural share of the population increased slightly between 1991 and 1997, as living and working conditions in the cities deteriorated.

Between 1991 and 1998, the share of workers in salaried[1] jobs with benefits fell sharply in Mexico. The compensation of the remaining self-employed workers, who include unpaid family workers as well as small business owners, was well above those of the salaried sector in 1991. By 1998, the incomes of salaried workers had fallen 25%, while those of the self-employed had declined 40%. At that point, the average income of the self-employed was substantially lower than that of the salaried labor force. This reflects the growth of low-income employment such as street vending and unpaid family work (for example, in shops and restaurants). After seven years, NAFTA has not delivered the promised benefits to workers in Mexico, and few if any of the agreement's stated goals has been attained.

Running hard but falling behind

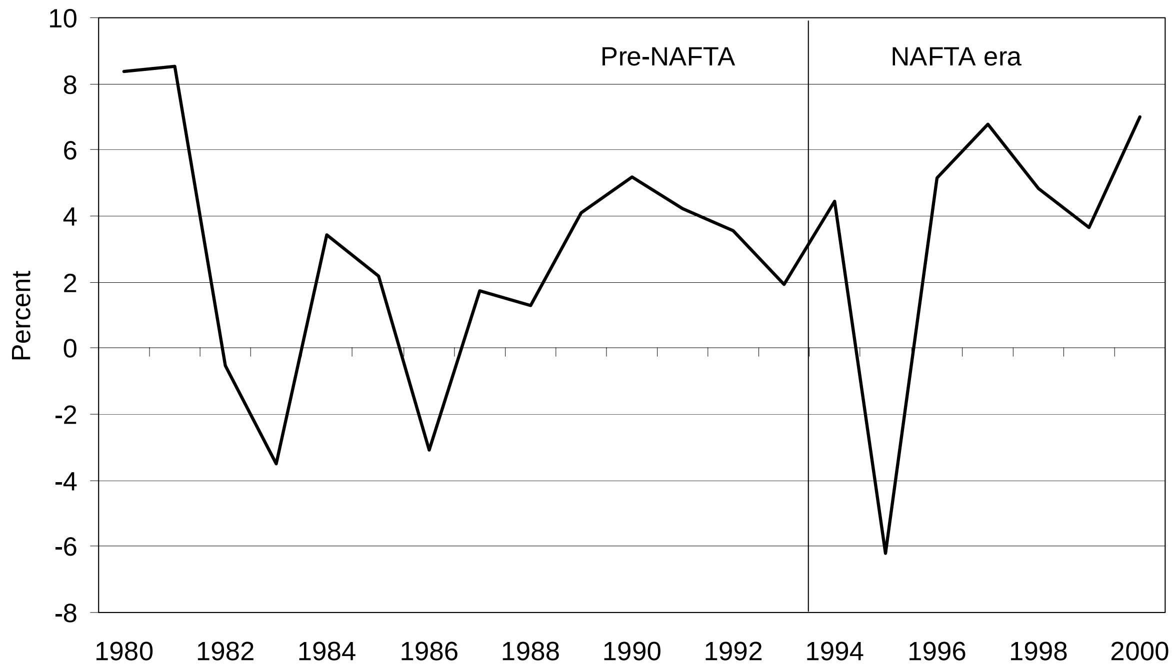
Despite a quick recovery from the 1995 peso crisis and a peak 7% gross domestic product (GDP) growth rate in 2000 (**Figure 2-A**), NAFTA still has failed to help most workers in Mexico.

Although foreign direct investment (FDI) in Mexico has continued to grow, total investment actually declined between 1994 and 1999 (**Table 2-1**). The only types of investment that have grown since 1994 are the maquiladora industries, reinvested profits, and stock market investments. Speculative flows of financial capital into stock market investments, in particular, increased, but overall investment in Mexico fell between 1994 and 1999. These inflows help explain the rapid—and perhaps unsustainable—growth in prices on the Mexican stock market in the late 1990s.

Manufacturing exports, as officially reported, have improved rapidly since NAFTA took effect. From 1995 to 1999, these exports grew at an annual rate of 16%, due almost exclusively to "value added" exports in Maquiladora production.[2] The total value of these exports increased 19.7% annually, as the average value added of products exported from Mexico decreased (relative to their overall value). However, maquiladora exports contain a substantial share of imported components from the U.S. and other countries, reducing the net benefits of these exports to the Mexican economy and its development. Thus,

FIGURE 2-A

Real GDP growth in Mexico, 1980-2000



Source: INEGI, Base de Información Económica, Febbruary 2001.

Table 2-1
Foreign investment (billions of U.S. dollars)

	1994	1999
Total foreign investment*	$19,045	$16,295
New investment	9,661	4,448
Profit reinvestment	2,336	2,627
Intrafirm investment	2,038	1,932
Investment in maquiladoras	895	2,778
Stock market investment	4,083	4,509

* Partials may not add to total due to rounding.

Source: VI Informe de Gobierno de Ernesto Zedillo, 2000.

the export growth and the foreign trade performance of the Mexican economy look better on paper than in reality. But even these benefits disappear when total imports are considered. Total manufacturing imports from the U.S. and the rest of the world grew 18.5% per year between 1995 and 1999, a fact that explains Mexico's rapidly growing overall foreign trade deficit in this period. In the long run, this process of economic growth with expanding foreign trade deficits could lead to another major currency crisis similar to the one that occurred in 1994 (Blecker 1996).

How strong was employment growth between 1995 and 1999?

Total employment in Mexico grew from 33.9 to 39.1 million jobs over the 1995-99 period (3.7% annually), according to officially reported data (INEGI 1995 and 1999). But these data must be used with some caution, because the sample used for the National Employment Survey changed in 1998. Comparing the 1998 and 1999 data provides a more realistic rate of employment growth. Total employment reported for 1998 was 38.6 million jobs, resulting in an actual rate of growth in 1999 of only 1.2%.

