



# The Mexican Economy After the Global Financial Crisis

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## Summary

The state of Mexico's economy is important for U.S. policymakers for many reasons, most significantly because a prosperous and democratic neighboring country is in the best interest of the United States. The two countries have strong economic, political, and social ties, which have direct policy implications related to bilateral trade, economic competitiveness, migration, and border security. In May 2010, President Barack Obama hosted Mexican President Felipe Calderón at a meeting in the White House in which the two leaders discussed key issues affecting the two countries. They agreed to continue and reinforce cooperation on creating jobs, promoting economic recovery and expansion, and encouraging inclusive prosperity across all levels of society in both countries. The 111<sup>th</sup> Congress is likely to maintain an active interest in Mexico on issues related to the North American Free Trade Agreement (NAFTA) and other trade issues, economic conditions in Mexico, migration, border security issues, and counter-narcotics.

The global financial crisis that began in 2008 and the U.S. economic downturn had strong adverse effects on the Mexican economy, largely due to its economic ties and dependence on the U.S. market. Mexico's gross domestic product (GDP) contracted by 6.6% in 2009, the sharpest decline of any Latin American economy. Mexico's reliance on the United States as an export market and the relative importance of exports to its overall economic performance make it highly susceptible to fluctuations in the U.S. economy. Most other Latin American countries are not as dependent on the United States as an export market. Economic reforms over the past 20 years and the government's responses to the effects of the global financial crisis have helped Mexico weather the economic downturn and improve conditions in 2010. However, sustained economic recovery will likely depend on the U.S. economic recovery and the ability to sustain this growth.

In addition to the adverse effects from the global financial crisis and the U.S. economic contraction, Mexico's economy is experiencing numerous other challenges. The escalation of violence since the government's crackdown on organized crime and drug trafficking has led to investor uncertainty in some regions of the country and, subsequently, a sharp decline in foreign direct investment flows. The impact has been the most severe on the manufacturing industry, which is mostly located along the U.S.-Mexico border and has experienced significant job losses. Increasing unemployment throughout the country has led to a growing trend towards informality and self-employment. This may present a long-term problem for the government because growth in the informal sector can lead to increased poverty levels, diminished productivity, and lower prospects for sustained economic growth. Another issue is the 16% drop in remittances to Mexico in 2009, which have mostly affected the poor. Remittance inflows, which are largely from the United States, are Mexico's second-highest source of foreign currency after oil.

Numerous analysts have noted that Mexico's potential to promote economic growth, increase productivity, and lower the poverty rate is very limited without implementing substantial structural reforms. President Calderón has proposed a number of reforms to address these challenges, including proposals to eliminate extreme poverty, overhaul public finances, privatize parts of the state oil company, adopt labor reforms, reform the telecommunications sector, and encourage political reforms. Most of these proposals, however, have deeply rooted political implications and have been strongly opposed by the major political parties in the Mexican Congress. There are some signs that the population may be pushing for change, but the prospects for passing any of the proposals will likely depend on the outcome of the 2012 presidential elections.

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## Introduction

The Mexican economy experienced the most serious decline in economic growth in Latin America after the global financial crisis began in 2008. Mexico's dependence on manufacturing exports and strong ties to the U.S. economy have made the country very vulnerable to external events and changing economic conditions in the United States. Public sector revenues declined as a result of the crisis and a number of estimates indicate that Mexico's gross domestic product (GDP) contracted by 6.6% in 2009. Though GDP is expected to grow in 2010, some economists predict that Mexico's economy will not return to its pre-crisis level for some time. Although Mexico has done much to modify its economic policy over the last twenty years through trade liberalization, privatization efforts, and a floating exchange rate regime, these policies have not been enough to protect Mexico from fluctuations in the U.S. economy. Many analysts argue that structural weaknesses in the Mexican economy have prevented the country from experiencing higher levels of growth and decreasing its dependence on the U.S. economy.

Mexico's economy is of interest to U.S. policymakers because of the strong economic linkages between the two countries, the proximity of Mexico to the United States, and the implications that economic issues have on political and social stability in Mexico. The 111<sup>th</sup> Congress is likely to maintain an active interest in Mexico on issues related to trade, economic conditions, migration, border issues and counter-narcotics. This report provides an overview of Mexico's economy post-financial crisis, effects of the global economic downturn, structural and other challenges in the Mexican economy, and implications for the United States.<sup>1</sup> This report will be updated as events warrant.

## Overview of Mexico's Economy

Based on a nominal GDP of \$1.7 trillion in 2009 (at purchasing power parity or PPP<sup>2</sup>) Mexico's economy is the 11<sup>th</sup> largest economy in the world and the second largest in Latin America, after Brazil.<sup>3</sup> Mexico has an open market economy with a strong export sector, though for many years it had strong protectionist trade policies to encourage industrial growth in the domestic economy.

## Current Conditions

The global financial crisis, and the subsequent downturn in the U.S. economy, resulted in the sharpest economic contraction in the Mexican economy in twenty years. It is estimated to have contracted by 6.6% in 2009, as shown in **Table 1**, while the Mexican peso depreciated against the

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<sup>1</sup> For more information on Mexico-U.S. relations and the Mexican economy, see CRS Report RL32724, *Mexico-U.S. Relations: Issues for Congress*, by Clare Ribando Seelke, and CRS Report RL32934, *U.S.-Mexico Economic Relations: Trends, Issues, and Implications*, by M. Angeles Villarreal.

<sup>2</sup> Purchasing power parity (PPP) is an economic technique that attempts to factor in price differences across countries when estimating the size of a foreign economy in U.S. dollars.

<sup>3</sup> Based on data from the Economist Intelligence Unit online database.

dollar by 25%.<sup>4</sup> Mexican merchandise exports to the United States decreased sharply. Mexico also experienced liquidity problems and a loss in investor confidence as a result of large losses on corporate foreign exchange positions in 2008, in addition to the uncertainty over the outbreak of the H1N1 virus in mid-2009.<sup>5</sup> Mexico's policy measures in response to the crisis and its prior economic performance have helped the economy begin to recover and the exchange rate to improve. Estimates for 2010 project that the economy will grow by about 3% to 4% and that domestic demand will also improve, though not significantly. The recovery is also due to an increase in external demand, which has driven up manufacturing exports, rather than from internal demand.<sup>6</sup> Manufacturing exports increased 34% year-on-year during the first five months of 2010, with much of the growth occurring in automotive exports (78% increase), which go mostly to the United States. Total exports have risen 38%.<sup>7</sup> Sectors of the economy that depend significantly on domestic demand, such as utilities, construction, and retail, are struggling, though an improvement is expected later this year. The Economist Intelligence Unit (EIU) projects GDP growth at 2.7% for 2011.<sup>8</sup>

## **Ties to the U.S. Economy**

Mexico's strong economic ties to the United States after implementation of the North American Free Trade Agreement (NAFTA) have deepened the dependency of the Mexican economy on U.S. economic conditions.<sup>9</sup> Mexico's reliance on the United States as an export market and the relative importance of exports to its overall economic performance make it highly susceptible to fluctuations in the U.S. economy. Exports equaled 26% of Mexico's GDP in 2009, a significant percentage, and 80% of Mexico's exports are destined for the United States. The United States is, by far, Mexico's most important partner in trade and investment, while Mexico is the United States' third largest trade partner after China and Canada. After oil and gas, most of Mexico's exports are manufactured goods.

Because a large percentage of Mexico's exports are destined for the United States, any change in U.S. demand can have significant economic consequences in Mexican industrial sectors. The recent downturn in the world economy caused a sharp decline in U.S.-Mexico trade and affected GDP growth in Mexico. As shown in **Figure 1**, economic growth in Mexico has followed the same economic patterns in the United States for many years, but with higher fluctuations in GDP growth rates. After a real decline in GDP of 6.22% in 1995, the Mexican economy managed to grow the following six years at about 4%-5% annual growth. The slowdown in the U.S. economy in 2001, which worsened after the September 11 terrorist attacks, hit Mexico's economy hard. Real GDP growth dropped from 6.6% in 2000 to a contraction of 0.2% in 2001. Improved economic conditions in the United States in the following years helped Mexico's economy

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<sup>4</sup> International Monetary Fund (IMF), *Public Information Notice*, "IMF Executive Board Concludes 2010 Article IV Consultation with Mexico," p. 2.

