Peterson Perspectives
Interviews on Current Issues

Edited Transcript

Episode 1: Renegotiation of NAFTA: Economic Implications and Political Risk

Gary Clyde Hufbauer assesses what Canada and Mexico would seek in any NAFTA renegotiation and what the economic effects of any new labor standards introduced by the United States would be.

Sherman Katz: Welcome to the first Peterson Perspectives interview on current international economic topics. The Peterson Institute for International Economics is a private, nonprofit, and nonpartisan research institute devoted to the study of international economic policy. Since 1981, the Institute has provided timely and objective analysis of, and concrete solutions to, a wide range of international economic problems. It is one of the very few economic think tanks widely regarded as nonpartisan by the press and neutral by the congress. This is the first in the series of biweekly interviews to be posted on our website with the senior fellows of the Institute to help share with you their views on emerging international economic issues in the news. These senior fellows produce the books, policy analysis, policy briefs, and working papers that are the heart and soul of the Institute's work.

Today we are pleased to present the Peterson perspective of Gary Hufbauer, Reginald Jones senior fellow, on the latest developments regarding NAFTA, an area that has been much in the news thanks to this year's presidential campaign. For the past sixteen years, Gary has been the leader in the institute's efforts to understand the NAFTA debate, and to analyze the economic impact of the NAFTA agreement itself. In 1992, Gary coauthored with Jeffrey Schott *North American Free Trade, Issues and Recommendations*, a book that examined the problems that would need to be addressed in a NAFTA deal. One year later, after the NAFTA negotiations concluded, Gary coauthored *NAFTA: An Assessment*, which analyzed the completed agreement including the side accords on labor and the environment. Twelve years later in 2005, Gary coauthored, also with Jeffrey Schott, *NAFTA Revisited: Achievements and Challenges*. This book compared actual experience in NAFTA's first ten years with both the objectives of the agreement's supporters and the charges of its critics. Gary's full bio, of course, appears in our website. Gary, welcome and thanks very much for joining us today.

Gary Hufbauer: Thank you.

Sherman Katz: Let's begin with this presidential campaign and the way it has highlighted the NAFTA issue. At a recent presidential campaign debate, Senators Hillary Clinton and Barack Obama both said that, if elected, they would seek to renegotiate the NAFTA agreement to incorporate stronger labor and environment provisions in the text of the agreement itself. How practical is that proposal?

Gary Hufbauer: Presidential debates are often more poetry than prose. So let's try to cut down to what is possible. Certainly, it would be possible to put in the kind of provisions that the United States negotiated in the agreement with Peru—which has been ratified by Congress—which included the so-called International Labor Organization Fundamental Principles of Rights at Work, and that enunciates four or five fundamental principles, and that could be included. I'm not sure that the people listening to the presidential debate had that technical vision in mind. Probably what they had in mind was more effective arbitration of environmental and labor disputes between the United States and Mexico, United States and Canada, and possibly between Canada and Mexico. And we might put in more effective arbitration provisions that would cover some of these issues, but we have to remember that if we do that, they will affect labor laws and environmental laws in the United States as well as in our neighboring countries. And that's where the rubber hits the road in the presidential rhetoric, because when you start thinking about changing or affecting the interpretation of US law through an international agreement, NAFTA, a lot of nervousness will be created even amongst NAFTA supporters, so I think that's where practical limits will arise in implementing these suggestions.

Sherman Katz: If we ask to renegotiate, do you think Canada and Mexico would want to reopen sensitive parts of the agreement as well?

Gary Hufbauer: Well, they would, and just sticking with the environmental issues, both Canada and Mexico have environmental complaints about what's happening in the United States. For a long time, Canada has been unhappy with what's happening with the Great Lakes—we have a Great Lake Mutual Compact System to monitor the quality of water—but Canada would like more to be done. Mexico would like more to be done in the quality of the Rio Grande and Colorado Rivers, which do flow into Mexico, and there would be other issues as well, just in the environment. On the labor issues, it wouldn't surprise me that Mexico would think that Mexicans who had been deported back into Mexico, who had been working in the United States, might have some claim to social security payments, for example, possibly other payments as well. They might want to include those things. So you get into a lot of sensitive issues very quickly, but Canada and Mexico would certainly have their wish list.

Sherman Katz: What about energy? Didn't we fight long and hard in the negotiations to get a special provision with Canada so that in case of a shortfall in energy in the United States, we could turn to Canada with the guarantee that they would treat us with the same preference that they treat Canadians?

