Past, Present and Future Economic Implications of NAFTA

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Major Paper presented to the Department of Economics of the University of Ottawa

In partial fulfillment of the requirements of the M.A. degree

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ECO 7997

Ottawa, Ontario, December 2002

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Introduction

Trade is the base of the very existence of human being. Since the beginning of human race people has been trading in order to survive. It has been evolving over the thousands of years taking various forms and having different types. Notion of "International Trade" was discovered a hundreds of years ago and was one of the main tools for countries to trade with each other and was very important in any given economy. In the 21st century international trade's inevitable role and importance in the rapidly globalizing world was more obvious then ever before. Countries modified their International Trade policies in order to keep up with the rest of the world, establishing various agreements, free trade zones and unions that would allow them to trade with each other with less obstacles and difficulties and impediments.

Among the developed countries of the world, U.S. and Canada are considered the largest and eighth largest economies in terms of Gross Domestic Product (GDP) respectively. In 1990 over $176 billion worth goods crossed the borders of these countries, providing millions of jobs both for Canada and U.S.

U.S. is considered the number one destination for Foreign Direct Investment (FDI), with $404 billion in FDI at the end of 1990. Canada, on the other hand, is the number one destination for U.S. FDI abroad, totaling $68 billion worth FDI in the beginning of 1990. Over one-fifth of Canada's five hundred largest industrial firms are predominantly owned by Americans. For their part, Canadians controlled $28 billion in direct investments in U.S., and Canadian companies provided over 500,000 jobs for American workers in the beginning of 1990. Over 400 million people were expected to benefit from NAFTA. It would cover more than 21.3 million square kilometers of territory (twice the area of 15-nation European Union), and combined GDP of 10 trillion dollars a year (in 1999).

Inevitably, U.S. and Canada came to a common agreement to establish Free Trade Agreement (FTA) that would allow them to trade on much wider scale and with less obstacles. FTA was implemented in 1989 and proved to be a successive trade agreement. It was followed by more sophisticated and expanded North American Free Trade Agreement in 1994 that included US's southern neighbor – Mexico.

This paper discusses the North American Free trade Agreement (NAFTA) enacted in North America among Canada, United States and Mexico. Although this Agreement involves numerous issues, I will concentrate on the following broad topics:

I will start with introduction to the topic of this paper. Then Chapter 1 takes a closer look at how the negotiations on NAFTA were performed, what were the issues discussed during the negotiations, and what were the each nation's hopes and expectations from NAFTA. Chapter 2 discusses the economic and particularly financial implications of NAFTA on the United States, Canada and Mexico. Chapter 3 will concentrate on some recent economic evaluations of NAFTA mostly with respect to Canada, and also present some thoughts from different publications and papers that evaluated NAFTA. The last Chapter 4 underlines the existing problems in NAFTA, and stresses out the ways to improve NAFTA in the future by presenting some future challenges and objectives from each NAFTA members' point of view and benefit. I will finish this paper with some conclusions and references.

Chapter 1. History: Negotiating the NAFTA

For neighbors and long time trading partners United States and Canada, agreements that would lead to more freedom in trade were considered of enormous importance. The "Free Trade Agreement" (FTA) was implemented with the purpose of easing trade conditions and eliminating different restrictions that existed between U.S. and Canada. FTA was not reached easily, governments at both sides were very cautious. But after many talks and negotiations Canada's Prime Minister Brian Mulroney and U.S. President Ronald Reagan signed Canada-U.S. Free Trade Agreement, which came into force on 1 January 1989. Although Canada and U.S. already had somewhat free access to each other's markets and economies, governments hoped that FTA would further liberalize trade polices and remove existing trade barriers in goods and services and in investment. It was believed in Canada that Canadian businesses would have much needed free access to the U.S. market and benefit from economies of scale.

Mexico on the other hand was struggling to get out of the debt recession of 1981-82. By heavily depending on oil exports, Mexico was suffering even more after sharp decline for oil prices and increase in interest rates. Recession almost doubled Mexico's fiscal debt that in turn led to rising inflation, larger current account deficit and loss of international reserves. Mexico's highly protected domestic market, import substitution policy, expansionary monetary and credit policies were not helping. Mexican government had to look for ways out of this situation; it was forced to ask International Monetary Fund (IMF) for loan to deal with its debt problem. IMF's loan came with some strings attached to it, such as reduction public spending, increase taxes and tighten its monetary policy. But that wasn't enough to improve the situation. Mexican authorities led by Presidents Miguel de la Madrid (1982-88) and Carlos Salinas (1988-94) began the process of liberalising the Mexican economy, removing restrictions on foreign investment and privatising state enterprises. Mexico has joined General Agreement on Tariffs and Trade (GATT) in 1986 that allowed to lower maximum tariffs by 20 per cent and partially eliminated import licences[1]. But still Mexico was unattractive for foreign

[1] See Maryse Robert (2000), "Negotiating NAFTA" page 26.

businesses and investments. It started to realise that it had to liberalise its trade relationship with U.S. and Canada on much wider scale.

In World Economic Forum in Davos, Switzerland (1990), Mexican President Carlos Salinas and Secretary of Trade and Industrial Development Jamie Serra met several leaders of European states. They quickly realised that Europeans would not satisfy their desperate need for investment flows, and Mexico was being overshadowed by newly reforming countries of Eastern Europe. Fear was that the lack of foreign investment would bring higher domestic interest rates and increase burden of already heavy debt. Salinas and Serra decided to approach U.S. Trade Representative Carla Hills expressing their interest in possible bilateral free trade agreement with U.S., which was the biggest trade partner for Mexico (more than 60% of its exports and 2/3 of its imports). U.S. authorities shortly approved the idea and made first moves towards the official negotiations.

For Canada, news about a possible bilateral U.S. - Mexico free trade agreement came as a warning. Having a long trade history with U.S. and a relative joy from benefits of existing FTA, Canadians were concerned about the impact of bilateral U.S. - Mexico agreement on Canadian interests in U.S. market.

Canadian trade and investment ties with Latin American countries and particularly with Mexico were insignificant historically, providing little commercial interest to enter into free trade negotiations with Mexicans. But on the other hand, Canada did not want to be hurt in any way by Mexican competition in U.S. market. During his visit to Mexico in March of 1990, Canadian Prime Minister Brian Mulroney showed some interest in trilateral free trade agreement between U.S.-Mexico-Canada. But Canadians decided to analyze and consult its provinces regarding the impacts of bilateral U.S. - Mexico agreement on Canada first and then decide to get into negotiations with U.S. and Mexico or not. Prime Minister Brian Mulroney ordered internal examination of implications of bilateral agreement between U.S. and Mexico for Canada. Department of External affairs formed small task force headed by Robert Clark, which had to secure impact analyzes from variety of government departments like energy, mine and resources, agriculture, industry, science and technology. Areas like agriculture and textile were given extra attention by the task force due to possible stiff competition from Mexicans in U.S. market if trilateral agreement were to be implemented. However impact analyzes indicated that Mexican access to U.S. and Canadian markets posed little threat for Canada. In April of 1990, the task force completed a draft memorandum on the issue and submitted it to the cabinet in May. Memorandum suggested two options. The first is to do nothing and simply to monitor negotiation developments between U.S. and Mexico. Second option was active participation in exploratory discussions that would not make Canada to directly participate in negotiations. Cabinet chose the second option, and decided to further explore possible effects of U.S-Mexico FTA on Canada. As it became even clearer that Mexico and U.S. were fully determined to negotiate, Canadians realized that they could not stay out of these negotiations any longer. Priorities and Planning Committee of the Cabinet prepared a second memorandum this time suggesting four options for Canada: continue to monitor developments, seek observer status at bilateral Mexican-U.S. free trade agreement, negotiate bilateral Canada-Mexico free trade agreement or to join U.S. and Mexico in trilateral negotiations. After some thoughts and discussions in Department of External Affairs and in Department of Finance, Canada decided to join trilateral negotiations[2]. This decision was prompted mainly by a concern

[2] See M. A. Cameron and B. W. Tomlin (2000), "The Making of NAFTA". Pages 63-68.

that a separate bilateral Mexico-U.S. agreement could give U.S. advantage over Canada in terms of attracting investment, and U.S. being the only country with access to the continental market. U.S. and Mexico accepted Canada's decision to join.