<sup>5</sup> *Ibid.*

<sup>6</sup> Economist Intelligence Unit (EIU), *ViewsWire*, "Mexico economy: Externally driven rebound," May 17, 2010.

<sup>7</sup> Based on data from Mexico's Instituto Nacional de Estadística y Geografía.

<sup>8</sup> EIU, *ViewsWire*, "Mexico economy: Externally driven rebound," May 17, 2010.

<sup>9</sup> The North American Free Trade Agreement (NAFTA) is a trilateral free trade agreement that eliminated trade and investment barriers between Canada, Mexico, and the United States. It has been in effect since January 1, 1994.

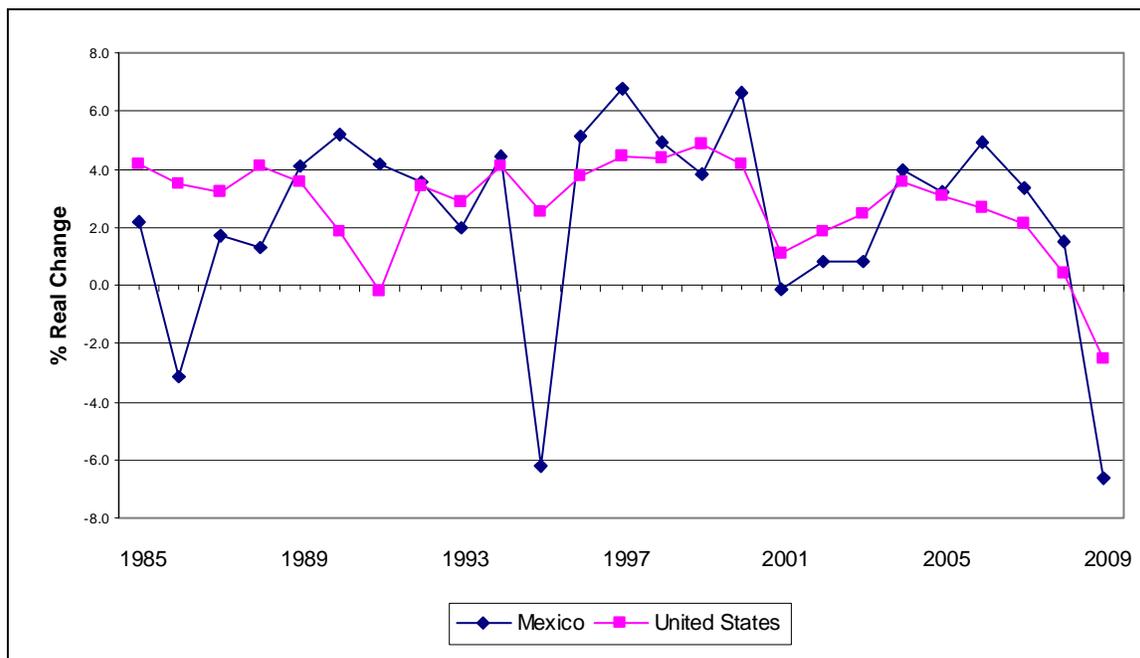
improve as well. Real GDP growth in 2004 was 4.0%, up from 0.8% in 2003 and 2004. Following the decline in the U.S. GDP growth rate of 2.7% in 2006 to -2.4% in 2009, Mexico's GDP growth rate fell from 5.1% in 2006 to -6.6% in 2009 (see **Figure 1**).

**Table 1. Mexico's Average Annual Real GDP Growth: 1990-2009**

<b>Year(s)</b>	<b>Average Annual Growth (%)</b>
1990	5.2
1991	4.2
1992	3.6
1993	2.0
1994	4.5
1995	-6.2
1996	5.1
1997	6.8
1998	4.9
1999	3.9
2000	6.6
2001	-0.2
2002	0.8
2003	0.8
2004	4.0
2005	3.2
2006	5.1
2007	3.3
2008	1.5
2009	-6.6

**Source:** Compiled by CRS using data from the Economist Intelligence Unit online database.

**Figure 1. Average Annual Real GDP Growth in Mexico and the United States  
1985-2009**



Source: Compiled by CRS using data from the Economist Intelligence Unit online database.

## Past Economic Policies and Reforms<sup>10</sup>

Until the early 1980s, Mexico had strong protectionist economic policies with high trade barriers in several key industries, including the computer and automotive industries. After the Mexican 1982 debt crisis, Mexico's trade policy began to change. The Mexican government took a series of steps toward unilateral trade liberalization to attract foreign investment and make the country more competitive in non-oil exports. In the late 1980s, Mexico proposed negotiations for a free trade agreement with the United States.

The Mexican economy suffered a financial crisis in 1995 that resulted from a number of complex financial, economic, and political factors. In response, the government abandoned its previous fixed exchange rate policy and adopted a floating exchange rate regime.<sup>11</sup> Mexico's currency

<sup>10</sup> For more information on the history of Mexico's past economic reforms and trade policies, see Juan Carlos Moreno-Brid and Jaime Ros, *Development and Growth in the Mexican Economy, A Historical Perspective* (Oxford University Press, 2009); and Gary Clyde Hufbauer and Jeffrey J. Schott, *NAFTA Revisited, Achievements and Challenge*, Institute for International Economics, October 2005.

<sup>11</sup> Between 1991-1994, the Mexican government maintained an exchange rate policy in which the Mexican peso depreciated daily against the U.S. dollar by a certain amount. The exchange rate policy was not sustainable and the government was forced to devalue the peso first by lifting the exchange band ceiling, and then allowing the peso to float freely in December 1994. See EIU, *Country Profile, Mexico*, 1996-97, pp. 10-12.

plunged by around 50% within six months as a result, sending the country into a deep recession.<sup>12</sup> The peso steadily depreciated through the end of the 1990s, which led to greater exports and helped the country's exporting industries but sharply raised import prices and lowered its terms of trade.<sup>13</sup> The change in the Mexican economy to an export-based economy may have helped to soften the impact of the currency devaluation. However, the peso devaluation resulted in a decline in real income, hurting the poorest segments of the population and also the newly emerging middle class.

After the 1994 devaluation, the government took several steps to restructure the economy and lessen the impact of the currency crisis among the more disadvantaged sectors of the economy. The goal was to create conditions for economic activity so that the economy could adjust in the shortest time possible. The United States and the International Monetary Fund assisted the Mexican government by putting together an emergency financial support package consisting of loans of up to \$50 billion, with most of the money coming from the U.S. Treasury. Mexico put forth efforts to demonstrate its commitment to fulfill all its financial obligations without a default on its debt by adopting tight monetary and fiscal policies to reduce inflation and absorb some of the costs of the banking sector crisis. The austerity plan included an increase in the value-added tax, budget cuts, increases in electricity and gasoline prices to decrease demand and government subsidies, and tighter monetary policy.<sup>14</sup>

## Effects of the Global Financial Crisis

The global financial crisis that began in 2008 resulted in a deepening of the recession in the U.S. economy that began in 2007. The U.S. economic contraction resulted in lower consumer demand in the United States and, consequently, lower demand for goods from Mexico. This has adversely affected Mexico's GDP growth, employment, production in the manufacturing industry, and investor confidence. Though real GDP growth has resumed in the United States, there is concern that the U.S. economy will not return to its pre-recession growth path or even remain permanently below it.<sup>15</sup> This will likely continue to have effects on economic conditions in Mexico.