Gary Hufbauer: Absolutely, we did. That was a provision, and the legal text is—as a lawyer like yourself would say, Sherman—a little squishy. But it's there and it does represent an obligation, a good-faith obligation by Canada. We would like to have the same obligation with Mexico, we don't have it, but unknown to many people in the United States, Canada is, by far, the largest energy supplier to the United States—natural gas, oil, electricity, all of these—they're a tremendous supplier, and we want them to continue to supply, we want them to continue to invest, and the worst thing that could be done in NAFTA would be to create a hostile environment to make Canada feel that it should pull back on the energy supply issue where cooperation has, in fact, been terrific.

Sherman Katz: And hasn't their Prime Minister, Steven Harper, implied, although he hasn't directly stated, that if we were to try to renegotiate that he would want to look at that provision again

Gary Hufbauer: Yes, he did say that. It was kind of an arrow across the bow. He's very friendly to the United States. I think he was just warning that it was a two-way street here, and Alberta is investing terrifically in the tar sands, building natural gas pipelines and so forth. Hydroelectricity is flowing down every day and don't take us for granted. That was basically what Prime Minister Harper was saying. Don't think that the United States is the only country which has issues that would like to open in NAFTA. And let me just mention an issue which has not come up in our own presidential debates, but every time I go to Canada it's a very big one: They think that our security restrictions at the border are quite harmful to investment in Canada, to the free flow of people and of goods back and forth across the border; which they feel hurts their economy much more than it hurts our economy.

Sherman Katz: And don't we import energy resources from Mexico as well?

Gary Hufbauer: Well, we do import from Mexico, we also export to Mexico; it's two-way trade. The problem with Mexico on the energy front is that Mexico is not investing enough in its own resources and in fact, is on the way to becoming a net energy importer, hard to believe, but it's on that path. And the president of Mexico, President Calderon, as his predecessor President Fox, recognizes this problem, wants to do more about it…there's a very nationalistic attitude towards energy in Mexico, but cooperation could, in fact, hopefully lead to an increase in both oil and gas production in Mexico. But again, it's going to take cooperation.

Sherman Katz: Let's come back to the intended effect of renegotiation that senators Clinton and Obama are talking about. There's an assumption, of course, that NAFTA in some way, shape, or form, is causing either job losses or lower wages in the United States. Is that true? And if we did put into place stronger provisions on labor, what impact would that have?

Gary Hufbauer: Well, this has been one of the key debates over the years. We'd be going right back to 1993—and everyone remembers Ross Perot and his image of the great sucking sound—all investments going to Mexico and jobs going to Mexico, and so forth. And the debates have raged on and on for the last 15 years now. In our view, the debate is completely misguided. Let me just throw out a few numbers. Back in 1993, the unemployment rate was about 7 percent in the United States. I know, right now, we are going through hard times because of the subprime crisis, nobody blames that on NAFTA, I would hope. But our unemployment rate is still below 5 percent, it's about 4.8 percent. So here we've had around 15 years of really very good overall performance of the US economy. Sure, we've had our ups and downs. But if we've lost so many jobs, why has unemployment gone down? What happens in the US economy every year is that about 16 to 17 million jobs turn over either because, people leave those jobs, or sometimes, a whole factory closes down and they're dislocated. But at the same time, every year, we create 18 to 19 million jobs, so we have a net job gain of about two million jobs per year. That was the case through the Clinton years and it's also been the case through the Bush years. People move in this economy. Now, if we didn't want that movement to happen, General Motors would still have half the US car market, Bethlehem steel would still be producing steel, and you can go on and on about the lack of change or the absence of change; we'd still be producing mechanical calculators. And I could then go back to the buggy-whip story; we'd still be making lots of carriages and buggy whips if we didn't have this turnover of jobs. So that is a vital part of the US economy.

NAFTA is a very small part of this much bigger story. But somehow NAFTA has been blamed, not only for what's happening in NAFTA, but also what's happening in the whole global economy and because of technology. So NAFTA has been demonized to an amazing extent. There's no time in this short program to be going into the arithmetic, but my colleagues and I completely disagree with the figure which was thrown out in one of the debates, that NAFTA is responsible for the loss of a million jobs. That phrase, "loss of a million jobs" suggests that a million are now permanently out of work, who otherwise would have had work. That's just not happened. What has happened is maybe every year, 50,000 to 60,000 people change their jobs because of NAFTA, and we have programs to deal with people who have to change their jobs. We have programs that are not good enough, but the metaphor of jobs lost on account of NAFTA is misleading to the American public.

Sherman Katz: Let's turn to the other side of the balance sheet. What would you say are some of the good effects that may be hard to identify from NAFTA? How does it help the country overall and, if you can say, how does it help individuals in particular?