Formal opening of negotiations of NAFTA happened on June 12, 1991 in Toronto. The ministers of three countries decided to divide the negotiations into six main areas: market access for goods, services, investment, intellectual property protection, dispute settlement mechanisms, and trade rules on subsidies, dumping and rules of origin. They also organized nineteen working groups to handle various issues within those six major areas. The leading departments in the negotiations were the U.S. Trade Representative (USTR), the Mexican Ministry of Commerce and Industrial Development (MMCID), and External Affairs and International Trade Canada (EAITC). Americans and Canadians relied on their departments and gave them responsibility for several other groups, twelve in case of U.S. and ten for Canada. Chief negotiators were Julius Katz for U.S., Herminio Blanco Mendoza for Mexico, and John Weekes for Canada. Their tasks were to deal with most difficult issues that constantly aroused during the negotiations.

Negotiators also made sure to include private sector of each of the countries. In Canada, business leaders were consulted through the International Trade Advisory Committee (ITAC) and Sectoral Advisory Groups of International Trade (SAGIT). In the U.S., seven policy advisory committees, thirty technical, sectoral and functional advisory committees, and the President's Advisory Committee for Trade Policy and Negotiations represented interests of business community of the U.S. for Mexico, private sector's interests were served through the Co-ordinator of Foreign Trade Business Organizations (CFTBO).

The first five months were spent to share the information and to get to know each other. Chief negotiators suggested that each country prepare a paper explaining its position and exchange it with its counterparts by the end of November of 1991. One of the main sessions was held in Dallas, Texas (17-21 February 1991) where approximately 400 negotiators gathered together in a session. They concentrated on areas that were close to resolution. Americans insisted that Mexico must open up their barriers more in order to get the deal. At the fifth ministerial meeting in Montreal in April of 1992, ministers acknowledged that they were making progress on most issues, but some areas needed more attention. Major disagreements were obvious in groups such as autos, energy, government procurements, investment and textiles. Being under US's pressure, Mexicans agreed to allow U.S. banks to set up branches in Mexico and to open all but fourteen petrochemical products to foreign investment to accept performance contracts. Canadians as well were showing great resistance in some areas, fearing that some changes to already set up Canada-U.S. FTA could harm Canadian interests in U.S. market. The main issues where Canadians could face stiff resistance from Americans were tariff-rate quota for wood, apparel, rules of origin in textiles and apparel, regional content value for autos, cultural industries, and government procurement. The issues of auto and lumber industry, which are one of the main sources of Canadian exports to the U.S., were given extra care in order to protect interests of producers in Canada.

Finally after hard work and some time countries were ready to ratify NAFTA. Canadians ratified it on June 23 1993. The U.S. House of Representatives approved it on 17 November 1993, followed by its Senate. Mexican Senate approved it on 23 November

1993[3]. Although, there were some issues left to be agreed on or changed, North American Free Trade Agreement came into effect on 1 January 1994.

Chapter 2. What was expected in terms of Economic Implications?

Each government had its objectives ready to present during the negotiations. Washington constantly mentioned that U.S. firms be allowed to enter into Canada's cultural industries like, publishing, film distribution and broadcasting sectors. Canadians on the other hand considered that their culture must be protected in order to keep it distinctive from U.S. But Americans kept on pushing for larger access for U.S. programming in Canadian cable companies. Washington also wanted the local content standards in the U.S.-Canada Auto Pact to be increased from 50 per cent to perhaps 70 per cent. In their opinion, this would make it for foreign automakers more difficult to qualify for duty-free access across Canada and U.S. American pharmaceutical industry was pushing to a revision of Canada's generic drug laws that limited patent protection to American firms. U.S. also wanted greater access for its banks to Canadian banking and financial systems, as well as to the beer and liquor industries. In their opinion NAFTA would allow U.S. manufacturers to take advantage of market specialization and lower Mexican wages to establish production-sharing arrangements and exploit economies of scale within North America[4].

Canadians also wanted access for its banks in the Mexican markets, relaxed government procurement codes, modification in the Jones Act governing U.S. maritime practices, removal or reduction of unilateral restraints by U.S. on softwood lumber imports, and also protection of Canada's cultural industries. Besides the insignificant

[3] See M. Robert (2000), "Negotiating NAFTA" pages 42-44.
[4] See J. A. McKinney (1992), "Implications of a North American Free Trade Region", pages 21-23

trade with Mexico (annual trade being only one one-hundredth the volume of annual trade with U.S.), Canadians believed that there were some opportunities for its businesses in Mexico.

Already, being third largest trading partner after Canada ($176 billion) and Japan ($138 billion), Mexico was benefiting from American attention. Transformation of Mexico, from relatively closed economy into a market-oriented economy, more than doubled US's exports to Mexico between 1986 and 1990, which created 320,000 new jobs in Mexico. The leading U.S. imports from Mexico in 1990 included oil and oil products worth $5.1 billion, electrical machinery worth $4.6 billion, motor vehicles worth $3.6 billion, etc. But clearly, all these changes were not nearly enough to improve Mexican economy substantially; Mexico's desires from NAFTA were almost countless. NAFTA was more likely make Mexico more attractive for foreign investment because it would guarantee firms secure and permanent access to tariff-free U.S. and Canadian markets. Even though most tariffs between U.S. and Mexico have been removed or reduced since Mexico joined GATT. Mexicans were highly protective of their energy industry. Despite a great need in investment and more openness in this market Mexicans considered this energy sector as a traditional one, which (in opinions of most Mexicans) have to be politically protected and mostly Mexican owned in the future. Sectors like; telecommunication, labour market and financial institution had also a central importance during the negotiations and were starving for more investment.

Main issues in NAFTA discussions were not whether capital be allowed to move, or whether Canada and U.S. should trade with Mexico, but the question was to how and under what circumstances trade and investment would take place. Table 1 illustrates increased trade generated from 1986 to 1992 between U.S. and Mexico and U.S. and Canada prior to implementation of NAFTA.

Table 1. U.S. Trade with Canada and Mexico (in billions of U.S. Dollars)

	1986	1987	1988	1989	1990	1991	1992
U.S. Trade with Canada	124	131	153	167	175	182	189
U.S. Trade with Mexico	30	35	44	52	59	64	75

Source: Department of Commerce, IMF, International Financial Statistics, 1992

From Table 1 it is clear that US's trade has been steadily increasing over the illustrated period. As one can see from Table 2, trade deficit between Canada and U.S. fell to $7,9 billion between 1988 and 1992. Canada experienced growth in trade deficit with Mexico, reaching almost $2 billion in 1992. U.S. had a positive trade balance with Mexico in 1992 when $5.4 billion more goods were exported to Mexico. Numbers of Table 1 and Table 2 suggest that Mexican market reforms were really working and attracting American attention.

Table 2. Trade Balances of Participating NAFTA countries (in billions of U.S. Dollars)

	1988	1989	1990	1991	1992
United States with Canada	-$11.7	-$11.3	-$10.8	-$8.6	-$7.9
United states with Mexico	-3.1	-2.6	-2.4	1.4	5.4
Canada with Mexico	-668. *	-909.0*	-995.0*	-1.7	-1.6

* In millions of dollars; *Source:* U.S. Department of Commerce, 1993

Primary fear for Americans and Canadians, with the implementation of NAFTA, was that most of the FDI would be attracted to Mexico because of the cheap labor costs. That in turn would lead to job losses in U.S. and Canada and increase Mexican exports. However, this argument ignored the fact that average productivity levels in Mexico are lower. They also ignored the role of exchange rate adjustment, should liberalized trade lead to persistent trade imbalances.

Nevertheless, according to Industry Canada, Mexico does seem to have a comparative advantage in low-skilled and low-value-added manufacturing. In effect, low-skilled Canadian and American workers will have to reallocate themselves into higher skill levels industries[5]. Of course, this transition would take some time, and in between, individual workers would be hurt, which might increase unemployment.