### Effect on Mexico's GDP Growth

Mexico has experienced the deepest recession in the Latin America region following the recent global financial crisis, largely due to its high dependence on manufacturing exports to the United States, although other factors have also contributed. Other Latin American countries have experienced negative economic consequences from the financial crisis but to a lesser extent than

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<sup>12</sup> EIU, "Mexico Finance: The Peso Crisis, Ten Years On," January 3, 2005.

<sup>13</sup> Terms of trade is defined as the ratio of the price a country receives for its export commodity to the price it pays for its import commodity. If the prices of a country's exports have risen relative to the prices the country paid for its imports, then the country is said to have improved its terms of trade.

<sup>14</sup> Joachim Zietz, "Why Did the Peso Collapse? Implications for American Trade," *Global Commerce*, Volume 1, No. 1, Summer 1995.

<sup>15</sup> For more information, see CRS Report R41332, *Economic Recovery: Sustaining U.S. Economic Growth in a Post-Crisis Economy*, by Craig K. Elwell.

Mexico. In Central America, El Salvador had the deepest economic contraction (-3.6%), while in South America, Paraguay was the country with the deepest contraction (-3.8%). Economic growth in most Latin American countries was affected by the crisis but because most of these countries were experiencing high levels of growth prior to the crisis and are not as dependent on the U.S. economy, they did not experience as deep a recession as Mexico (see **Table 2**). The forecast for 2010 shows most of the economies in the Western Hemisphere rebounding to positive economic growth, with the exception of Venezuela, which is expected to experience a drop in real GDP growth of 5.5%, as shown in **Table 2** below.

**Table 2. Percent Change in Real GDP for Selected Countries: 2007-2009 and Projections for 2010-2011**

	2007	2008	2009 <sup>a</sup>	2010 <sup>b</sup>	2011 <sup>b</sup>
<b>North America</b>					
Canada	2.5	0.4	-2.5	3.2	2.1
<b>Mexico</b>	<b>3.3</b>	<b>1.5</b>	<b>-6.6</b>	<b>4.6</b>	<b>3.3</b>
United States	2.1	0.4	-2.4	2.7	2.0
<b>Central America</b>					
Belize	1.2	3.8	-0.9	1.0	0.6
Costa Rica	8.0	2.8	-1.1	3.6	3.5
El Salvador	4.2	2.4	-3.6	1.5	1.9
Guatemala	6.3	3.3	0.6	2.3	2.2
Honduras	6.3	4.2	-2.1	2.9	2.8
Nicaragua	3.1	2.8	-1.5	2.2	2.1
Panama	12.1	10.7	2.4	5.6	4.0
<b>South America</b>					
Argentina	8.7	6.8	0.9	6.8	4.0
Bolivia	4.6	6.2	3.4	4.0	3.8
Brazil	6.1	5.1	-0.2	7.8	4.5
Chile	4.6	3.7	-1.5	4.8	5.6
Colombia	6.3	2.7	0.8	4.6	4.4
Ecuador	2.0	7.2	0.4	2.3	2.3
Paraguay	6.8	5.8	-3.8	8.5	4.5
Peru	8.9	9.8	0.9	6.7	4.1
Uruguay	7.5	8.5	2.9	5.6	4.2
Venezuela	8.2	4.8	-3.3	-5.5	-2.5

**Source:** Compiled by CRS using data from the Economist Intelligence Unit online database.

**Notes:**

- a. Some figures are estimates.
- b. Forecast.

## Exports

In 2009, Mexico's total trade with the world declined sharply with lower demand in the United States for Mexican products and lower consumer demand in Mexico contributing to the decline. Mexico's exports to all countries decreased 21.5% to \$229.6 billion in 2009 (see **Table 3**). Imports also decreased in 2009, by 24.4% to \$234.4 billion. Exports to the United States decreased 17.6% in 2009. Prior to the recession, Mexico had been experiencing steady annual growth in exports. Between 2003 and 2008, Mexico's exports increased from \$164.8 billion to \$292.6 billion, an increase of 77.5%. Export volumes rose in November and December of 2009, with exports for December 2009 up 23.7% year-on-year from 2008. Preliminary figures by the Mexican government show an increase in exports of 7.6% year-on-year for the first six months of 2010.<sup>16</sup> U.S. trade data show that Mexico's exports to the United States from January-June 2010 are up 38.2% and imports from the United States are up 30.0% year-on-year.<sup>17</sup>

**Table 3. Mexico's Exports: 2003-2009**

(U.S.\$ in billions)

Mexico's Exports	2003	2004	2005	2006	2007	2008	2009	Change 2008-2009
To the United States	144.3	164.5	183.6	211.8	223.4	234.6	193.3	-17.6%
Total Exports	164.8	188.0	214.2	249.9	272.0	292.6	229.6	-21.5%

**Source:** Compiled by CRS using data from Mexico's Secretaría de Economía, Subsecretaría de Negociaciones Comerciales Internacionales.

## Employment

Mexico's labor market conditions deteriorated during the crisis and unemployment rose to its highest level since 2000. As a result, private consumption and retail sales fell significantly. The unemployment rate in the last quarter of 2009 was by far the highest figure in the past decade.<sup>18</sup> The unemployment problem is more severe in urban areas, with the unemployment rate in large cities reaching 7.6% while that in small communities was only 3.7%.<sup>19</sup> Government data on unemployment may not reflect deeper employment effects because the data include jobs in the informal sector, which are oftentimes very low-paying jobs that have no health or retirement benefits. A report by the International Monetary Fund stated that though the unemployment rate

<sup>16</sup> Based on data from Mexico's *Instituto Nacional de Estadísticas y Geografía*.

<sup>17</sup> Based on data from the United States International Trade Commission online database.

<sup>18</sup> IMF, "Mexico: 2010 Article IV Consultation – Staff Report and Public Information Notice on the Executive Board Discussion," IMF Country Report No. 10/71, p. 5.

<sup>19</sup> EIU, *ViewsWire*, "Mexico Economy: Pseudo Recovery," December 4, 2009.

peaked in September 2009, private consumption continued to lag afterwards and consumer confidence remained weak.<sup>20</sup>

The economic crisis has resulted in a shortage of opportunities in the formal economy in Mexico. Mexico's job market has a large informal sector and the crisis may have caused a growing trend towards informality and self-employment.<sup>21</sup> The formal sector of the economy contracted after the downturn while the number of jobs in the informal market increased. Informal sector jobs nearly doubled in the third quarter of 2009 when compared to the same period in 2008. One report estimates that 39.3% of the Mexican workforce is in the informal sector and that if workers classified as formal but receive no health coverage were included, the informality figure would rise to 45.3%.<sup>22</sup> Growth in the informal sector of the economy can present a social problem for the government because workers in the informal sector do not receive the same social benefits as workers in the formal sector. Informal employment tends to be concentrated among poor workers who may not have the ability to save for retirement, for a house, or have health insurance.<sup>23</sup>

The financial crisis effect has had a particularly adverse effect on young workers in Mexico, as it has in other parts of Latin American and developing countries worldwide. While an economic crisis can produce a positive effect of motivating students to stay in school longer, it can also have the opposite effect in countries such as Mexico with youths dropping out of school because they have lost career expectations. The level of unemployed youths represent a serious concern for the Mexican government due to the possibility of youths turning to criminal organizations for work and or attempting to migrate illegally to the United States. A top education official in Mexico who heads the national adult education program estimated that 700,000 young people dropped out of school last year.<sup>24</sup> The education program has made efforts to coordinate with various state education departments to target recent dropouts and get them back into the education system. Many of the youths who choose not to go back to school often end up in low-paid informal jobs. Those who do go back to college and graduate also face difficulties in finding employment in their field.<sup>25</sup>

## **Manufacturing**

Manufacturing industries have been severely affected by the decline in external demand, particularly in high-value added industries. The sharp drop in exports to the United States led to a large drop in industrial production. As a result, business and consumer confidence has weakened

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<sup>20</sup> IMF, *Mexico: 2010 Article IV Consultation – Staff Report and Public Information Notice on the Executive Board Discussion*, March 2010.