Total employment in Mexico must grow 2.5% in order to fulfill the yearly demand for 1.2 million new jobs (CONAPO 2000). Since GDP grew 3.7% in 1999, these data suggest that GDP should grow at about 7% annually to achieve a sustained 2.5% growth rate in employment and avoid rising unemployment. Yet Mexico has achieved a 7% rate of growth in only one year (2000) in the past decade.

Agricultural employment trends

Agricultural activities are still the most important single source of employment in Mexico. In 1999, agricultural employment (8.2 million workers) accounted for 21% of the total labor force. For the past 10 years, agricultural employment has hovered around eight million. This stability suggests that NAFTA did not lead to a major surge in migration trends from the countryside to the cities. Over the long term, steady growth in corn imports has helped stimulate a general migration process. This doesn't mean that most *campesinos*—traditional corn growers—will decide to remain in rural areas in the future. A major increase in rural-to-urban migration process could start sometime in the next decade if corn prices keep falling and no other sources of income generation are provided to *campesinos*.

Interstate migration patterns, however, remained unchanged in this period, which reinforces the idea that most corn growers still are cultivating their land plots (Nadal 2000). What is more remarkable is that there was a slight increase in the share of the population living in rural areas between 1991 and 1997.

Migration is another major alternative for Mexican workers who cannot find good jobs. Northbound international migration has increased all through the 1990s, and the number of permanent migrants, in particular, has been on the rise (Tuirán 2000). The geographical origin of these migrants is very diverse, as many of the new migrants come from regions with no previous history of migration flows to the United States. At the same time, more migrants are coming from urban areas and are better educated, which provides a stark contrast with the traditional image of rural, illiterate migrants. This shift in migration patterns is another significant indicator of a decline in the supply of good jobs in Mexico, even for well-educated workers.

Nonagricultural employment trends

Despite the increase in migration to the north, it appears that the rapid growth in Mexico's potential labor supply has been matched by a seemingly impressive rate of growth in nonagricultural occupations. On average, the number of employed has increased by slightly less than 1.3 million per year. The unemployment rate has, therefore, not shown any upward trend and has remained at a low level, with only short-term fluctuations as economic activity has varied. Unemployment in urban areas remained at very low levels of 2-3% between 1987 and 1999. The only major exception was in 1995, corresponding with the peso crisis, when overall unemployment surged above 6% and reached almost 14% for teenagers. Overall, however, unemployment rates have been low by international standards, rarely exceeding 8% even for young people.

It would be misleading, however, to conclude from such steadily low unemployment measures that Mexico has avoided the difficulties that most market economies face of providing enough jobs. There are, in fact, clear explanations as to why the official unemployment measures are so low. Mexico's labor force statistics count someone as employed if that person has worked at least one hour in the week before the survey takes place, following ILO standards (Hussmans et al. 1990). Under this definition, a person is counted as employed regardless of whether the person only works half time for no pay in a family business or works full time in a modern manufacturing plant. But Mexico's low rate of open unemployment is not a statistical distortion—it primarily reflects the workings of a different labor market structure.[3] Given that a large proportion of the population has no capacity for saving, and that there is no unemployment insurance, open unemployment in Mexico is, to paraphrase Gunnar Myrdal, a luxury few can afford.

Not surprisingly, unemployment rates are clearly higher for the most educated, who have higher incomes and greater savings capacity. But for those at the bottom of the wage scale, being "employed" does not guarantee an adequate standard of living, especially given the broad definition of what constitutes employment in the Mexican labor market.. Deteriorating labor market conditions in Mexico have thus resulted in a decline in the quality of jobs rather than increases in unemployment rates, as might be the case in other economies with effective social safety nets.

The inability of the Mexican economy to create good quality jobs reflects two primary trends: a virtual halt in the process of urbanization, and the large and growing share of workers holding low-productivity, low-paying jobs in urban areas. While the economy was reducing the relative number of workers occupied in agricultural activities between 1970 and 1990, the past decade witnessed a reversal of this trend. Modernization of the economy, crudely defined as a declining share of rural and agricultural activities in the economy, was stagnant during most of these years. In spite of deficiencies in sampling and comparability of national employment surveys, the available data clearly show that, in the 1990s, the share of the labor force in less-urbanized areas and the share engaged in agricultural activities have both remained roughly constant at around 50% and 20-25%, respectively (INEGI-ENE 1991 and 1997).[4]

The deteriorating labor market conditions in the most important cities are reflected by an increase in the proportion of workers who are either self-employed or work in businesses with less than five employees. These low productivity jobs usually offer low pay. The share of the self-employed in total employment between 1987 and 1999 is shown in **Table 2-2**. The most important trend in urban employment in Mexico is the growth in service sector employment, as is happening in most economies. Rapid employment growth (and production) in trade and service industries poses two problems for the Mexican economy. Unlike service sector jobs in developed economies, Mexico's non-industrial activities do not include a strong and dynamic sector of high value-added services. Even in the case of the growing employment in financial service activities—a process clearly associated with privatization and new investments—a large part of this expansion can be attributed to continued protection and the absence of regulation (but not to the spread of highly competitive, world-class services). Thus, wages and productivity in these industries are low, by world standards.

Mexico's service sector growth is characterized by extreme heterogeneity, running the gamut from

TABLE 2-2
Labor structure in urbanized areas, 1991-98

	1991	1998
Owner	4.8%	4.0%
Self-employed	16.6	22.8
Waged	73.9	61.2
Unpaid	4.6	12.0
Other	0.1	0.1
Total	100.0	100.0

Source: Calculations based on data files from INEGI's Encuesta Nacional de Empleo (ENE), 1991 and 1998.

single-person activities such as street vending to stock market brokering using the latest technologies and facilities. Furthermore, unlike the newly industrialized countries of Asia, Mexico's adoption of an economic strategy that relies on sustained growth in manufacturing exports—facilitated by its close geographic proximity to the U.S.—has not increased the share of manufacturing employment in the economy.