Even though Mexican markets were not totally isolated from international developments, Mexican financial markets were highly regulated prior to NAFTA, and foreign financial institutions were not allowed to operate in Mexico. Mexican government used to control interest rate level, and credit was directed to support government's strategy of import-substituting industrialization, which financially eroded competitive position of dominant financial institutions. Mexican government tried to improve the situation by nationalizing banking system, reducing financing requirements, and removing exchange rate controls.

These developments put Mexico into much better position to deal with the challenges that would likely appear in NAFTA. Considering the fact that these developments only took place just before the signature of the Agreement, monetary and financial implications of NAFTA were considered of greater importance for Mexico than either for Canada or U.S.

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[5] W. R. White (1994), "The Implications of the FTA and the NAFTA on Canada and Mexico." page 6.

All three members of NAFTA were expected to benefit from its provisions, which stimulate further integration of the financial sectors of these economies. Financial integration of this sort thought to bring more efficient allocation of capital across borders and more efficient financial services to consumers. Mexico will likely gain the most from the liberalization of international capital flows. Because Mexican financial system is underdeveloped. Statistically, there was approximately one bank branch per 2000 people in Canada and U.S.; the comparable figure in Mexico was 19,000 people. Access to insurance coverage and mortgages was also more restricted in Mexico. Therefore Mexican financial system would likely gain more from NAFTA than U.S. and Canada. NAFTA should bring competition between foreign and Mexican banks, and among foreign banks operating in Mexico.

Canada's advantage in Mexico might be the fact that both Canada and Mexico allow multibranching and universal banking. Canadians will have an opportunity to operate in Mexican market and compete against U.S. financial institutions as well. One example of this is Scotiabank that acquired a bank to offer a brokerage and other financial services in Mexico. In contrast, U.S. banks have the geographical advantage of proximity and a greater knowledge of local customs and the language.

Provisions of NAFTA were also expected to affect the monetary policy and exchange rate regimes. For highly integrated Canadian and U.S. short-term financial markets this effect will probably be minimum. But Mexican authorities put strong emphasis on structural reforms, fiscal restraint and the reduction of inflation through restrictive monetary policies. Inflation fell dramatically from 180 per cent in 1988 to 7.2 percent in 1994. Real exchange rate appreciated for about 25 per cent between 1990 and 1994. But it was not certain how much the nominal value of peso would fall. The establishment of an autonomous Bank of Mexico with a mandate to pursue price stability was expected to be of help.

Negotiations of NAFTA brought some thoughts about exchange rate regime changes among its members. As in the case of European Union some ideas about more fixed exchange rate system between U.S., Mexico and Canada were given some arguments. But in the case of NAFTA, circumstances were quite different. There was no a great desire towards some sort of economic union between NAFTA governments like it was in European Union. Despite some of the likely benefits (lower transaction costs, less uncertainty) from having relative fixed exchange rate regime, negotiators did not discuss anything like that because of the major differences in political views of its members. Moreover, such regimes can only exist when there is a relative wage similarity across countries; relatively labor mobility and economies should be a subject to the same shocks. Clearly these and some of the other conditions were not met in case of NAFTA and when it comes to labor movements, FTA and NAFTA were not to provide international labor mobility, they are trade agreements only.

While economic implications of NAFTA are yet to be seen in coming decades, it is evident that the process of continental, industrial restructuring has begun.

Chapter 3. Recent Evaluations:
Macro- and Micro -economic aspects

Since the implementation of NAFTA in 1994 economies of Canada, Mexico and United States has been reshaped to some degree. Designed to foster increased trade and investment among partners, NAFTA contains schedules for tariff elimination and reduction of non-tariff barriers, as well as provisions on the conduct of business in the free trade are. Although some tariffs remain in place in certain areas for products in

Canada's supply managed sectors (dairy and poultry), as well as sugar, dairy and cotton in the U.S.; as of the date, almost all tariffs on Canada-U.S. trade in originating goods were eliminated. Also NAFTA provides for nearly all tariffs to be removed on trade in originating goods between Canada and Mexico by January 1, 2003[6].

Although it is relatively early to evaluate the impact of NAFTA on the member countries, I will report some aggregate and sectoral indicators that may be useful in the analysis.

The growth of GDP is an important issue evaluated by economists in the three member countries. Growth in divergence of real per capita income in PPPs (Purchasing Price Parities), measured at prices of 1995, among three countries was monitored during the NAFTA years. First, Table 3 reports average growth trends in North America from 1970 to 2000 using purchasing price parities of 1995.

Table 3. Average growth trends in North America from 1997 to 2000 (in percentages)

	1970-2000	**1970-1994**	**1994-2000**
Average rate of growth of GDP in PPPs at prices of 1995			
Canada	**3.3**	**3.2**	**3.8**
Mexico	**4.0**	**4.1**	**3.5**
United States	**3.3**	**3.1**	**3.9**
Average rate of growth of GDP per capita in PPPs at prices of 1995			
Canada	**2.1**	**1.9**	**2.8**
Mexico	**1.6**	**1.5**	**2.1**
United States	**2.2**	**2.1**	**2.9**

Source: Duran (2002), "NAFTA Macroeconomics".

[6] See Department of Foreign Affairs and Intern. Tr., "NAFTA at Five years, a partnership at work" 1999.

From Table 3 we can see that average growth rate of GDP in PPPs at prices of 1995 for U.S. is the highest average growth rate that occurred during the NAFTA years, 3.9 percent, compared to the 1970-1994 period of 3.1 per cent. Overall Canadian growth rate for years 1970-2000 was 3.3 percent, the same in U.S. For Mexico average growth rate during the NAFTA years was smaller, 3.5 percent compared to 4.1 per cent of pre-NAFTA years 1970-1994, but the NAFTA period includes the so called "tequila crisis" of 1994-1995. For U.S. the numbers are 3.9 per cent during 1994-2000 and 3.1 per cent during 1970-1994. Similar pattern can be observed from Table 3 for average per capita growth of GDP for Canada and United States. For Mexico, although average growth of GDP fell during the NAFTA years from 4.1 per cent during 1970-1994 to 3.5 per cent during 1994-2000 period, average per capita growth of GDP has risen from 1.5 per cent to 2.1 per cent. If one compares this per capita growth between Canada and U.S. it is clear that Canadian per capita growth was less than that in U.S. (1.9 per cent in 1970-1994 compared to 2.1 per cent in U.S. for the same time, and 2.8 per cent compared to US`s 2.9 per cent during the same periods of time). In my view, these results are more of a favour to NAFTA`s positive impact on GDP growth than to a disfavouring it.

Second, it does seem that every sector of the Canadian economy benefited from the GDP growth. Table 4 illustrates this statement numerically.

Table 4. Growth rate of GDP at basic prices by industry (for the year 1997 numbers are in millions of constant Canadian and the rest is in percentage growth rates)

	1997	1998	1999	2000	2001
All industries[1]	816,808	3.9 %	5.2%	4.6%	1.3%
Goods-producing industries					
Agriculture, forestry, fishing and hunting	20,427	6.2%	6.5%	-1.0%	-7.3%
Mining and oil and gas extraction	33,935	1.5%	-1.6%	7.5%	1.6%
Manufacturing	142,282	4.9%	7.2%	5.4%	-4.6%
Construction industries	42,995	3.1%	4.9%	4.2%	3.8%
Utilities	26,685	-2.04%	2.1%	4.6%	-2.4%
Services-producing industries					
Transportation and warehousing	40,337	1.73%	5.5%	4.5%	-1.62%
Information and cultural industries	27,979	6.7%	13.6%	13.2%	9.8%
Wholesale trade	43,694	8.0%	7.4%	6.1%	1.9%
Retail trade	42,252	7.5%	5.2%	5.4%	3.8%
Finance and insurance, real estate and renting and leasing and management of companies and enterprises	161,097	3.1%	4.9%	3.8%	3.4%
Professional, scientific and technical services	30,289	12.3%	10.8%	10.1%	6.5%
Administrative and support, waste management and remediation services	15,386	6.7%	8.8%	7.8%	4.6%
Public administration	49,482	1.5%	1.6%	1.9%	3.4%
Educational services	42,314	0.6%	1.7%	0.5%	0.72%
Health care and social assistance	51,403	0.9%	2.5%	1.3%	2.0%
Arts, entertainment and recreation	7,405	2.6%	6.3%	5.2%	2.3%
Accommodation and food services	19,652	5.7%	3.4%	3.8%	2.8%
Other services (except public administration)	19,194	2.9%	3.2%	1.9%	3.2%