<sup>21</sup> Formal sector workers are defined as salaried workers employed by a firm that registers them with the Mexican government and are covered by Mexican labor regulations and laws. Informal sector workers are defined as self-employed individuals or workers who are hired by a firm that has not registered them formally with the Mexican government.

<sup>22</sup> EIU, *ViewsWire*, "Mexico Economy: Pseudo Recovery," December 4, 2009.

<sup>23</sup> Levy, Santiago, *Good Intentions, Bad Outcomes, Social Policy, Informality, and Economic Growth in Mexico* (Washington, D.C.: Brookings Institution Press, 2008), p. 8.

<sup>24</sup> Sara Miller Llana, "Unemployment among Latin America Youths Fuels 'Lost Generation'," *Christian Science Monitor*, March 12, 2010.

<sup>25</sup> *Ibid.*

to record lows and subsequently has put downward pressure on consumption and investment.<sup>26</sup> Job losses in Mexico increased in 2008 and 2009, with possibilities of further job losses in export-oriented assembly plants as they cut capacity due to the downturn in demand.

The annual growth rate of Mexico's industrial production decreased from 5.7% in 2006 to -0.6% in 2008 and to -10.1% in 2009. A higher demand for Mexican exports to the United States and a projected improvement in Mexico's domestic economy are expected to result in higher industrial production in the next two years. Production growth is projected to reach 4.1% in 2010 and 3.6% in 2011.<sup>27</sup>

The economic crisis, combined with the increased violence along the U.S.-Mexico border, has hurt the manufacturing industry and many of Mexico's export-oriented assembly plants have shut down in recent years, especially along the U.S.-Mexico border. A majority of these export-oriented plants have U.S. parent companies, though some parent companies are located in Asia and Europe. The border region with the United States has the highest concentration of assembly plants and workers.

Ciudad Juárez, Chihuahua, the city with the highest concentration of jobs in export assembly plants, has experienced the highest job losses, as a result of lower U.S. demand and the drug-related violence that has occurred in this manufacturing city over the past two years. Manufacturing employment in Cd. Juarez decreased from 214,272 in July 2007 to 168,011 in December 2009, a loss of 46,261 jobs (22% decrease). In Tijuana, Baja California, employment decreased from 174,105 in July 2007 to 136,957 in December 2009, a loss of 37,148 jobs (21% decrease). The total number of export-oriented manufacturing plants in Mexico increased from 5,083 in July 2007 to 5,245 in December 2009. However, employment decreased from 1,910,112 in July 2007 to 1,641,465 in December 2009, a loss of 268,647 jobs (14% decrease).<sup>28</sup>

## **Energy Sector**

Although the financial crisis did not impact the energy sector, Mexico's long-term economic recovery and stability will depend upon what happens in the oil industry. The Mexican government depends heavily on oil revenues, which provide 30% to 40% of the government's fiscal revenues, but oil production in Mexico is declining rapidly. Many analysts state that Mexican oil production has peaked and that the country's production will continue to decline in the coming years.<sup>29</sup> Mexico is the 7<sup>th</sup> largest producer of oil in the world and is one of the top three sources of U.S. oil imports, along with Canada and Saudi Arabia. Mexico's state oil company, *Petróleos Mexicanos* (Pemex) has stated that output from the country's biggest oilfield, Cantarell, is declining much more rapidly than expected.<sup>30</sup> Production is declining so rapidly,

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<sup>26</sup> Organization for Economic Cooperation and Development (OECD), *OECD Economic Surveys: Mexico*, July 2009.

<sup>27</sup> Global Insight, *Quarterly Review and Outlook: Latin America and Caribbean*, Fourth-Quarter 2009.

<sup>28</sup> *Ibid.*

<sup>29</sup> U.S. Energy Information Administration, *Country Analysis Briefs, Mexico Oil*, June 2010.

<sup>30</sup> *Latin America Weekly Report*, September 3, 2009, p. 11.

Mexico could possibly begin importing oil within ten years.<sup>31</sup> Mexico's exports of crude oil have been falling since 2006, and it is currently a net importer of both gasoline and natural gas.

The Cantarell oilfield is Mexico's main offshore field. Production at Cantarell has been declining rapidly since it reached its peak production level of 2.12 million barrels per day (b/d) in 2004. In 2009, Cantarell produced only 630,000 b/d, down 38% from the 2008 level and 70% from its peak in 2004.<sup>32</sup> National production has fallen for the fifth consecutive year. Nationally, Mexico produced 2.6 million barrels of oil per day in 2009, down from a record 3.4 million barrels per day in 2004. It exported 1.225 million barrels p/d in 2009, compared with 1.403 million barrels p/d in 2008.<sup>33</sup>

The Mexican government has used oil revenues from Pemex for government operating expenses, which has come at the expense of needed reinvestment in the company itself. Because the government relies so heavily on oil income, any decline in production has major fiscal implications.<sup>34</sup> According to one journal article, if oil output drops below two million b/d, the government would have to cut spending by more than 10% or increase taxes correspondingly, which would likely affect economic recovery.<sup>35</sup>

In 2008, the government enacted new legislation that sought to reform the country's oil sector, which was nationalized in 1938, and to help increase production capability. The reforms permit Pemex to create incentive-based service contracts with private companies. Some analysts contend, however, that the reforms did not go far enough and that they do little to help the company address its major challenges. Most experts contend that Pemex has only the capacity to produce in shallow waters and needs to bring in new technologies and know-how through private investment to allow the company to successfully explore and produce in the deep waters in the Gulf of Mexico.<sup>36</sup> The lack of further reforms is keeping Mexico from allowing much-needed foreign investment for oil exploration. Though the performance-based contracts are expected to increase production and reserves, Pemex faces serious challenges in finding new, productive wells and also lacks resources for investment in increasing engineering capacity and exploration, and has an operating deficit as of January 25, 2010.<sup>37</sup> It is estimated that Mexico may have about 50 billion barrels in the deeper waters of the Gulf of Mexico, but many experts contend that the country lacks the expertise, technology, and capital it needs for oil exploration.<sup>38</sup>

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<sup>31</sup> Clifford Krauss and Elisabeth Malkin, "Mexico Oil Politics Keeps Riches Just Out of Reach," *New York Times*, March 9, 2010.

<sup>32</sup> U.S. Energy Information Administration, *Country Analysis Briefs, Mexico Oil*, June 2010.

<sup>33</sup> Center for Strategic and International Studies (CSIS) Americas Program, *Hemisphere Highlights*, January 2010, p. 2.

<sup>34</sup> *Latin America Weekly Report*, September 3, 2009, p. 11.

<sup>35</sup> "How many Mexicans does it take to drill an oil well?," *The Economist*, October 3-9<sup>th</sup>, 2009, p. 43.

<sup>36</sup> Woodrow Wilson International Center for Scholars, Latin American Program, *The Outlook for Energy Reform in Latin America*, March 2010.