As a result of these trends, the structure of the urban labor landscape has changed in important ways in the 1990s. The most important shift is the diminishing share of regular salaried occupations in total employment. Between 1991 and 1998, the share of salaried employees in total employment decreased by 13 percentage points, from 73.9% to 61.2%. The resulting void was filled by either informal employment activities or simple unemployment. The share of self-employed workers increased by 50%, and the share of workers having unpaid positions as their first occupation doubled (as shown in Table 2-2).

Older salaried workers apparently switched to self-employed occupations, while younger workers were even less fortunate, moving into unpaid positions or becoming unemployed in this period. The share of workers aged 12 to 14 that had unpaid positions jumped from 40% to 60% between 1991 and 1998. The reduction in salaried occupations has cut across most industries. However, there are significant differences between those industries. A high proportion of nonsalaried jobs in the labor market indicates a backward production structure. For example, retail trade, food, transportation, and accommodations have among the largest shares of self-employed and unpaid workers. The high rate of nonsalaried jobs in these industries reflects the large presence of small firms and relative simplicity of the tasks performed by the workers in those jobs. Comparing 1991 and 1998, the loss of salaried occupations was almost completely offset by the growth in self-employed and unpaid workers.

Traditional manufacturing activities show the sharpest relative reductions in the shares of salaried workers, with the modern manufacturing, construction, trade, and communications industries being the next largest losers of salaried jobs. These changes are partially explained by the effects of the 1995 crisis upon traditional types of production in manufacturing and other industries, but they also reflect long-term segmentation trends in labor markets.

The growing share of self-employed workers means that people moved to deteriorating labor occupations. Wages decreased by 27% between 1991 and 1998, while overall hourly income from labor decreased 40%. Thus, labor income for the self-employed was cut in half in this period (**Table 2-3)**.

TABLE 2-3
Mean hourly income from labor, 1991-98 (1993 pesos)

	1991	1998	Percent change
Owner	20.53	10.71	-47.8
Subcontractors	12.47	n.a.	n.a.
Self-employed	7.71	3.89	-49.6
Co-operatives	4.22	7.01	66.2
Salaried	6.57	4.83	-26.6
Salaried, by piece or percentage	8.31	4.40	-47.0
Other	6.12	n.a.	n.a.
All	7.04	4.22	-40.0

Source: Author’s calculations based on data files from INEGI’s Encuesta Nacional de Empleo (ENE), 1991 and 1998.

TABLE 2-4
Share of salaried workers with fringe benefits in urban areas (percent)

	1991	1998
End-of-the-year bonus	62.7	54.5
Participation in profits	19.2	15.4
Paid holidays	59.3	50.4
Credit for housing	13.3	21.8
Health insurance (IMSS)	45.5	42.7
Health insurance (ISSSTE)	7.0	4.6
Private health	12.5	9.3

Source: Author’s calculations based on ENE data files, 1991 and 1998.

Average self-employment incomes fell from 17% above salaried worker incomes in 1991 to 19% below in 1998. In real terms, the relative well-being of the self-employed did not decrease as much as suggested by income comparisons, but this is far from reassuring. Reductions in real wages do not entirely explain the deterioration of labor conditions. During the same period, the share of salaried workers receiving fringe benefits also fell systematically, as shown in **Table 2-4.**

The maquiladora sector’s employment performance contrasts significantly with that of Mexico’s other large manufacturing plants. The maquiladora sector began as a program for in-bond processing plants, primarily making goods for re-export in Mexico’s northern border cities. These plants employed an industrially inexperienced labor force to perform simple assembly tasks in traditional manufacturing. Maquiladoras have evolved over time, but they have remained largely isolated from the rest of the Mexican economy. Maquiladora employment grew rapidly, from 60,000 workers in 1975 to 420,000 in 1990. The pace of job creation slowed somewhat in the early 1990s, but it accelerated again after the 1994–95 peso devaluation. In

TABLE 2-5
Employment in selected maquiladora activities in 2000

	Employment
Electric and electronic parts and components	335,668
Apparel and textiles	281,866
Transportation equipment and parts	237,004
Electric and electronic apparatus and appliances	104,262
Other manufacturing activities	142,805

Source: Base de Información Económca, INEGI.

2000, maquiladora industries employed 1.3 million workers, concentrated mostly in electrical and electronic products, auto parts, and apparel and textiles. Employment in those activities accounts for more than 80% of total manufacturing employment in the maquiladora plants (**Table 2-5**).

Maquiladoras have helped offset weak job creation in other domestic manufacturing industries,[5] accounting for about 13% of total manufacturing employment in 1995 and almost 16% in 1999. Maquiladora plants contributed 35% of all new manufacturing employment between 1995 and 1999. Most of the remaining jobs created during this period were in small non-maquiladora plants (Alarcón and Zepeda 1997, 1998).

The 1995 recession's impact on maquiladora plants was relatively mild, which is not surprising given their nearly complete specialization in export production.[6] Maquiladora job growth accelerated between 1995 and 1997, adding 150,000 positions each year during this three-year period. This sum far exceeds the 60,000 jobs added each year between 1987 and 1989. Employment in maquiladora apparel production rose rapidly from 1995 to 1997, a fact closely linked to the relaxation of the Multifibre Agreement quotas after the implementation of NAFTA (O'Day 1997). Maquiladora jobs in electronics and auto part exports expanded as well, in keeping with those industries' global strategies (Carrillo and Gonzalez 1999).