1.North American Industry classification Standard. Author's own calculations based on the following *Source: Statistics Canada*, http://www.statcan.ca/english/Pgdb/econ41.htm

As seen from above table on average all industries experienced growth. In 1998 GDP experienced 3.9% growth, from 816,808 millions of Canadian dollars in 1997 to 848,963 in 1998. In 1999 GDP growth was 5.2%, in 2000 the growth was 4.6%, and in 2001 it was 1.3%. If we look at particular industry, we can see that for example, agriculture, forestry, fishing and hunting industries grew from 20, 427 million in 1997 to 21,696 million, which is equivalent to 6.2% growth rate, afterwards they have experienced a slight decrease of 1.0% in 2000 and even more decrease of 7.3% in 2001.This decrease might have been prompted by growing Mexican competitions in agricultural sector in U.S. market.

Constant increase of output was observed in most other industries as well. For instance mining and oil and gas extraction industries also grew from 33,935 million in 1997 to 34,461 million of dollars in 1998, the equivalence of 1.5% increase. The highest growth rate for these industries was 7.5% increase in 1999, though their share of GDP increased for about 1.6% in 2001. Also from Table 4 we can see that almost all reported services-producing industries experienced constant growth during 1997-2001 period. One example is information and cultural industries that grew from 27,979 in 1997 to 29,866 in 1998, an increase of 6.7%. The highest growth rate for these industries was in 1999 when growth was equivalent to 13.6% increase.

Despite the slight decreases of sectoral GDP levels in some industries, these numbers again suggest that NAFTA has not badly hurt any industry in particular so far. All other industries (wholesale and retail trade, finance and insurance, educational services and etc.) have benefited during the NAFTA years by experiencing growth.

For NAFTA members, matters concerning labor force movements and creation of new jobs in NAFTA are also amongst the main priorities. Integration process that is taking place requires increase in employment that would absorb the increase in the labor force. For now full employment is not being reached. Canada is relatively a small population country, with a labor force of around 16 million people, while U.S. is the biggest among NAFTA members, with 142 million and Mexico with around 43 million people. Mexico's average population is much younger than its two northern members. Mexico's labor force is also growing at a fastest rate, it requires to create around 1.3 million of new jobs per year, in the U.S. it is 1.1 million and in Canada below 1 million a year. According to Duran (2002) one might expect that most jobs would be created in leading export sectors after the signature of NAFTA, but it was not the case in Mexico and United States. Their contributions in the States and Mexico were marginal. Out of the total created new jobs the leading sectors' share was only 2.81 per cent in the U.S., 0.77 per cent in Mexico while in Canada it was 20.51 per cent. In some cases leading export sectors had a negative impact on job creation, mainly in areas such as metal industries, industrial machinery and equipment clay and glass productions etc. in Mexico. In the States areas like paper production, chemicals, farms and transportation also suffered from job losses. Especially Mexican manufacturing industry has suffered massive job losses (181 thousand jobs) during the financial crisis in 1994-1995. Although Mexican labor market has recovered since February 1998, reaching the employment level beyond the April 1994 level, it is obvious that Mexico has to go further. It has only created 50 thousand new jobs since 1994. One of the problems in Mexico's manufacturing sector is the lack of productivity growth in traditional sectors that are falling behind the modernization and technological improvement. On top of everything, after the devaluation of Mexican peso in 1994, labor costs dropped dramatically and have not gone up since then. This might give Mexico comparative advantage in labor markets over the

U.S. and Canada, but at the same time it weakens the domestic market as well as overall NAFTA market. Other than that, three countries still tend to focus on one problem or on few commodities. The usual issues are drugs and immigration; the commodities are softwood lumber, sugar, fruit and vegetables. Also, NAFTA has contributed to employment increases in several Mexican industries, which in turn led to an output and productivity increases. While Mexican productivity level grew at about 3.3 percent a year during 1980s, during the NAFTA years this percentage increased to 5.8 percent a year, as mentioned by R.De la O (2002). Despite the provisions in NAFTA concerning the facilitation of labour force movements among its members, crossborder mobility is still restricted, especially this restriction is relatively high for low skilled Mexican workers compared to those in states and Canada. However, in the future this issue will have to be considered closely and seriously by each government. The reason is that as countries will experience further increase in financial integration, in trade and in investment flows among countries, labour immobility may slowdown the overall integration process and some of potential welfare benefits of people that they can get by easily moving into different economic regions in NAFTA.

Labour force indicators during the NAFTA years for Canada are much better compared to Mexico. As shown below in Table 5, for example, the number of employed people in 1997 was 13,774.4 thousand and in 1998 it has reached 14,140.4 thousand people, a growth of 2.6%. In 1999 increase was 2.7%, 2.6% in 2000 and 1.12% in 2001 respectively. Although, labour force has grown steadily since the signature of NAFTA, employment to population ratio has been mostly rising over the reported NAFTA years. Employment to population ratios are 59.0 percent in 1997, 59.7 percent in 1998 and 61.2 percent in 2001, a steady increase. Participation rate also increased from 64.9 percent in

1997 to 66.0 percent in 2001. In general unemployment level fell from 9.1 percent in 1997 to 7.2 percent in 2001. Although we can see from the Table 5 that this level has reached its minimum in 2000 when it was only 6.8 percent. All mentioned and other results are presented below in Table 5.

Table 5. Labour force characteristics for 1997-2001 period. (thousands of people in 1997 and for the years 1998-2001 in percentage forms)

	1997	1998	1999	2000	2001
	Thousands		Percentages		
Population 15 years and over	23,359.3	1.3%	1.2%	1.3%	1.3%
Labour force	15,153.0	1.7%	2.0%	1.8%	1.5%
Employed	13,774.4	2.6%	2.7%	2.6%	1.12%
Full time	11,139.7	2.9%	3.3%	3.0%	1.12%
Part time	2,634.8	1.4%	0.3%	0.7%	1.1%
Unemployed	1,378.6	-7.3%	-6.8%	-0.8%	7.3%
Not in the labour force	8,206.3	0.5%	-0.006%	0.4%	1.0%
Actual hours worked	471,023.4	1.7%	3.6%	3.3%	-0.88%
In percentage terms					
Employment to population ratio	59.0%	59.7%	60.6%	61.4%	61.2%
Participation rate	64.9%	65.1%	65.6%	65.9%	66.0%
Unemployment rate	9.1%	8.3%	7.6%	6.8%	7.2%
Author's calculations based on the following *Source*: Statistics Canada: http://www.statcan.ca/english/Pgdb/econ10.htm					

Exchange rate and price stability was also of concern during the NAFTA years. Prices behavior has been more stable in U.S. and Canada compared to Mexico. Instability in Mexican case can be explained with the fact that Mexico's economy is still subject to large structural reforms on the supply side, so that prices have to adjust more than in Canada or in U.S. Since NAFTA's implementation real effective exchange rates had moved in opposite direction in the case of Mexico and U.S., while Canada has had a more stable process. Table 6 presents Mexican exchange rate for the month of December, for years 1990 to 2001:

Table 6. Monthly (December) Exchange Rate of Mexican Peso Into one U.S. dollar, 1990-2001 (Pesos per US dollar)

	1990	**1991**	**1992**	**1993**	**1994**	**1995**	**1996**	**1997**	**1998**	**1999**	**2000**	**2001**
December	**2.941**	**3.070**	**3.118**	**3.108**	**3.931**	**7.660**	**7.877**	**8.136**	**9.912**	**9.415**	**9.444**	**9.167**
Source: http://www.inegi.gob.mx/difusion/ingles/fieeco.html												

As we can see from the table, Mexican Peso was loosing grounds against one U.S. dollar prior to NAFTA years and during the NAFTA years as well. Since 1990, 2.941 pesos per U.S. dollar, value of peso kept falling, reaching 9.167 pesos for one U.S. dollar in 2001.