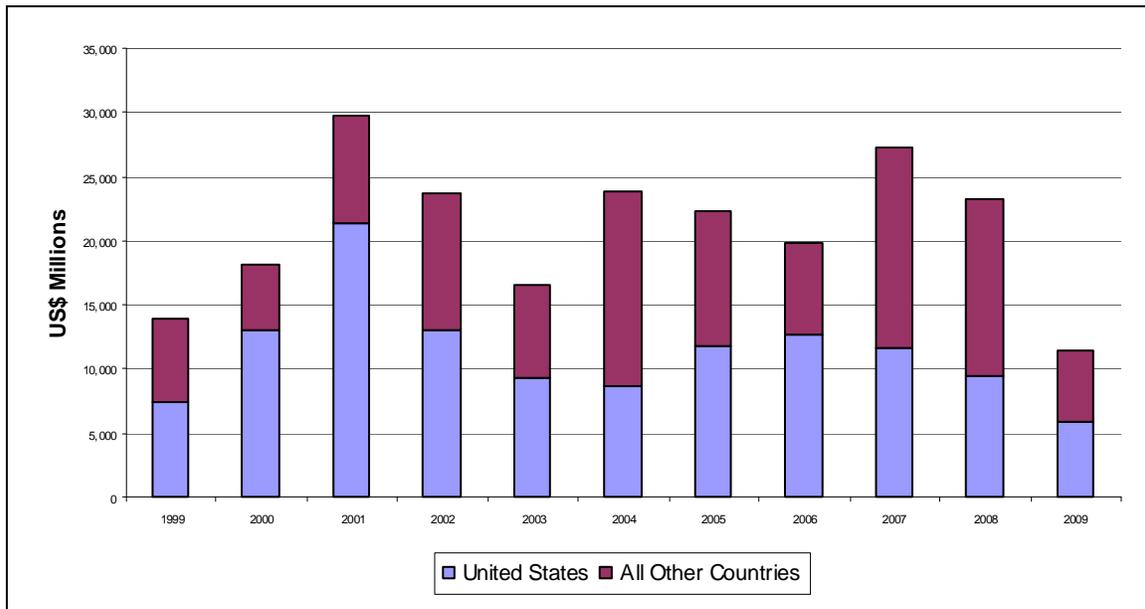
<sup>37</sup> CSIS Americas Program, *Hemisphere Highlights*, January 2010, p. 2.

<sup>38</sup> "How many Mexicans does it take to drill an oil well?," *The Economist*, October 3-9<sup>th</sup>, 2009, p. 43.

## Foreign Direct Investment Declines

The flows of FDI to Mexico dropped sharply in 2009. Although investment decisions are affected by a number of factors, the Mexican government attributed a large percentage of the decline to the global financial crisis.<sup>39</sup> Total FDI flows to Mexico decreased by 50.7%, from \$23.1 billion in 2008 to \$11.4 billion in 2009. Investment flows to Mexico have been fluctuating since during the 10-year period between 1999 and 2009 as shown in **Figure 2**. The highest growth rate of total investment flows to Mexico during this period was 43.6% in 2004, after a decline of 29.8% during the previous year. The United States is the largest investor in Mexico, accounting for slightly over 50% of investment flows in 2009 and for 54.1% of cumulative investment flows between 1999 and 2009. U.S. inflows totaled \$5.8 billion in 2009, down from \$9.5 billion in 2008, a 38.8% decrease. Other major foreign investors in Mexico are Spain and Holland, accounting for 15.2% and 10.7%, respectively, of cumulative investment flows between 1999 and 2009, respectively.<sup>40</sup>

**Figure 2. Flows of Foreign Direct Investment to Mexico**  
(US\$ Millions)



**Source:** Produced by CRS using data from Mexico's *Secretaría de Economía, Dirección General de Inversión Extranjera*.

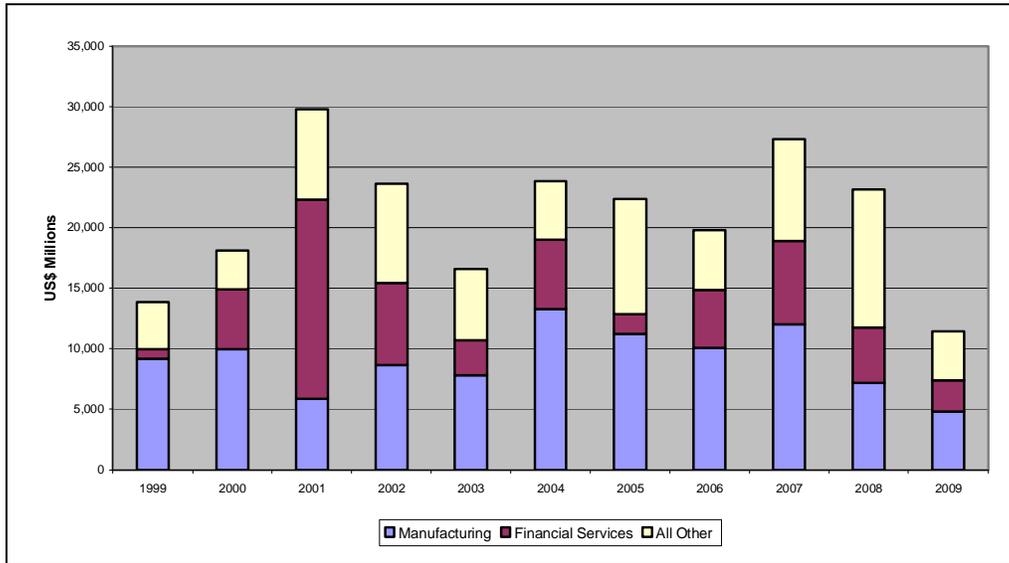
<sup>39</sup> Agence France-Presse, "Foreign Investment Plunges 50 Percent in Mexico," February 25, 2010.

<sup>40</sup> Mexico's *Secretaría de Economía, Dirección General de Inversión Extranjera*.

U.S. foreign direct investment in Mexico has increased considerably since the implementation of NAFTA. The stock of U.S. FDI in Mexico increased from \$17.0 billion in 1994, the year of NAFTA's implementation, to \$95.6 billion in 2008. Although NAFTA's foreign investment provisions may have encouraged U.S. investment by increasing investor confidence, there is a likelihood that much of the growth would likely have occurred anyway because of Mexico's liberalization policies on foreign investment in the late 1980s and early 1990s.

Most foreign investment in Mexico is in the manufacturing industry, of which the maquiladora industry is a part, and in financial services. Both sectors experienced declines in investment flows in 2009 following the global financial crisis. Approximately 44% of cumulative FDI flows to Mexico between 1999 and 2009 were in manufacturing and 26% were in financial services. FDI flows in manufacturing decreased by 32.6% in 2009, from \$7.2 billion in 2008 to \$4.8 billion in 2009, after reaching a peak of \$13.3 billion in 2004 during the 1999-2009 period (see **Figure 3**). FDI flows in financial services decreased from \$4.6 billion in 2008 to \$2.6 billion in 2009 (44%).

**Figure 3. Foreign Direct Investment Flows to Mexico by Sector**  
(US\$ Millions)



**Source:** Produced by CRS using data from Mexico's *Secretaría de Economía, Dirección General de Inversión Extranjera*.