There were also important regional changes as maquiladora plants were established in cities far from the Mexico-U.S. border. Between 1994 and 1999, the proportion of maquiladora workers in non-border locations increased from 16% to 22% as maquiladora production began shifting southward to sites such as Jalisco, the State of Mexico, Mexico City, Puebla, and Yucatan. Apparel-producing maquiladora plants, in contrast, moved to areas where compliance with labor laws is low, such as the states of Puebla and Morelos.

Declining wages

Most directly employed workers have seen a steady erosion of their wages in the 1990s. In the last decade, the minimum wage in Mexico lost almost 50% of its purchasing power. The minimum wage is set each year through a process that includes consultations between official unions, employers, and the federal government. Currently the minimum wage is just a reference point for the wage bargaining

TABLE 2-6
Wages in Mexico, 1990-99 (1990 = 100)

Year	Mimimum wage	Contractual wages	Wages in manufacturing
1990	100.00	100.00	100.00
1993	67.50	84.90	111.40
1994	65.80	81.50	105.20
1995	81.10	85.50	88.70
1996	66.50	76.60	81.20
1997	58.90	68.20	82.90
1998	56.90	66.50	85.70
1999	55.40	66.80	88.40
Change,1993-99	-17.9%	-21.3%	-20.6%

Source: 6° Informe de gobierno de Ernesto Zedillo, 2000

process of wage and salary workers, and wages are usually set above this level in negotiated contracts.

Labor income in industries whose wage bargaining processes are under federal supervision (the so-called *salarios contractuales* or contractual wages) lost almost more than 21% of their purchasing power between 1993 (the year before NAFTA took effect) and 1999 (**Table 2-6**). Manufacturing wages also declined by almost 21% in this period, and the purchasing power of the minimum wage fell 17.9% through 1999. The decline in real wages since NAFTA took effect helps explain the decline in labor incomes (see Table 2-3).

Conclusion

The decline in real wages and the lack of access to stable, well-paid jobs are critical problems confronting Mexico's workforce. While NAFTA has benefited a few sectors of the economy, mostly maquiladora industries and the very wealthy, it has also increased inequality and reduced incomes and job quality for the vast majority of workers in Mexico. In many ways (such as the stagnation of the manufacturing share of employment), the entire process of development has been halted, and in some cases it even may have been reversed. NAFTA has created some of the most important challenges for Mexico's development in the 21st century. The question that remains is whether Mexico can, under NAFTA, restart its stalled development and find a way to redistribute the benefits of the resulting growth.

Endnotes

1. Most workers in Mexico are paid a daily wage, as opposed to the hourly wage paid in the U.S. These workers are referred to in Mexico's statistics as "salaried," or, more literally, "waged" employees. These terms refer to several different methods of payment (both daily and piece-work, for example). Thus, a salaried job in Mexico can be very different from one in the U.S.

2. Under U.S. tariff code provisions (HTS 9802), U.S. firms are allowed to send U.S-made inputs abroad for assembly and then return those semi-finished or finished products to the U.S., paying a tariff only on value added abroad.

3. The condition of open unemployment includes "frictional" unemployment, that is, people who know for sure or firmly believe they will be hired in the near future (Rendon y Salas 1993). For further discussion of measures of Mexico's unemployment see, for example, Fleck and Sorrentino (1994).

4. The share of less-urbanized areas was 52.6% in 1991 and 53.6% in 1997. The share in agriculture was 23.6% in 1991 and 24.1% in 1997 (derived from INEGI- ENE 1991 and 1997).

5. Prior to the 1994-95 economic crisis, domestic-oriented and export-oriented manufacturing plants were approximately even in terms of employment creation. However, the 1994-95 devaluation of the peso gave exporters a boost, and maquiladora employment rose faster than in domestic-oriented producers.

6. In fact, short-term economic or political events appear to have little effect on maquiladora activities.

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FALSE PROMISE

Canada in the Free Trade Era

by Bruce Campbell, Canadian Centre for Policy Alternatives

It has been 12 years since the Canada-U.S. Free Trade Agreement was implemented and seven years since it was renegotiated, extended to Mexico, and renamed NAFTA, the North American Free Trade Agreement. And NAFTA is now the template for the Free Trade Area of the Americas (FTAA) initiative), for which presidents and prime ministers from the hemisphere were scheduled to meet in Quebec City in April 2001 to set a course for its completion by 2005.[1]

"[F]ree trade agreements are designed to force adjustments on our societies," says Donald Johnston, former Liberal government minister and head of the Organization for Economic Cooperation and Development (quoted in Crane 1997a). His words display a candor rare among free trade proponents. Indeed, major adjustments have taken place in the Canadian economic and social landscape since the government promised a new dawn of prosperity in 1989, when the FTA went into effect:

- Trade with the U.S. has expanded dramatically during these 12 years. Exports are now equivalent to 40% of gross domestic product, up from 25% in 1989. (More than half of Canadian manufacturing output now flows south of the border, and Canadian producers account for less than half of domestic demand). This north-south trade boom has been mirrored by a relative decline in trade within Canada. Trade has also become more concentrated with the U.S.—from 74% to 85% of exports—and less concentrated with the rest of the world. Two-way investment flows have also increased greatly. Both Canadian foreign direct investment and portfolio flows to the U.S. grew much faster than did U.S. flows to Canada during this period.

- Growth performance in the 1990s was worse than in any other decade of the last century except the 1930s. Average per capita income fell steadily in the first seven years of the decade and only regained 1989 levels by 1999. By comparison, per capita income in the U.S. grew 14% during this period (Sharpe 2000).

- Canada has become a noticeably more unequal society in the free trade era. Real incomes declined for the large majority of Canadians in the 1990s; they increased only for the top fifth. Employment became more insecure and the social safety net frayed.

- While productivity has grown—rapidly in some sectors—wages have not, a trend mirroring the delinking that has taken place in the U.S. But the overall productivity gap with the U.S. has not narrowed as free trade proponents predicted; rather, it has widened recently.