Through most NAFTA years Canadian dollar kept loosing ground compared to its neighbor. In 1997 one U.S. dollar was traded to 0.7222 Canadian dollar. This figure consistently fell, and in 2001 the figure was 0.6456 U.S. dollar per one Canadian[7]. NAFTA could have been one of the causes that helped exchange depreciation against U.S. dollar, as NAFTA was intended to stimulate trade, investment, and other sectors of the economy of its members, most attention is still being paid to these issues.

The issue of weak Canadian currency was one of the central worrisome issues for most Canadians. But naturally, when comparing Canadian economy to that of U.S. most indicators show that things like productivity level, level of overall technological innovation, and smaller size of its economy eventually led to a depreciation of Canadian dollar against U.S. dollar. Here debates about whether a common currency should be implemented in the future catch economists' attention. Surely some economists like Dobson (2002) brought option of some sort of currency union into surface. But they again conclude that this is the tricky question that needs to be deeply analysed in the near future. More on this in the next section.

Implementation of NAFTA was initially intended to increase and to liberalize trade conditions by eliminating obstacles that existed among Canada, U.S. and Mexico. Recent studies and researches indicate that NAFTA indeed is very favorable to trade improvement among three member countries. The following Table 7 illustrates share of interregional trade for each country:

Table 7. Share of Interregional trade in total of each country (in percentages)

	USA	MEXICO	**CANADA**
1996			
Exports	37.1	86.3	79.4
Imports	29.1	77.5	75.7
2001			
Exports	51.6	90.0	84.6
Imports	30.6	70.2	72.7
Share variation between 1996 to 2001			
Exports	14.5	3.7	5.2
Imports	1.5	-7.3	-3.0

Source: Department of Commerce. Statistics Canada and INEGI

[7] See Statistics Canada: http://www.statcan.ca/english/Pgdb/econ07.htm

From Table 7 we can see that from 1996 to 2001 share of exports and imports of each of the three countries in NAFTA region have increased. For United States exports increased from 37.1 percent in 1996 to 51.6 percent in 2001, and imports have risen to 30.6 percent in 2001. In Mexico exports have increased to 90.0 percent in 2001 from 86.3 percent in 1996. Imports interestingly have declined to 70.2 percent in 2001 from 77.5 percent in 1996. This result suggests that decrease in imports in Mexico compared to the increase of exports were undeniable effect of NAFTA's trade provisions. Mexico intensified its production level, by producing more for foreign markets (U.S. and Canada in this example) and as well as for its internal, domestic market. In Canada this pattern was similar to Mexican. Exports in 2001 increased to 84.6 percent from 79.4 percent in 1996 and imports decreased to 72.7 percent in 2001 from 75.7 percent in 1996. As we can see from the share variations presented in Table 7 Canada and Mexico experienced export increase and import decrease in overall interregional NAFTA market, again perhaps because of the increased production of goods for both foreign and domestic markets. Figures 1a. and 1b. For Canadian exports to and imports from the United States show how Canada's exports and imports have grown with a slight decrease from year 2000 to 2001.[8]

[8] Source: http://strategis.ic.gc.ca/sc_mrkti/tdst/tdo/tdo.php#tag

Figure 1a. Canadian Merchandise Imports from U.S. (in millions of Canadian dollars)

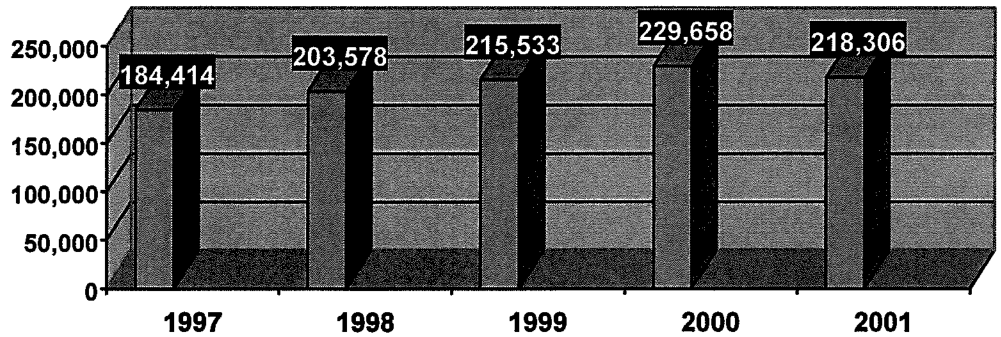
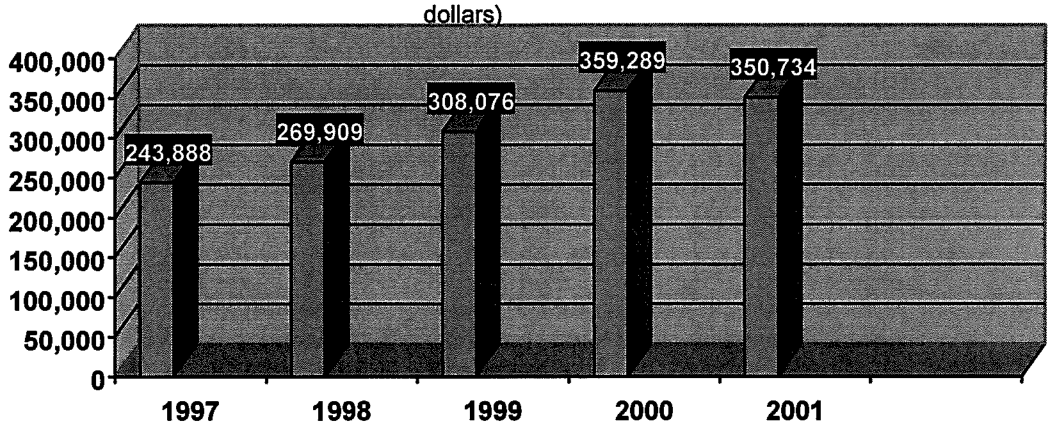


Figure 1b. Canadian Merchandise Exports to the United States (millions of Canadian dollars)

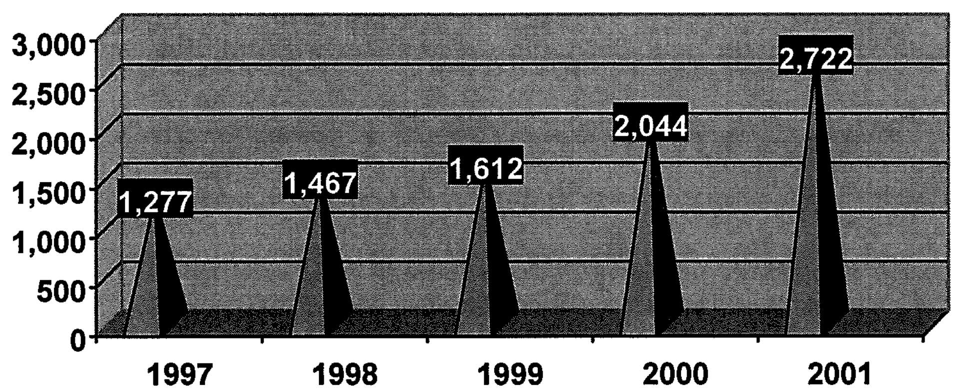


Imports from U.S. were 184,414 millions of Canadian dollars in 1997 and has been increasing over the years, only with a slight decrease in 2001 when imports fell to 218,306 millions of Canadian dollars from 229,658 in 2000. Exports followed the same growing pattern through 1997 to 2001 with a slight decrease in 2001 when Canada exported 8,555 million Canadian dollars worth products to U.S. This slight decrease in exports to U.S. might have been associated with the slowing performance of the U.S.

economy. To compensate somewhat Canada at the same time increased its merchandise exports to Mexico.