## Fall in Remittances

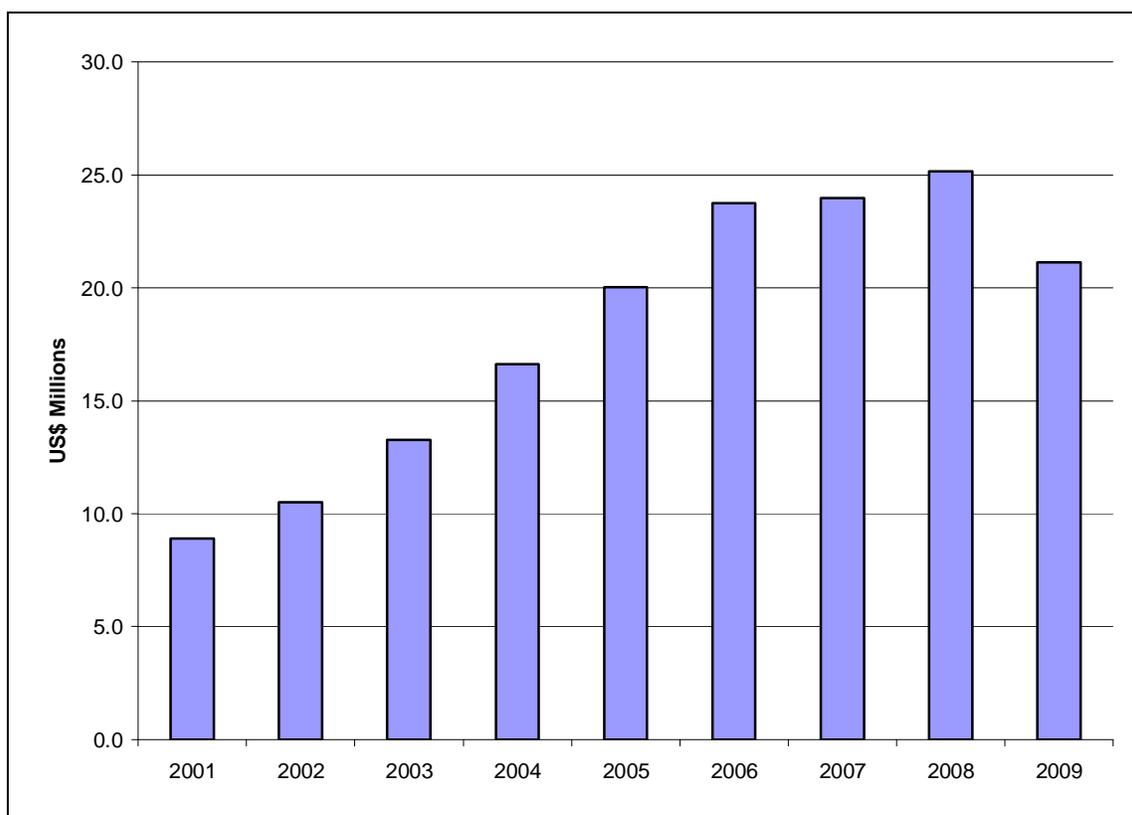
On January 27, 2010, the *Banco de México* (Mexico's Central Bank) reported that remittance inflows fell 16.0% in 2009 to \$21.1 billion (see **Figure 4**). The decline in remittances is mostly due to the global financial crisis and the slowdown in the U.S. economy as the rising jobless rate has taken a toll on Mexican immigrants in the United States. Remittances are the second-highest source of foreign currency after oil, with tourism revenues following in third place. Mexico receives the largest amount of remittances in Latin America and the third largest in the world, after India and China. Many of the Mexican workers in the United States who send money back to their families work in the construction and services sectors, which have both been negatively affected by the financial crisis. Approximately 239,000 immigrant Hispanics, of which Mexicans

comprise 30%, lost their jobs in 2008, with almost 100,000 of these jobs in the construction industry, according to one estimate.<sup>41</sup>

The decline in remittances to Mexico is significantly greater than the fall in remittances to other countries dependent on the U.S. economy. In Central America and the Caribbean remittances also fell in 2009 but by considerably lower percentages. In El Salvador, remittances fell 8.5% to \$3.6 billion and in Honduras, the fall was 11.1%.<sup>42</sup> Remittances to Mexico are expected to grow 5% in 2010.<sup>43</sup>

**Figure 4. Remittances to Mexico: 2001-2009**

US\$ Millions



**Source:** Compiled by CRS using data from the Inter-American Development Bank, The Multilateral Investment Fund.

For a number of years, remittances were considered a stable financial flow for Mexico as workers in the United States made efforts to send money to family members, especially to regions of the country experiencing economic crises or natural disasters. Annual remittances to Mexico grew substantially between 2001 and 2008, from \$8.9 billion to \$25.1 billion, an increase of 182.0%.

<sup>41</sup> Joel Millman, "Remittances to Mexico Fall More than Forecast," *The Wall Street Journal*, January 28, 2009, p. A3.

<sup>42</sup> "What Mexico's Record Drop in Remittances Means," *Latin American Economy and Business*, January 2010.

<sup>43</sup> Ibid.

The annual growth rate reached a high of 26.3% in 2003, continuing to increase annually at a slower rate until 2009 (see **Table 4**). There is an interrelationship between remittances to Mexico and economic growth in the United States, but not much is known about the extent of this relationship.<sup>44</sup> Although the relationship between GDP growth in the United States and the level of remittances is not very clear, the Mexican government attributes the 2009 decline to the global financial crisis.<sup>45</sup>

**Table 4. Remittances to Mexico and U.S. Real GDP Growth**

US\$ Billions and Percentages

	2001	2002	2003	2004	2005	2006	2007	2008	2009
Amount	\$8.9	\$10.5	\$13.3	\$16.6	\$20.0	\$23.7	\$24.0	\$ 25.1	\$21.1
Change	—	18.5%	26.3%	25.2%	20.6%	18.5%	1.0%	4.9%	-16.0%
Change in U.S. Real GDP	1.1%	1.8%	2.5%	3.6%	3.1%	2.7%	2.1%	0.4%	-2.4%

**Source:** Compiled by CRS using data from the Inter-American Development Bank, The Multilateral Investment Fund; and the Economist Intelligence Unit on-line database.

Mexico’s remittance inflows represent a lower percentage of GDP (less than 4%) than countries in Central America where the inflow could be as high as 16% of GDP, yet many of the poorest communities in Mexico rely on this money for their day-to-day life. Remittances tend to go mostly to areas that are lacking in economic opportunities in the poorer regions of Mexico, and some states have been more severely affected by recent declines than others.<sup>46</sup> Remittances are often a vital lifeline for the poor in Mexico; states that experience more drastic declines may be particularly exposed to risk.<sup>47</sup> A large majority of families spend the money on basic needs, such as rent, food, medicine, or utilities.

The financial crisis had significant effects on poverty in Mexico. One study estimates that the crisis will raise the poverty rate by nearly four percentage points between 2008 and 2010. The study also estimates that the poorest 20% of Mexican households will suffer an average loss in per capita income of about 8% between 2008 and 2010, compared with 5% for the entire population. This loss would be in addition to any declines in existing safety-net government transfers that benefit many of the extremely poor in Mexico.<sup>48</sup> Poverty has been one of Mexico’s more serious economic challenges for many years and the government has made significant efforts to address this issue. These efforts were effective in bringing down the poverty rate between 2000 and 2007. However, poverty rates increased in 2008. The extreme poverty rate

<sup>44</sup> Migration Policy Institute, *Migration Facts*, “Variable Impacts: State-level Analysis of the Slowdown in the Growth of Remittances to Mexico,” September 2007.

<sup>45</sup> “Mexico Sees Record 15.7 percent Annual Drop in Money Sent Home by Migrants,” Associated Press, January 27, 2010.

<sup>46</sup> “What Mexico’s Record Drop in Remittances Means,” *Latin American Economy and Business*, January 2010.

<sup>47</sup> *Ibid.*

<sup>48</sup> The World Bank, *Economic Premise*, “The Impact of the Financial Crisis on Poverty and Income Distribution: Insights from Simulations in Selected Countries,” March 2010.

went up to 18% in 2008, after having fallen from 24% to 14% between 2000 and 2006. Mexico's continuing problem of poverty is especially widespread in rural areas and remains at the Latin American average.<sup>49</sup> In rural areas the percentage of those living in moderate poverty was 61% in 2008, while that of those living in extreme poverty was 32%. The rates for urban areas were 40% and 11%, respectively.<sup>50</sup>

## Structural and Other Economic Challenges

Mexico's past economic reforms have helped the country modify its macroeconomic policies and restore policy credibility since the 1995 currency crisis. Key reforms included measures to reduce public debt, the introduction of a balanced budget rule, an inflation targeting framework and a floating exchange rate policy.<sup>51</sup> The measures have been successful in stabilizing inflation, achieving balanced federal budgets, reducing public debt, reducing exposures to currency risk, and lowering current account deficits and foreign financing needs. In addition, the government's actions to build up its foreign reserves helped the country to avoid the financial stress that other emerging markets experienced due to the 2008 global financial crisis.<sup>52</sup> Despite these improvements, numerous political analysts and economists agree that Mexico needs significant political and economic structural reforms to improve its potential for long-term economic growth.