- Successive waves of corporate restructuring—bankruptcies, mergers, takeovers, and downsizing—have been accompanied by public sector restructuring—downsizing, deregulation, privatization, and offloading of state responsibilities. Public sector spending and employment have declined sharply, and publicly owned enterprises in strategic sectors such as energy and transportation have been transferred *en masse* to the private sector.

FTA and NAFTA boosters did not promise vague social adjustments, however; they sold the agreements based on rising productivity and rising incomes. By this standard the treaties have clearly not delivered, and their proponents can only offer the weak defense that things would have been worse in the absence of the agreements. Workers and policy makers in the FTAA countries may want to take the Canadian experience into account before buying into these unproved promises.

The Canadian labor market during the free trade era

As noted above, exports to the U.S. have grown rapidly during the FTA/NAFTA era. Imports from the U.S. have also grown but not as quickly, resulting in a growing trade surplus (**Figure 3-A**).[2] The average annual trade surplus was $C19.7 billion during the 1990s, more than double the $C9.4 billion average in the 1980s. Canada's current account surplus with the U.S., which includes net payments to U.S. investors, was also positive albeit much lower, averaging $C6 billion annually. Here too, though, it was a lot higher than in the 1980s when the bilateral current account was roughly in balance.

Manufacturing employment bore the brunt of corporate restructuring, most severely in the first wave (1989-93), falling by 414,000 or 20% of the workforce. (The number of manufacturing establishments fell by 19% during 1988-95). High-tariff sectors were especially hard hit—leather experienced a 48% drop in employment, clothing 31%, primary textiles 32%, and furniture 39%. But employment was also slashed in medium-tariff sectors such as machinery (32%) and electrical and electronic products (28%). By the end of the decade manufacturing employment was still 6% below its 1989 level. Employment in clothing, for example, was still 26% below 1989, and electrical/electronics was down 19%. Wages were flat or falling even in the so-called winning export sectors.

Unemployment in the 1990s averaged 9.6% compared to the U.S. rate of 5.8%—a doubling of the gap compared to the 1980s (Sharpe 2000). This level of unemployment was higher than in any other decade since the 1930s. While average worker earnings were stagnant, casualized (or nonstandard) employment exploded, as people struggled to cope during the prolonged slump and restructuring.

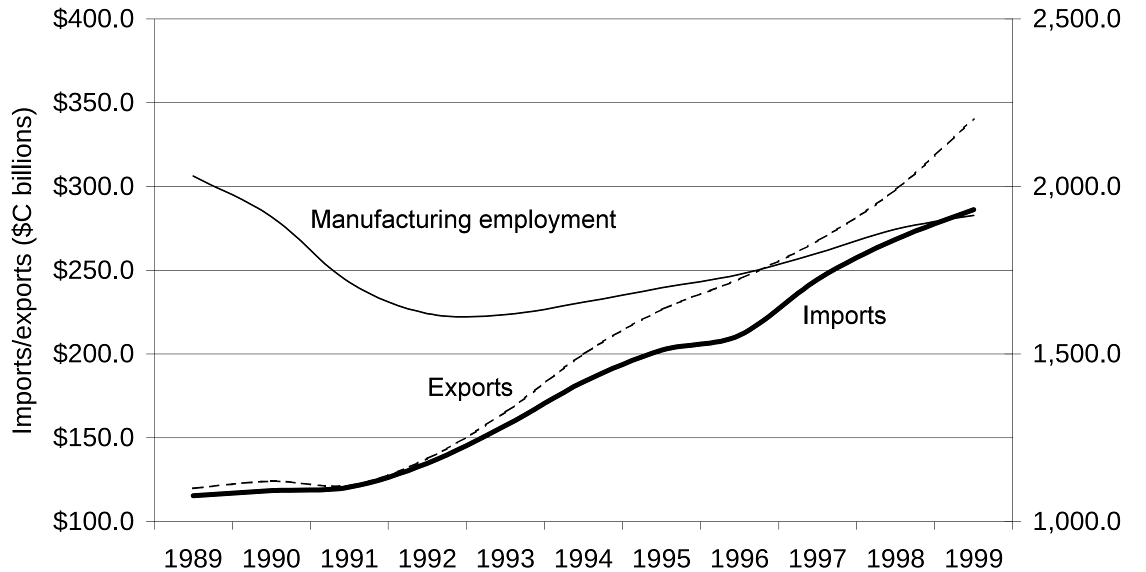
Paid full-time employment growth for most of the decade was almost nonexistent (Jackson and Robinson 2000). The absolute number of full-time jobs did not recover its 1989 level until 1998. Self-employment skyrocketed, accounting for 43% of new job creation between 1989 and 1999. Part-time employment accounted for another 37% of net employment growth during 1989-99. More than half of this growth was involuntary—due to the inability of people (mainly women) to find full-time work. Temporary work grew from 5% to 12% of total employment during the first half of the decade. Labor force participation rates dropped sharply, and at the end of the decade they were still well below their 1989 rates.

Evidence that the trade expansion and economic integration under NAFTA have had adverse employment effects in Canada comes from the government itself, in the form of a little-known study commissioned by Industry Canada.

The authors, Dungan and Murphy (1999), found that, while business sector exports grew quickly, import growth also kept pace. At the same time, the import content per unit of exports also grew markedly, while the domestic content per unit of exports fell.

FIGURE 3-A

Canada-U.S. exports and imports and manufacturing employment



Source: Statistics Canada, Employment Earnings and Hourings, annual estimates 1987-99; Canada's Balance of Payments, first quarter 1997, third quarter 2000.

What did this mean for jobs? Employment (direct and indirect) in export industries rose from 19.6% of total business sector employment in 1989 to 28.3% in 1997. However, the rapid rise in imports displaced (or destroyed) even more employment. The job-displacing effect of imports rose steadily from an equivalent of 21.1% of total business employment in 1989 to 32.7% in 1997. The authors conclude: “imports are displacing ‘relatively’ more jobs than exports are adding” (Dungan and Murphy 1999).