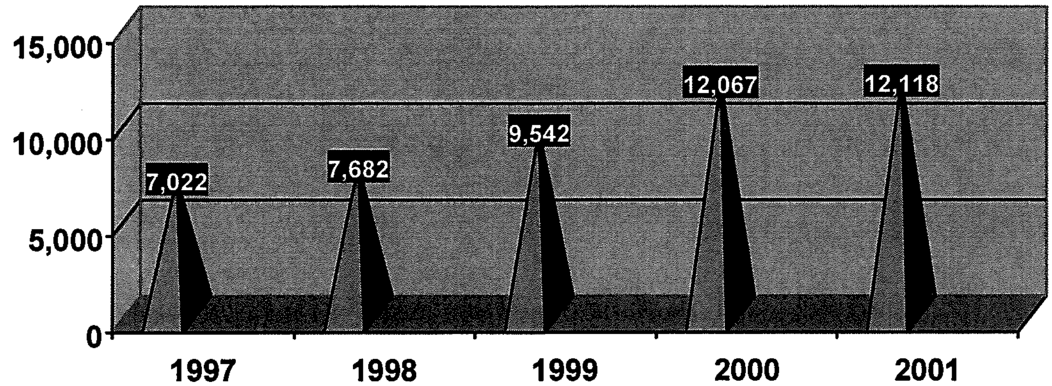
Canada has much benefited from NAFTA provisions that gave greater access to the Mexican market. Businesses were given access to previously highly restricted sectors, such as financial services, trucking, energy, automotive products and fisheries. Mexico has become Canada's 13th largest export market and fourth largest import source. Exports to Mexico have risen consistently, reaching $2,722 million in 2001, an increase of 65 per cent over the first five years in NAFTA. Imports from Mexico have increased to $12,118 million by 2001. These results can be seen on the following figures 2a. and 2b.[9]

Figure 2b. Canadian Exports to Mexico (in millions of Canadian dollars)



[9] Source: http://strategis.ic.gc.ca/sc_mrkti/tdst/tdo/tdo.php#tag

Figure 2b. Canadian Imports from Mexico (in millions of Canadian dollars)



Clearly we can see from above graphs, Canadian exports from as well as imports to Mexico were steadily rising over the NAFTA years. These increases are the signs of effectiveness of NAFTA provisions that were basically intended to improve trade relations among its members.

When talking about trade increase in NAFTA countries, one should note the fact that during the past few years there were number of conducted studies and papers by several economists, like McCallum (1995), Brown (2002), Anderson and Wincoop (2001), Coulombe (2002) and Helliwell (2002), dedicated to a so called "border effects" issue in North America, mainly between Canada and United States. Here the border effect is calculated by obtaining the ratio of interprovincial weighted trade to province-state weighted trade, which then can be interpreted as value that shows how much more Canadian provinces trade with each other compared to the trade between provinces and states in America. McCallum estimated this effect in 1988 and then re-estimated it in 1995 using a gravity model. For example, using 1988 data for interprovincial and province-state trade, McCullum calculated this effect and concluded that other things being equal, trade between two provinces is more than 20 times larger than trade between a province and a state. This result was obtained before the enactment of FTA and NAFTA. Later studies by Helliwell (1998), using a more sophisticated and newer data for years 1990 and 1996, showed that after enactment of FTA border effect fell from 19.5 to 11.9, a result attributed to the FTA. Later on, studies by Anderson and Wincoop (2001) on welfare analysis show that variability of border effect depends not only on weighted interprovincial and province-state trade, but also on economic size and density (economic size divided by distance) of the trading partners. According to them country with bigger economy and higher density, like U.S., tends to have smaller border effect compared to a small sized economy. They say that Canadians would have substantial increases in their welfare levels if border effects were small or even absent. But not all authors agree with their statement. For example Helliwell (2002, p.44) argues that subjective well-being in Canada is significantly higher than in the United States, thus ignoring the idea that welfare could rise by more than one-third relative to than in U.S. simply by reducing trade barriers.

One of the main objectives of NAFTA was to stimulate the flow of investment to a higher degree among its members. It is believed those massive flows of investment from U.S. to Mexico and Canada helped to increase productive capacities in the region. Since the enactment of NAFTA, investment flows has increased, accumulated flows reached a total of $119,527 billion U.S. dollars at the end of 2001. As seen below in Table 8, for Canada, U.S. FDI kept increasing since the signature of NAFTA. In 1994 U.S. FDI to Canada was 6,047 millions of U.S. dollars and it rose steadily until 1998, when it reached 7,832 millions of U.S. dollars. In 1999 it fell to 1,811 million from 7,832 million in 1998. One of the reasons for this decline might have been the fact that during the same years United States increased its FDI to Mexico (from 4,593 in 1998 to 5,978 millions in 1999) and to the rest of the world. The following Table 8 illustrates these results.

Table 8. Flows of U.S. Direct investment in Mexico and Canada (millions of U.S. dollars)

	Canada	Mexico	Total
1994	6,047	4,457	10,504
1995	8,602	2,983	11,585
1996	7,181	2,405	9,586
1997	7,642	5,596	13,238
1998	7,832	4,593	12,425
1999	1,811	5,978	7,789
2000	18,950	5,302	24,252
2001	14,440	15,708	30,148
In the period			**119,527**

Source: Duran (2002), "NAFTA Macroeconomics".

As it was the case before the NAFTA, U.S. remains as the largest investor in Canada. Between 1993 and 1998 U.S. investment in Canada increased by 63 per cent, from $90.6 billion. On the other hand, U.S. is still the largest destination for Canadian foreign direct investment. In 1998 the stock of Canadian investment in U.S. reached $126 billion, up 23 per cent over 1997 and 86 per cent during the NAFTA's first five years. But as it was recently mentioned in a commentary paper by Wendy Dobson (April 2002), overall share of Canadian FDI in U.S. has declined from more than 70 percent in mid-1980s. The share of inward FDI from U.S. to Canada has also declined to 70 percent in 1998, down from 80 percent in the 1970's. According to Dawson, this decline in FDI reflects the increased interests of investors of both U.S. and Canada in other parts/countries of the world, such as Mexico.

Significant increases of Canadian FDI in Mexico have quadrupled during the NAFTA years to $2.2 billion in 1998. Canadian FDI is concentrated in mining, banking and telecommunications sectors. Potentials remain in areas like gas and energy. Mexican investment into Canada is also growing steadily, but remains relatively small. See the following figure 3a. and 3b.[10]

Figure 3a. Mexican Investment in Canada (in millions of Canadian dollars)

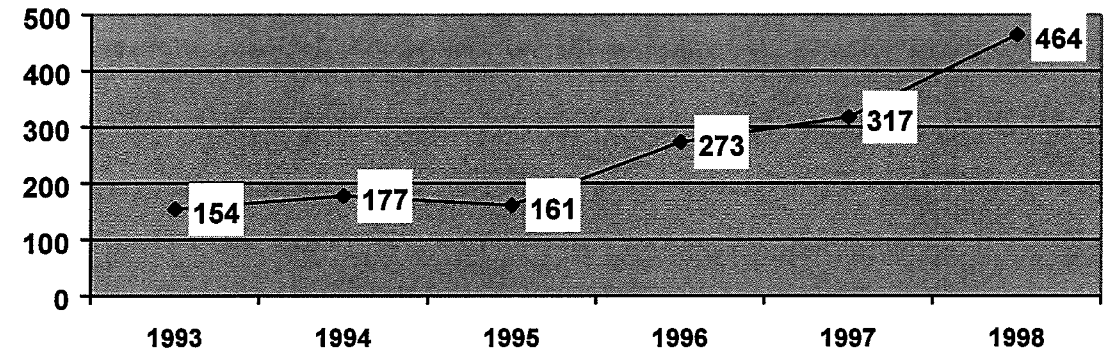
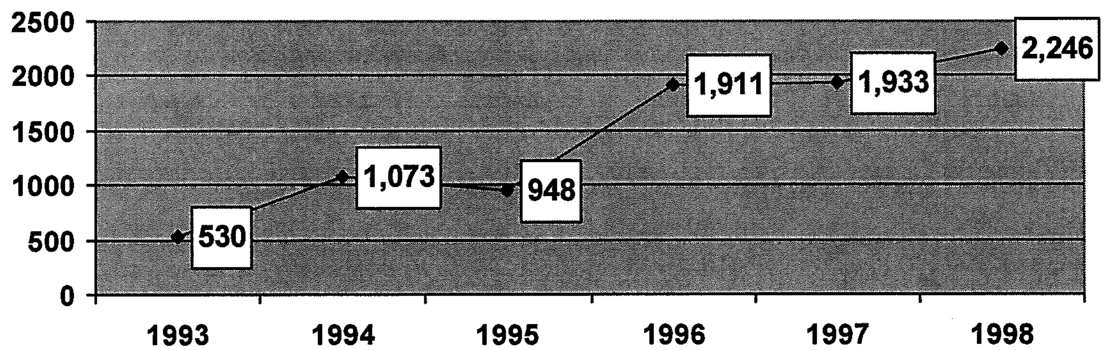