The government's responses to the recent global financial crisis helped the country weather the 2009 recession and improve conditions in 2010. The government used a number of tools, including macroeconomic policies, targeted assistance to financial institutions, interventions by Mexico's Central Bank to cut interest rates and maintain the country's liquidity, and actions to increase confidence by securing lines of credit. Mexico worked with the U.S. Federal Reserve and the International Monetary Fund (IMF) to secure a \$30 billion swap line from the U.S. Federal Reserve and an IMF Flexible Credit Line of \$47 billion.<sup>53</sup> Though Mexico did not use the credit lines, the arrangements helped to improve confidence in the economy. The government also took measures in the FY2010 budget by including substantive tax reforms to offset revenue losses from lower oil production.<sup>54</sup> Mexico's key challenge over the next few years will likely be the issue of further reforms in the tax system to replace the declining share of oil revenues with tax revenues. With its tax revenues representing only 10% of GDP, Mexico has one of the lowest tax collection rates in Latin America and it is not viewed as being enough to meet the country's social needs.<sup>55</sup> Though the government has already taken some steps to increase tax revenues, economists generally agree that Mexico needs further tax reforms to broaden its tax base.

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<sup>49</sup> "What Mexico's Record Drop in Remittances Means," *Latin American Economy and Business*, January 2010.

<sup>50</sup> *Poverty Report*, Consejo Nacional de Evaluación de la Política de Desarrollo Social (CONEVAL), July 18, 2009.

<sup>51</sup> "Mexico Recovering, but Crisis Spotlights Challenges, says IMF," *IMF Survey Magazine: In the News*, March 16, 2010.

<sup>52</sup> OECD, *OECD Surveys – Mexico*, July 2009, p. 11.

<sup>53</sup> IMF, "IMF Executive Board Concludes 2010 Article IV Consultation with Mexico," Public Information Notice (PIBN) No. 10/39, March 16, 2010, pp. 1-2.

<sup>54</sup> *Ibid.*

<sup>55</sup> OECD, *OECD Surveys – Mexico*, July 2009, p. 13.

One of Mexico's primary challenges in making its economy more efficient and increasing productivity is the issue of monopolies and limited competition. A 2009 book co-published by the World Bank and Palgrave Macmillan,<sup>56</sup> as well as numerous reports and journal articles, report that special interest groups in business and labor have blocked changes in Mexico that would introduce more market forces into the economy. The publication *No Growth Without Equity* states that "Mexico seems to be caught up in a high-inequality, low growth state" and that reforms must be put into place in order for Mexico to improve economic growth.

One key issue discussed in the World Bank-Palgrave Macmillan book is the oil industry, which, according to the book, is controlled by the federal government and the oil industry labor union whose own interests are not in balance with the interests of Pemex. The book notes that the "passivity" with which these groups have exercised their property rights with respect to Pemex have hindered the performance of the oil industry and its capacity to grow.<sup>57</sup> The book argues that the influence and power of the federal government, the energy-intensive industrial firms, and the industry's labor union have prevented change from taking place in the oil sector because change would eliminate many of the benefits they have received for many years.<sup>58</sup> Pemex's labor union has resisted change because thousands of jobs are at stake if the company were to be opened up to competition. The large industrial companies that use large amounts of energy at subsidized prices do not want to lose these benefits under a more competitive environment.<sup>59</sup>

The country's telecommunications sector is another area that is frequently mentioned as not having enough competition and being controlled by a monopoly. *Teléfonos de México* controls the telecommunications market in Mexico and has successfully fought antitrust regulators in court. As a result, Mexico's telecommunications industry has probably not developed as fast as it could if more competition were introduced.<sup>60</sup>

Some also argue that another challenge to the Mexican economy are the powerful labor unions. Mexico's labor unions have a monopoly on hiring, firing and collective bargaining and exert a great deal of influence in the energy and healthcare industries, and most importantly, in education. The National Teacher's Union, for example, is the biggest teachers' union in Latin America and the most powerful in Mexico. Analysts argue that the monopolist control over such a large portion of public and private sector activities in Mexico is limiting economic growth in Mexico and preventing the development of a "middle-class society" in Mexico.<sup>61</sup>

In September 2009, President Calderón delivered his third state of the union address to the Mexican Congress and proposed a number of reforms to address the economic and political challenges facing the country. These reforms included the following:

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<sup>56</sup> Levy, Santiago, and Michael Walton, editors, *No Growth Without Equity? – Inequality, Interests, and Competition in Mexico*, (Washington, DC: Palgrave MacMillan and The World Bank, 2009).

<sup>57</sup> Ibid, p. 412.

<sup>58</sup> Ibid., p. 417.

<sup>59</sup> Elisabeth Malkin, "Are Monopolies Holding Mexico Back," *The New York Times*, June 2, 2009.

<sup>60</sup> Ibid.

<sup>61</sup> Jorge Castañeda, "A Paralyzed Democracy – How to Move Mexico Into the Future," *Newsweek*, February 12, 2010.

- Proposals to eliminate extreme poverty, introduce universal healthcare, and improve the quality of education for all children.
- Public sector finance reform.
- Transformation of state enterprises, which would privatize some parts of the state oil monopoly Pemex.
- Telecommunications sector reform to increase coverage and allow more competition in this sector.
- Labor reform measures to bring more flexibility to the labor market by making it easier for companies to hire and fire.
- Regulatory reform, with the aim of reducing unnecessary government regulations and making the government less bureaucratic.
- Increase of government coordination and citizen participation in the war against organized crime.
- Fundamental political reform, which would allow re-election for some public offices.<sup>62</sup>

The prospects for passage of President Calderón's proposals by the Mexican Congress are not viewed as very likely. Some of the proposals are viewed as highly controversial and have deep-seated political implications and efforts to restructure the energy sector or to adopt labor and fiscal reforms have been strongly opposed by the major political parties. Without the structural reforms necessary to bring about significant changes, Mexico's potential to increase economic growth, boost development, and lower the poverty rate will likely be very limited.<sup>63</sup> However, there are signs that the population may be pushing for change and much will depend on the outcome of the 2012 presidential election.

Another serious economic challenge in Mexico is related to the violence taking place in some regions of Mexico after President Calderón's campaign against organized crime and drug trafficking. The escalation of violence has resulted in increased risk aversion which has impacted foreign investment flows, particularly in the manufacturing industry. The costs from the drug trade far outweigh any of the benefits that drug-trafficking and associated crime might bring in terms of increased cash flows or positive spill-over effects. Some estimates of the costs associated with violence, investment losses, drug abuse, and other direct costs are estimated at \$4.6 billion per year, or 0.5% of GDP.<sup>64</sup> Costs could be even higher when taking into account the indirect costs of large numbers of violence-related outward migration, which lowers Mexico's potential growth rate.<sup>65</sup> The city planning department of Juárez estimates 116,000 homes were abandoned as of early 2010 because of the violence. This could translate into a population of up to 400,000

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<sup>62</sup> "Mexico and NAFTA," *Latin American Regional Report*, September 2009, pp. 2-4.

<sup>63</sup> *Ibid.*, p. 3.

<sup>64</sup> EIU, *Country Report – Mexico*, July 2010, pp. 13-14.