What did this mean in terms of actual jobs created and destroyed? It is a simple matter to derive these numbers from Dungan and Murphy’s data (see **Figure 3-B**). The result is striking. Between 1989 and 1997, 870,700 export jobs were created, but during the same period 1,147,100 jobs were destroyed by imports. Thus, Canada’s trade boom resulted in a net destruction of 276,000 jobs.

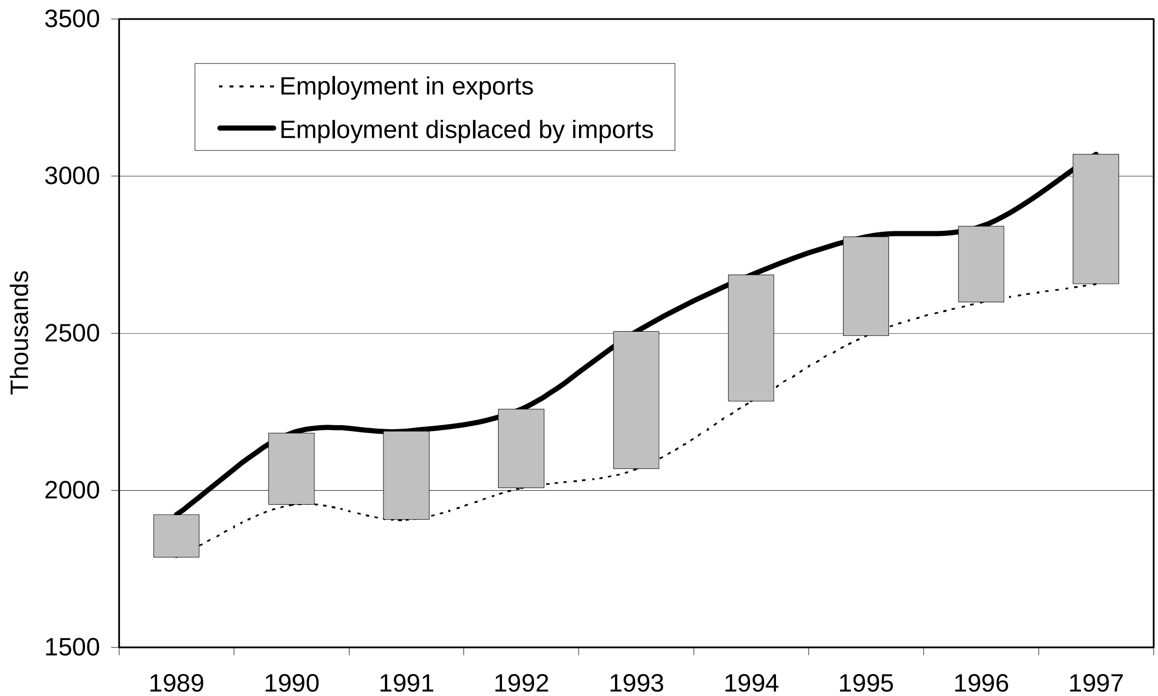
With this evidence, we can say more convincingly than ever that the conventional wisdom propagated by the business and political elites—that the trade expansion under NAFTA has meant a jobs bonanza for Canada—is false. On the contrary, trade expansion caused, at least in the first eight years of free trade, a major net *destruction* of jobs.

The study also found that the labor productivity of the jobs displaced by imports was moderately lower than that of exports, though the productivity of these displaced jobs was still higher than the average productivity level for the business sector as a whole. This the authors see as beneficial for the economy as whole.

However, the positive spin on the study’s findings is premised on the existence of macroeconomic policies whose priority is creating full employment conditions and on the expectation that displaced workers will find other jobs, and that those jobs will be at higher levels of productivity income. There are

FIGURE 3-B

Employment in exports vs. employment displaced by imports, 1989-97



Source: Dungan and Murphy (1999).

three problems with these assumptions. First, it is not clear that these displaced workers are, by and large, finding higher productivity jobs elsewhere in the economy. In fact, to the extent that they are finding jobs outside the tradable sector, the jobs they find are likely at lower levels of productivity. Second, workers both in the tradable sectors and in the economy generally have not seen productivity growth translate into income gains. Third, and most importantly, macroeconomic policy in the 1990s (as will be described shortly) has not focused on employment creation. Rather, policy makers have focused on ultra low inflation and wage control to enhance business competitiveness under NAFTA. Unemployment since the grim 1990s has lately fallen to around 7%, but this is still far above the 5.4% average unemployment rate for the entire three decades from 1950 to 1980.

As for incomes, market income collapsed for low-income earners and inequality widened, most strikingly during the first half of the decade. Market incomes of the bottom 10% of families with children fell an astounding 84% during 1990-96, and those of the next 10% fell 31% (Yalnizyan 1998). But the restructuring and the massive labor market failure was offset by public transfers, keeping the overall distribution of income after taxes and transfers stable for a while. The consequent accumulation of fiscal deficits became politically unpalatable, though, and the government's ensuing "war on the deficit" provided the rationale for the social cuts that resulted in a widening of overall income inequality in the latter half of the decade—the first such widening in the postwar era. (Inequality in Canada still remains much lower than in the United States.)

The top 20% of families increased their share of market income from 41.9% to 45.2% during 1989-98, while the bottom 20% saw their share drop from 3.8% to 3.l% (Robinson 2001). Even after taxes and transfers, the bottom 40% of families saw their inflation-adjusted income fall by close to 5% during 1989-98. The next 40% saw almost no change in their incomes. Only the top 20% saw a significant gain in per capita disposable income, an increase of 6.6%.