Figure 3b. Canadian Investment in Mexico (in millions of Canadian dollars)



As it can be seen from Figure 1a. despite the small values, Mexican investment to Canada has been rising through almost all NAFTA years. In 1993 Mexicans invested 154 million Canadian dollars worth investment into Canada. It reached 464 million in 1998,

[10] Source: Stock of FDI, Statistics Canada, 1998

spectacular increase. The still relatively small volume of investments can be characterized with the facts that Mexico is still small and undeveloped economically, and it would probably be unable for the years to come to make big investments into other countries. Mexico is rather in a great need for investment in first place. Figure 1b. shows Canadian investments are helping Mexico. Although, these figures are small compared to the investment volumes that United States makes into Mexico, numbers have been growing over from 530 millions of Canadian dollars in 1993 to 2,246 millions in 1998.

Over the years, a number of studies and assessments have addressed the issues of the impact on NAFTA on the North American economy. Overall, these reports show that the effects of the NAFTA have been positive. Despite the difficulty to isolate the impact of the NAFTA on economic variables such as trade and investment flows or economic growth and job creation, a number of recent analyses attempted to shed light on these issues. Recent paper by the bank of Montreal (March, 1998) support the conclusion that the NAFTA has had a positive impact on sales and job growth in Canada and throughout North America. It further reports that businesses across the continent expect to pursue cross-border opportunities even more aggressively over the next couple of years[11]. Other studies that focus more on the Mexico-United States dimensions of the NAFTA come to similar positive conclusions. They show that the impact of the NAFTA on jobs has been neutral to moderately positive[12].

NAFTA's welfare indicators show that the differences among its member countries are huge. While in Mexico average schooling year is 7 years, in Canada and United States they are 18 and 16 years respectively. The consequences of this outcome for Mexico are the low-income level of most people, where more than 40 million people earn

[11] See Department of Foreign Affairs (1999), *The NAFTA at Five Years, a partnership at work.*

about $1.00 per day. Mexico's income distribution system is also one of the worst in the world. The ratio of the highest quintile to the lowest is 13, in Canada it is 5, and in U.S. it is 9. Level of literacy in Mexico is also lower compared to its NAFTA partners (almost 100 percent in Canada and The States), which is 89 per cent; in rural areas with large Indian population this number is sometimes even smaller. Table 9 illustrates some of the observations concerning overall welfare indicators in NAFTA countries.

Table 9. North America: Basic DATA related to Welfare in three countries (2000)

Indicators	Canada	United States	Mexico
Population, total	**30.8 mln.**	**281.6 mln.**	**98.0 mln.**
Population growth (annual %)	**0.8**	**1.2**	**1.4**
Life expectancy at birth (years)	**78.9**	**77.1**	**73**
Population age 15 to 64 (% of total)	**67%**	**65%**	**58%**
Fertility rate, total (births per woman)	**1.6**	**2.1**	**2.6**
Mortality rate, under 5 (per 1,000 live births)	**7.2**	**8.7**	**35.8**
Average years of schooling	**17.5**	**16.0**	**7.0**
Urban population (% of total)	**78.7**	**77.2**	**74.4**
GNI per capita, Atlas method (current US $)	**21,130.0**	**34,100.0**	**5,110.0**
Personal computers (per 1,000 people)	**390.2**	**585.2**	**50.6**
Internet users	**12.7 mln.**	**95.4 mln.**	**2.7 mln.**
Source: Duran (2002): "NAFTA Macroeconomics".			

[12] See www.ustr.gov

From the table it is obvious that compared to its partners, Mexico's population is growing faster. With annual population growth of 1.4 per cent, Mexico has the shortest life expectancy rate, the lowest fertility and highest mortality rates. All these findings indicate that Mexico has still a lot to go through to increase welfare level and overall living standards. Wage differentials are relatively small between Canada and the United States. While with Mexico the situation is different. Mexican labor costs dropped dramatically, when peso significantly devaluated in 1994, and have not improved since then. This in turn gave Mexico comparative advantage over U.S. and Canada, but at the same time it weakens domestic and overall NAFTA markets. When it comes to productivity, paradoxically in Mexico it has been increasing at a faster rate than in the United States and Canada. But other problems mentioned earlier in this section of the paper are overshadowing this improvement. Mexican workers generally receiving very small or no benefits at all from increased productivity.

Chapter 4. Future Prospects and Challenges.

Being so far relatively successful for its member countries, the NAFTA still has a lot more to bring in the future, there are bunch of matters that need to be improved and maybe even changed in the context of NAFTA's provisions. These improvements are especially important to NAFTA's least developed member country-Mexico.

How should NAFTA be further evolved? Should it be expanded to other American countries on the continent to form Free Trade Agreement of Americas (FTAA)? While it is still early to set the certain standards of how FTA should be expanded to other

American countries, during the meeting that took place in December of 1994 in Miami, 34 democratically elected presidents in the Americas promised to negotiate FTAA by 2005. Obviously almost after a decade that promise will most likely be unfulfilled.

No more than few analysts of NAFTA, like W.Dobson (2002) and R.A.Pastor (2001), have thoroughly looked at the experience of the longest-running, most successful regional trading scheme of European Union (EU). Few country leaders gave serious interests on how should future relationship among North American countries be formed. Exception was the newly inaugurated president of Mexico Vicente Fox Quesada. He boldly proposed to replace Free Trade Area with a common market that will look like the one existing in EU[13]. But his idea of a common market was not taken seriously into account in Canada and in U.S. as well. Although recognizing that this might take possible 20 years or more, President Fox has also proposed the idea of free labor movement in North America. He understood that major differences in incomes would probably be the biggest obstacle for that idea to come true. There was another proposal by Mexicans to form a compensation fund that would assist the development of the poor regions of Mexico. President of the United States George Bush and Canadian Prime Minister Jean Chretien promised to study these ideas.

There are sectors within each NAFTA member country, like financial sectors in U.S. and Canada, who are pretty much satisfied with the performance of NAFTA so far. But there are also people who would prefer to renounce or fundamentally alter the FTA. In his book "Toward a North American Community" Professor Robert A. Pastor of International Relations at Emory University presents the following seven compelling

[13] See R.A.Pastor (2001), "Toward a North American Community".

reasons for the need to reevaluate NAFTA and seek for the new ideas to deepen the relationship between its members.

First, he thinks that NAFTA has not changed US's relationship towards its two neighbors. This relationship is driven by highly organized domestic interests inside U.S. that lack trinational rules to deal with Mexico and Canada. Mostly issues like immigration policy towards Mexico and protectionism from competition with Canadian producers of dairy and textile products come first for U.S. officials, which in turn leads to asymmetry of powers between neighbors leading to a difficulty in coordination to solve various problems between these three countries. The best way to change these habits is to submit them to a new structure that will be based on rules rather than power or sense on inferiority.