<sup>65</sup> *Ibid.*

people, one-third of the city, that has migrated.<sup>66</sup> Violence has also had a severe impact on employment in Juárez, with the city losing 23.9% (91,940) of its formal jobs.<sup>67</sup>

Some analysts believe that Mexico must increase investor confidence to remain competitive because the drug violence is causing anxiety and uncertainty among investors. Cd. Juárez, which is close to the border with the United States and where much of the manufacturing industry is located, was, until recently, considered an attractive city for foreign investors and for doing business. However, the border violence that has erupted since Mexico's crackdown on organized crime has changed the business environment and business leaders have been forced to take steps in increasing security in manufacturing plants such as abolishing overtime so that workers can go home before sunset. The *Asociación de Maquiladoras*, a local trade group located in Juárez, states that some foreign investors have passed on opening plants in Juárez since 2008, but that this was due to the recession and not to the increase in violence.<sup>68</sup>

## Implications for the United States

The relationship between the United States and Mexico is important to policymakers from both countries because of the mutual interest in a number of key issues affecting the two countries such as bilateral trade, economic competitiveness, and border security. During his state visit to Washington, D.C., in May 2010, Mexican President Felipe Calderón emphasized the need for increased cooperation in North America in order to increase the competitiveness of the region.<sup>69</sup> President Barack Obama hosted a meeting with President Calderón where the two leaders discussed numerous key bilateral and hemispheric issues affecting the two countries. The leaders reaffirmed the shared values in areas such as economic competitiveness, social and economic well-being, and the security of citizens in both countries. One area of cooperation that was highlighted in a press release after the meeting was the need for mutual economic growth. The two leaders vowed to enhance and reinforce efforts to create jobs, promote economic recovery and expansion, and encourage inclusive prosperity across all levels of society in both countries.<sup>70</sup>

The two leaders discussed the following actions for bilateral cooperation to enhance competitiveness: 1) the creation of a Twenty-First Century Border to facilitate the secure and efficient flow of goods and people and reduce the cost of doing business between the two countries; 2) a commitment to continuing cooperation for safe, efficient, secure, and compatible modes of transportation; 3) a commitment to significantly enhance the economic competitiveness and the economic well-being of both countries through improved regulatory cooperation; and 4) the enhancement of intellectual property rights protection to promote innovation and investment in technology and human capital.<sup>71</sup> The two leaders also underscored the importance of human

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<sup>66</sup> Nicholas Casey, "Cartel Wars Gut Juárez, Onetime Boom Town," *Wall Street Journal*, March 20, 2010.

<sup>67</sup> Gobierno Federal de México, *Todos Somos Juárez: Reconstruyamos la Ciudad*, May 2010.

<sup>68</sup> Nicholas Casey, "Juárez Violence Puts Factories on Defensive—Executives Train to Foil Kidnappings, Drive in Convoys as Drug Cartels," *Wall Street Journal*, March 26, 2010.

<sup>69</sup> CSIS Americas Program, *Hemisphere Highlights*, May 2010, pp. 1-2.

<sup>70</sup> The White House, "Joint Statement from President Barack Obama and President Felipe Calderón," press release, May 19, 2010.

<sup>71</sup> *Ibid.*

capital and touched upon the issue of immigration. President Obama underscored his commitment to comprehensive immigration reform in the United States while President Calderón stated that his administration was committed to creating more job and educational opportunities in Mexico. Both leaders acknowledged the importance of taking actions to address the problem of illegal immigration, border security, human trafficking groups, and agreed to set priorities for the future.<sup>72</sup>

The economic relationship between the United States and Mexico is highly interdependent with NAFTA playing a central role. The Mexican truck issue is the main trade issue related to NAFTA that has concerned policymakers over the past few years. Under NAFTA, Mexican commercial trucks were to have been given full access to four U.S. border states in 1995 and full access throughout the United States in 2000. Citing safety concerns, however, the United States refused implementation of NAFTA's trucking provisions and the Mexican government objected. In the 111<sup>th</sup> Congress, the U.S. Congress terminated a cross-border trucking pilot program that was launched by the Bush Administration. The program was terminated under FY2009 Omnibus Appropriations Act (P.L. 111-8). On April 2, 2009, a trade association representing carriers in Mexico's trucking industry filed a notice of arbitration under the investment chapter (Chapter 11) of NAFTA. The notice of arbitration alleges that the U.S. Department of Transportation restricts Mexican carrier operations in the United States and Mexican investment in U.S. carriers, which is in violation of NAFTA Articles 1102 and 1103. It also charges that the United States has failed to comply with a 2001 ruling by a NAFTA dispute resolution panel. Mexico retaliated on the termination of the trucking program by imposing tariffs on 90 U.S. products exported to Mexico with an estimated value of \$2.4 billion.<sup>73</sup>

During his state visit to the United States, President Calderón stated during a press conference that the trucking dispute impacts jobs, companies, and consumers in Mexico and in the United States.<sup>74</sup> President Obama has pledged to work with Mexico to overcome the obstacles in implementing NAFTA trucking provisions. U.S. Transportation Secretary Ray LaHood stated in June 2010 that the Obama Administration would be relaunching the cross-border trucking program with Mexico and would present a proposal to Congress soon.<sup>75</sup>

Another key issue that could have significant implications for the United States is Mexico's declining oil production. Mexico is one of the United States' top three suppliers of crude petroleum oil. If Mexico is unable to continue oil production at the same level, the United States may no longer be able to rely on Mexico as a source of oil imports. However, there is a possibility that the Mexican government will eventually pass reform measures to allow foreign investment for increased engineering capacity and exploration. This could bring opportunities for U.S. companies in drilling and exploration services and could increase U.S. merchandise exports such

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<sup>72</sup> Ibid.

<sup>73</sup> For more information, see CRS Report RL31738, *North American Free Trade Agreement (NAFTA) Implementation: The Future of Commercial Trucking Across the Mexican Border*, by John Frittelli.

<sup>74</sup> Rossella Brevetti, "Obama, Mexico's Calderon Discuss Obstacles to Resolving Truck Dispute," *International Trade Daily*, May 20, 2010.

<sup>75</sup> Rosella Brevetti, "DOT's LaHood Says Truck Program with Mexico Needs to be Relunched," *International Trade Reporter*, June 17, 2010.

as electrical apparatus, valves, pipes, pumps, electric motors and generators, and other related goods.<sup>76</sup>

Some proponents of improving the economic relationship between Mexico and the United States recommend that the two countries work more closely on regulatory cooperation and deepen the economic relationship. Numerous analysts believe that the economic challenges that Mexico is facing are contributing to poverty and organized crime, and that a prosperous and democratic Mexico is in the best interest of the United States. One suggestion is that Mexico and the United States change the relationship from the current emphasis on anti-narcotic efforts and welcome a new stage in bilateral relations by focusing on other concepts such as immigration reform in the United States, energy reform in Mexico, security concerns, harmonization of standards and regulations, and legitimate security and border issues across the region.<sup>77</sup> Another observer contends that Mexico's dependence on the U.S. economy diminishes its ability to diversify its markets and also limits the extent of Mexico's long-term potential for economic growth. He states that the two countries should work together to jointly improve their global competitiveness and in sectors where co-production is possible, but that this will not work if either of the two countries protects itself against imports from the other.<sup>78</sup>

Opponents of further North American integration contend that trade liberalization under NAFTA has been harmful to the U.S. economy and resulted in large job losses in the United States. Legislation was introduced in the 111<sup>th</sup> Congress for the United States to withdraw from NAFTA (H.R. 4759). The bill would require the president to give written notice to Mexico and Canada of the U.S. withdrawal, which would occur six months after the bill's enactment. The bill had 27 co-sponsors and was referred to the House Ways and Means Committee. Supporters of the bill argue that NAFTA did not live up to its promises and that it has resulted in large job losses in the United States and Mexico. Opponents of the bill contend that NAFTA has had overall positive economic effects in all three countries of North America and that withdrawing from NAFTA would diminish trade and investment flows across the region, hurting U.S. exports and economic growth and causing more job losses. The higher tariffs, they argue, would hurt U.S. exports to Mexico. They point to the losses in exports that have occurred already from Mexico's retaliatory tariffs due to the trucking dispute and those exports represent only a small percentage of total U.S. exports to Mexico.<sup>79</sup>

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<sup>76</sup> Department of Commerce, U.S. Commercial Service – Mexico, Energy Industry, see <https://www.buyusa.gov>.

<sup>77</sup> Jorge Castañeda, "Time for a reset in U.S.-Mexican relations," *The Washington Post*, May 17, 2010.

<sup>78</sup> Center for Strategic and International Studies, *Mexico's Periodic Bad Times*, by Sidney Weintraub, August 2009.

<sup>79</sup> *International Trade Reporter*, "Legislation for Withdrawal from NAFTA Introduced in House with Bipartisan Support," March 11, 2010.

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