These have been difficult times for Canadian unions as well. The waves of layoffs and plant closures and the threat of closures in heavily unionized manufacturing sectors cut into their numbers: unionization rates in manufacturing fell from 35.0% to 33.4% during 1988-92. Years of defensive bargaining have resulted in unions' inability to appropriate a share of productivity increases for their members. This, too, signals an erosion of labor's bargaining power. And yet, despite the disastrous labor market conditions in manufacturing and throughout the economy, despite negative changes in labor laws and employment standards in some provinces, total union membership (not just in manufacturing) has remained remarkably stable: the overall unionization rate slipped only slightly from 32.0% of the paid workforce in 1987 to 30.7% in 1998 (Jackson and Robinson 2000).

NAFTA's role

To what extent should NAFTA take credit (or blame) for these changes? It is impossible to examine NAFTA in isolation from the broad anti-government and pro-deregulation policy agenda that has for the last two decades been transforming national economies and restructuring the roles and relationships among governments, markets, and citizens in the push to create an integrated global market economy. As a cornerstone of this well-known neoliberal family of policies—privatization, deregulation, investment and trade liberalization, public sector cutbacks, tax cuts, and monetary austerity—NAFTA has made it easier for Canadian policy makers to bring about a "structural adjustment" of the economy in line with the dominant U.S. model. Advancing and entrenching these policies in a treaty has secured investor rights, reined in interventionist government impulses and bargaining table demands of labor, and provided insurance against future governments' backsliding.

These policies have had, with some exceptions, an adverse impact on the employment and income conditions of working people in Canada. This is not an unintended consequence since, in essence, these policies transfer power from workers to management and investors, from wages to profits, from the public sector to the market.

But assessing causality is a complex task. Outcomes are the result of policies interacting with each other in mutually reinforcing ways. They are shaped by technological forces, corporate strategies, and a varied landscape of social and labor market institutions. NAFTA and its siblings have put downward pressure on employment and income conditions, but their impact varies from country to country, from sector to sector, from province to province depending on the strength of social and labor market institutions and the commitment of governments to either counter or reinforce these pressures. To be sure, policy choices do exist, but their range is more constrained, and with each turn of the "free market" screw the NAFTA legal framework makes it more difficult and often impossible to go in the other direction. For all these reasons isolating NAFTA impacts is exceedingly difficult.

The key provisions of the agreement itself that directly or indirectly affect product or labor markets are a good place to start. NAFTA removes tariffs and other non-tariff barriers on all goods and services, thus impeding governments' ability to protect strategic or vulnerable sectors from import competition. These tariff restrictions also prevent governments from granting tariff or duty waivers to foreign multinationals in exchange for commitments to strengthen domestic capacity and employment.

NAFTA's most important provisions apply to investment. The treaty entrenches a set of rules protecting private property rights of investors, and virtually all types of ownership interests, financial or non-financial, direct or indirect, actual or potential, are covered. NAFTA liberalizes investment, enhancing its ability to operate less hampered by non-commercial considerations and reducing the risk of future governments unilaterally imposing new conditions on investment.

The very broad national treatment provisions of NAFTA oblige each member country to treat foreign investors exactly the same as it treats its own national investors, regardless of their contribution to the national economy. These provisions create an impetus for powerful alliances between foreign and domestically owned businesses to promote further deregulation and resist new regulation, since any policy to regulate foreign capital has to be applied equally to national capital. They remove important industrial policy tools, from local sourcing to technology transfer—tools that seek to channel foreign investment to strengthen domestic industrial capacity, create jobs, etc.

NAFTA prevents governments from regulating the outflow as well as the inflow of capital. It prevents governments from placing restrictions on any kind of cross-border financial transfer, including profits, dividends, royalties, fees, proceeds of sale of an investment, and payments on loans to subsidiaries. It also prevents governments from restricting the transfer of physical assets and technologies. While NAFTA claims to break down international protections and barriers, it provides strong intellectual property protection (patent, copyright, trademark, etc.) for corporations' technology. This is another instance of taking power out of the public realm and empowering corporations.

NAFTA limits the ability of state-owned enterprises to operate in ways that are inconsistent with commercial practice and in ways that impair benefits expected by private investors of the other NAFTA countries. This clearly affects the ability of public enterprises to pursue public policy goals that may override commercial goals. It also limits the ability of future governments to re-regulate or re-nationalize industries once they have been deregulated or privatized. It provides the legal framework for greater private penetration into traditionally public areas, notably health care and education.

Finally, NAFTA guarantees investors the right to prompt compensation at "fair market value" for measures that are deemed to be "tantamount to expropriation"—a vague term for measures that are seen in some way to impair commercial benefits, including any future benefits that might be expected. Claims under these and other provisions may be adjudicated through various dispute panels, including an investor-state disputes tribunal, where in recent years a flurry of corporate challenges have forced governments to reverse policy decisions. The likelihood of these kinds of challenges is putting a chill on any policy or regulation that might be perceived as an infringement of investor rights.

Under these rules of continental integration, considerations of competitiveness tend to trump all other policy considerations. In Canada this dynamic has had three major impacts:

- *Corporations cut costs, restructure.* On the corporate level, Canadian companies rationalize their cost cutting and restructuring through takeovers, downsizing, closure, and relocations as the only means to stay competitive against their NAFTA partners. Increased competition also intensifies the pressure on employers to demand worker concessions. Workers (except certain elite categories) are legally confined by national borders. Capital has the upper hand, since it can move more easily under the new regime or threaten to move if labor does not make wage and other concessions. It also increases the pressure to lower costs through production and work reorganization, leading to the increased use of part-time, temporary, and contract workers and outsourcing to non-union firms in low-wage jurisdictions.