Gary Hufbauer: This is where I would say people on my side of the debate have a hard time. It's easy to point to somebody who has lost his job and is now unemployed and there is some trade taking place, and then leap to the accusation that it's NAFTA. You have a real person, a live person, and he can be photographed, and you can write a story about him in the newspaper or interview him or her. In terms of the gains games on the other side of the picture, they are harder to picture, and in each case they are smaller. So I'm going to name some of them. But they cut across, literally, millions of people whereas the anecdotes about jobs lost tend to be individuals or individual factories.

Mangoes: you know, 15 years ago, ask yourself, did you eat mangoes? Well, if you did, you were a pretty affluent person who could afford mangoes. We didn't have them. Now they're in the grocery stores everywhere. Avocadoes are much cheaper than they were. Both come from Mexico. What else? Undershirts, undergarments of all kinds… a lot of clothing is cheaper in Wal-Mart today than it was 15 years ago, thanks to NAFTA. Now those are items that I guess many people come in contact with on a daily basis. There's also, of course, a lot of electronics which you don't see in your car. Electronics that move your car or the seat—the frame of the seat—have come from Mexico or Canada, and are cheaper than they otherwise would have been. So you can go through those examples, and while each one of them is small, they can't be dismissed in the aggregate. It's a lot of little pebbles across the whole economy. Now when we try to do the numbers on this, our estimate is that about $200 per person in the United States, or $600, let's say, roughly per household, is the payoff in terms of either more productive work or lower cost on account of NAFTA. That's not "nothing," I mean, that's something. I'm not saying it's the biggest thing in the economy, but it's certainly a significant payoff. And it's not only the products I mentioned, but it's also being much more efficient in producing a lot of other products. Let me just throw out one more example, and that's cement. There's a very good Mexican cement company which is doing a lot of business in the United States now, and has really made cement cheaper more efficiently than the companies it has replaced.

Sherman Katz: If we had new provisions on labor and required Mexico—as you said we did with Peru—to incorporate the core labor standards, right to organize, bargain collectively, no child labor, no forced labor, I appreciate you haven't done the research on this to date, but what would you suggest people consider as they think about how long it would take any such effects in Mexican economy, that is, more unions and so on and so forth, to have an economic impact on workers back in the United States?

Gary Hufbauer: Well, it would be a very indirect and slow impact. I think it would have benefits in Mexico if you had NAFTA arbitration of genuine complaints where there's child labor or forced labor, let's say, very long working hours, 10 to 12 hours a day, very bad working conditions. Worker unions are… very difficult to unionize by government interference. That would make a difference in Mexico, or at least to some Mexican workers. Would it make a difference back here in the United States? Well, I suppose to those people who are really concerned with conditions in Mexico, and there are quite a few people, now they would feel better about that, and that's a good thing. Would it make a difference to a worker in Ohio? Probably not, in terms of his pay packet, his benefits. The notion that working conditions in Mexico affect pay packets in Ohio—which I realize is widely believed has practically no economic, statistical, or other evidence; it's a belief you can't find evidence for. That doesn't mean people don't believe it, but let me try to give a counter example of just why it isn't so. If low wages and poor working conditions were such an attractive force for firms, they would all flood to Haiti. Compared to Mexico, Haiti is really cheap. Labor is about a third the cost in Haiti than it is in Mexico. It's not happening. Why not? Because of all the chaos:—the electricity isn't functioning, the police don't work, the judicial system doesn't work, and the roads aren't there and on and on—it's not very effective to produce in Haiti.

Well, similarly, in Mexico, Mexico is much better than Haiti, but Mexican working conditions, productivity, don't begin to compare to what's happening in Ohio. Let me just now throw out another number. The United States today, US firms today, have about $80 billion of investment in Mexico. That's the whole stock of investment: $80 billion. Each year, this same collection of US firms invests in the United States about $800 billion, that's each year. You know, if Mexico were the sucking sound, investment in Mexico would be much larger, but it isn't because there are just practical limits. The labor conditions would gradually improve in Mexico, as the economy gets better, but you can't legislate prosperity. It just can't be done; if it could be done, we would be all rich.

Sherman Katz: Gary, unfortunately, we're out of time, and we have to end this fascinating discussion with that answer. Thank you very much for making this auspicious beginning to the Peterson Perspective Interview Series on the website. For any listeners who wish to quote parts of this and future Peterson Perspectives, transcripts of the interviews will also be posted on our website. Of course, under applicable copyright laws, there can be no reproduction of any portion of this interview without permission from the Institute. And the views expressed here are those of the person being interviewed, but do not necessarily reflect the individual members of the Institute board or the Institute's advisory committees. Please join us soon for the next Peterson Perspective interview, and thanks for your attention to this one.