Second, NAFTA have not eliminated contradictions that exist in integrating three diverse economies and societies. The most important contradiction is that barriers eliminated to trade in legal products between United States and Mexico often makes it easier to smuggle illegal products like drugs from Mexico to the United States and illicit guns from U.S. to Mexico. As governments at both sides try to cope with these illegal issues, legitimate businesses suffer by paying for the delays. Solution of these problems also requires new formulas that can be incorporated into NAFTA.

Third, different foreign policy issues that three governments practice towards other foreign countries, for example Cuba, make it difficult to strengthen cooperative spirit. Although it might not be possible for the three to eliminate differences in their relations towards Cuba, they might benefit more and be more effective in their policies if they succeeded.

Fourth is the issue of exchange rate differentials and controversial issues like common currency. As years past three economies are becoming highly integrated with each other and major shifts in foreign exchange rates will have a huge impact on trade and domestic businesses. Undervalued exchange rates could lead to industrial restructuring or they could bring even higher protectionism feelings among governments. While single currency could solve many of these problems, they might create others too. Common currency or a common market might bring controversies in issues like sovereignty, the way governments conduct independent monetary and fiscal policies, which might lessen the feeling of independency in Canada or in Mexico. But no matter what are the arguments from each government, they would probably be better off to deal with the issues now rather than delay them.

Fifth, the three countries are getting more and more socially integrated because of immigration. While for Canada and the United States immigration is the main source of population growth and employment, for Mexico emigration and remittances have negative psychological and financial effects. This issue of immigration is among the most important issues for Mexicans.

Sixth, NAFTA would benefit from an office that would hold responsibility to devise a North American plan for transportation and infrastructure and maybe for other issues as well. Without this sort of office, trucker that carries either imported or exported goods across three countries must cross 64 separate jurisdictions in North America, which in turn makes it difficult for a trucker to keep his or her costs low[14].

Seventh, Pastor thinks that most compelling practical reason to approach NAFTA with a different attitude is its original premise's lack of realism. NAFTA was negotiated to

[14] See R.A.Pastor (2001), "Toward a North American Community".

eliminate trade barriers in long-term period, but in short-term, however, it ignored uneven economic development, different vulnerabilities, and wide disparities in income and unemployment among the three countries. The main argument for deepening NAFTA is that problems can no longer be kept in any of the three countries, and new opportunities benefit all three. All the above arguments and suggestions that were not one of the first agendas in first place in the United States and Canada were probably even more forgotten after the events of 9-11 of 2001 in New York.

NAFTA has also a big deal when it comes to environment. Actually NAFTA is the first trade agreement that takes into account environmental considerations. There is a commission named Commission for Environmental Cooperation (CEC) that was established by the NAFTA side agreement to specifically deal with environmental issues. Each of the three countries have their says in CEC and they also must get along to meet CEC's requirements, for example when it comes to explicit commitments by each nation to reduce toxic substances in the North American environment, or they must induce changes in priorities for conservation and promote public participation. With the enactment of NAFTA there came more and more concerns from environmentalists of how this type of trade and other agreements will be affecting region's environment. It is obvious on one hand that environment suffers more in economically undeveloped or poor countries, and most environmentalists agree that sustainable economic growth is the ultimate goal for each of the three member countries especially for Mexico. NAFTA's environmental provisions are partially included in the NAFTA text itself, but most of these provisions are contained in the side agreement called the North American Agreement on Environmental cooperation (NAAEC). Under the NAAEC's environmental provisions each party agreed to enforce its domestic environmental laws and to have high environmental standards that should not be relaxed on purpose to attract more investment. Although many agree that NAAEC is doing a good job enforcing its regulations on three sides, there are still objectives and challenges need to be brought up.

While each country is trying to do its best when it comes to environment, governments perhaps have to be even more understanding of the possible environmental problems that NAFTA might bring in the future, especially Mexican government, which is the most suspicious of the NAAEC's intentions towards the better and safer environment for the generations to come. Ratification of Kyoto Protocol (in which the developed nations agreed to limit their greenhouse gas emissions) by Canadian government is the first big step towards the safe environment, I think others should follow it.

Canada's the main interest in the future is further integration to the U.S. as well as world market. The big ideas presented by Dabson (2002) are one of the next important steps towards the future integration. These ideas are, first, a some sort of a customs union that might be established in NAFTA countries towards the rest of the world, which will have common external tariff and allow for free circulation of goods and services within that customs union. Second ideas is a common market, where not only goods and services will be free traded but there will be a way for a freerer circulation of capital, people and technology. This market will have to be formally negotiated by NAFTA members. Third idea is a strategic bargain, this idea if realized will help to achieve deeper integration, without undermining political autonomy of each of the members, by organizing special working groups. For Canada it would combine security initiatives with customs-union and common-market like reductions in barriers to trade, to investment and to mobility of labour. However to realize these ideas Canada can no longer stay away from national security problems that faced North America after the events of September 11, 2001. The economic prosperity of Canada and the United States will largely depend on more secure but open borders with each other and with the rest of the world.

As it was mentioned earlier, there were numerous comparisons between EU and the NAFTA region, questions were asked whether it will be possible to change the NAFTA region to similar community that exists in Europe these days. Frankly speaking, I don't think it is ever going to happen in North America. Idea of a common currency, in this case it would probably be U.S. dollar, is somewhat frightening to Canadian and Mexican governments especially, despite all the benefits it could bring with it. Well at least it would not be considered as a real future economic scenario in North and Latin America for at least several decades, until countries in, lets say, FTAA will narrow huge gaps in economic developments among each other.

In the future, Mexico will probably try to improve its energy industry, reform its social security and health care, labour laws and infrastructure. To successfully bring reforms into energy industry President Fox will need to bring some changes into Mexican constitution, which protects energy industry by long laid rules that gives exclusive rights of ownership only to nationals. But to do that Fox has to convince Mexican congress and receive two-thirds of votes.

United States perhaps will concentrate on issues like national security, immigration policy, defense policy, look for more sources of energy supply from Canada, and electricity supply from both Mexico and Canada.

The main challenges for Canada in the future is further reduction of tariffs on industrial goods, increase in trade relations with Mexico and liberalization of relations with the United States. For Mexico, fear of getting too open for the trade with the United States and feeling of weakening its sovereignty is still remaining. They must find the ways to eliminate their fears and further liberalize their relatively closed areas of trade. United States has to have a better understanding of Mexican problems and realize that if there are any kinds of crises it will not be longer contained in Mexico only. A problem on one part of North America would certainly affect the other parts.

Conclusions.

As a conclusion I would like to say that almost a decade has passed since the North American Free Trade Agreement came into force. This decade is a small period of time for NAFTA to come into full force and to be equally effective and efficient for all of its member countries at the same time. While historically Canada and United States are long time trading partners, and implementation of FTA and NAFTA let these neighbors to integrate with each other even more economically, culturally and financially, wide range of differences in Mexico might drag back NAFTA's full integration in North America for few decades. Although Mexico's successive open market reforms somewhat narrowed the gap between it's NAFTA partners, number of events, like terrorists's attack in New York in 2001 and US's new campaign against Iraq, overshadows the importance of NAFTA to Mexico, Canada and even to United States itself. Nevertheless, based on the presented facts and opinions in this paper, one can baldly say that NAFTA is serving as an effective tool for trade liberalization in the variety of sections of each country's economy. However concluding this paper I would like to stress and underline the facts that for NAFTA to reach a near perfection over its members there are still a lot of obstacles to overcome. These obstacles might be the ones like, further narrowing of the economic gaps among Mexico, Canada and United States; a clear understanding of the fact that NAFTA is a trade agreement only, and its further integration and possible extension to other countries in south America, should not reduce the sovereignty feelings, and should not be any sort of threat to national security issues. Although, at this point of time it might seem ridiculous that NAFTA might be redefined as some sort of Economic Union, or be the basis for a common borderless, free trading market for its members, I do not rule out the possibility that in the farthest future it might quite be a reality.

And again maybe North American leaders should probably stop ignoring EU's experience and try to learn from them. And maybe North America will find the magic formula to bring the developing countries on the continent to the industrial world.

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