- *The government adds corporate breaks, drops worker and environmental protections.* The Canadian government is shifting its fiscal and regulatory policies in order to be more competitive under NAFTA. This translates to raising subsidies while lowering taxes, regulations, and standards to maintain and attract investment. There are no *common* rules governing acceptable and unacceptable subsidies or limiting subsidy wars among governments. And labor and environmental side agreements, which purport to limit the competitive bidding-down of labor and environmental regulations, are ineffectual. Policy levers such as performance requirements and (conditional) tariffs, which aim to nudge investors in accordance with public policy priorities, have been largely removed. Thus, the need to provide incentives to attract investment has created dual stresses—downward pressure on regulations and upward pressure on government spending.

- *Macro policy tilts to capital, away from labor.* The macroeconomic policy priorities and choices, especially on the issue of wage control, changed under NAFTA. They have included disciplining labor through monetary policy austerity, reducing government income supports—notably unemployment insurance and other social program spending—and lowering corporate and personal taxes. As a result the wages and well-being of Canadian workers are declining.

The last point requires further explanation, since the connection between macroeconomic policy and NAFTA is not usually made (Jackson 1999).[3] Most economists agree that the great Canadian slump of the 1990s was caused mainly by bad macroeconomic policy choices—first by severe monetary tightening, which coincided with the implementation of the bilateral FTA, and later in the decade by fiscal retrenchment, which, according to the OECD, was the harshest of any industrial country in the postwar era. At its peak in 1990, short-term interest rates were five points above U.S. rates. The massive federal spending cuts began in 1995 and over four years cut spending from 16% to 11% of GDP, the lowest level since the late 1930s. Program spending at all levels of government fell from 45% to less than 35% of GDP during 1992-99, an unprecedented structural shift in the public-private sector balance (Stanford and Brown 2000).

Many economists look at this disastrous economic record as the consequence of macro-policy error. The NAFTA-induced structural changes have been largely ignored. Were policy makers—in both the Mulroney and Chretien regimes—simply incompetent, or were they acting out of conviction that the top priority was to administer a structural jolt to the economy in order to enhance the conditions for Canadian business competitiveness?

Monetary policy in the late 1980s and early 1990s was driven by the determination of monetary authorities to virtually eliminate inflation from the Canadian economy (which at the time was roughly the same as U.S. inflation and thus was not a problem). Canadian authorities were also concerned about falling labor cost competitiveness with U.S. manufacturing as Canada entered free trade. Productivity was growing more slowly, and real wages were growing faster, than in the U.S. These wage increases were certainly justified by productivity increases, but in the de-unionized United States, wages were rising more slowly than productivity.

Policy makers also believed that a major fiscal adjustment was required to bring Canadian social programs and policies into line as integration with the U.S. proceeded. A 1996 report from the government's Privy Council Office noted: "the basic affordability of the [social safety net] system and the benefits payment regime has a direct consequence on competitiveness.…By raising the cost of labour as a productive input, such programs can either drive jobs south or encourage further substitution of capital for labour" (Privy Council Office 1997).

Thus, the Bank of Canada deliberately raised unemployment to discipline labor. The federal government later massively cut unemployment insurance programs and welfare transfers to (in its view) strengthen the incentive to work and enhance labor market flexibility. (The deep recession-induced deficits were the main justification to the general public for the social cuts that followed). As the unemployment insurance changes kicked in, the proportion of the unemployed collecting benefits dropped dramatically, from 75% in 1990 to 36% in 2000 (Canadian Labor Congress 1999), essentially the same as the U.S. level (37% in 2000; Mishel et al. 2001). Though monetary tightening (punishing interest rates and an overvalued Canadian dollar) would have short-term negative consequences for the economy, including a deterioration in competitiveness, policy makers believed it would, along with the fiscal adjustments, accelerate the necessary restructuring and strengthen the long-term competitiveness of Canadian business in the new North America.

The bulk of the social program destruction was implemented by 1997, and with the budget balanced, the government began the second phase of the fiscal adjustment—corporate and upper-end income tax cuts. In 2000, the finance minister announced tax cuts totaling more than $100 billion over five years.[4] Canadians are far enough along now in this adventure to answer the question: "Have the FTA and NAFTA delivered the goods that were promised?" The answer depends on who you ask. For those who wanted to diminish the role of government as an active player in the economy and provider of collective social protections, and for those whose wanted to improve the environment for business competitiveness by disciplining wages, NAFTA and its predecessor have been a success.

But in the public debate that preceded implementation of the free trade deal, delivering the goods, according to proponents, meant rising productivity levels and rising incomes. It meant ushering in a golden age of prosperity for all Canadians. That was the promise to the Canadian public. The answer here is clearly no.

The Canadian employment situation has unquestionably improved in the last two years, though workers have yet to reap any benefits in terms of improved earnings. However, with the erosion of their social protections Canadians have become more dependent on the private labor market than at any time in the last 40 years. As one observer put it, workers are now flying without a net (Stanford and Brown 2000). As the economy slows in 2001, this employment resurgence may prove to be short-lived, and the future for Canadian workers is once again clouded.

Endnotes

1. Data cited in this paper are drawn directly or indirectly from various Statistics Canada documents*: Labour Force Survey, Employment Earnings and Hours, Canada's Balance of Payments, Survey of Consumer Finances, Income Distribution by Size,* and *Canadian Economic Observer.*

2. Despite the dramatic increase in the share of total economic output accounted for by exports, the share of total employment accounted for by exports grew much more slowly (Dungan and Murphy 1999), due mainly to the increased import content of exports. Dungan and Murphy also observe that there was almost no growth in labor productivity in the export sector. It should also be noted that the proportion of imported inputs in Canadian exports is much higher than the proportion of imported inputs in American exports.

3. Andrew Jackson (1999) was the first to make the connection between macroeconomic policy and NAFTA.

4. Whether the Canadian government made a specific commitment to the Americans in response to congressional pressure to raise the value of the Canadian dollar relative to the U.S. dollar is not known. However, the Bank of Canada's raising of short-term interest rates had the effect of pushing the Canadian dollar to a peak of 89 cents in 1990.

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