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Mexico's Free Trade Agreements

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Summary

Mexico has had a growing commitment to trade integration through the formation of free trade agreements (FTAs) since the 1990s and its trade policy is among the most open in the world. Mexico's pursuit of FTAs with other countries not only provides economic benefits, but could also potentially reduce its economic dependence on the United States. The United States is, by far, Mexico's most significant trading partner. About 80% of Mexico's exports go to the United States and 49% of Mexico's imports come from the United States. Mexico's second largest trading partner is China, accounting for approximately 6% of Mexico's exports and imports. In an effort to increase trade with other countries, Mexico has a total of 11 trade agreements involving 41 countries. These include agreements with most countries in the Western Hemisphere including the United States and Canada, Chile, Costa Rica, Nicaragua, Guatemala, El Salvador, and Honduras. In addition, Mexico has negotiated FTAs outside of the Western Hemisphere and entered into agreements with Israel and the European Union in July 2000. Mexico also has an FTA with Japan.

Economic motivations are generally the major driving force for the formation of free trade agreements among countries, but there are other reasons countries enter into FTAs, including political and security factors. One of Mexico's primary motivations for the unilateral trade liberalization efforts of the late 1980s and early 1990s was to improve economic conditions in the country, which policymakers hoped would lead to greater investor confidence and attract more foreign investment. Trade agreements are also expected to improve investor confidence, attract foreign investment, and create jobs. Mexico may have other reasons for entering into FTAs, such as expanding market access and decreasing its reliance on the United States as an export market. The slow progress in multilateral negotiations may also contribute to the increasing interest throughout the world in regional trade blocs. Some countries may see smaller trade arrangements as "building blocks" for multilateral agreements.

Since Mexico began trade liberalization in the early 1990s, its trade with the world has risen rapidly, with exports increasing more rapidly than imports. Mexico's trade balance with all countries went from a deficit of $13.5 billion in 1993 to surpluses of $7.1 billion in 1995 and $6.5 billion in 1996. Since 1998, Mexico's trade balance has remained in deficit, reaching $17.5 billion in 2008 and then declining to $4.8 billion in 2009. The trade balance with the United States went from a deficit of $2.4 billion in 1993 to a surplus of $72.5 billion in 2009. Exports to the United States increased from $42.9 billion in 1993 to $234.6 billion in 2008, and then declined to $184.9 billion in 2009. Mexico's imports from the United States increased from $45.3 billion in 1993 to $152.6 billion in 2008, and then declined to $112.4 billion in 2009 due to the economic downturn.

In the 111th Congress, issues of concern related to the trade and economic relationship with Mexico involve mostly economic conditions in Mexico, issues related to the North American Free Trade Agreement (NAFTA), the effect of NAFTA, economic conditions in Mexico and Mexican migrant workers in the United States. This report provides an overview of Mexico's free trade agreements, its motivations for trade liberalization and entering into free trade agreements, and some of the issues Mexico faces in addressing its economic challenges.

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Introduction

The number of regional trade agreements (RTAs) throughout the world has grown steadily since the early 1990s. One of the reasons for the increasing interest in bilateral or regional trade agreements is the impasse of the Doha Development Agenda (DDA). Many members of the World Trade Organization (WTO) are focusing on regional or bilateral free trade agreements as a key component of their foreign and commercial policy.[1] This interest is evident among industrialized and developing countries, and throughout various world regions, including numerous countries in the Americas, Europe, and Asia. Mexico is a member of the WTO, which permits members to enter into regional trade integration arrangements under certain conditions that are defined within specific WTO rules.[2]

Since the early 1990s, Mexico has had a growing commitment to trade liberalizations and has a trade policy that is among the most open in the world. Mexico has actively pursued free trade agreements with other countries to help promote economic growth, but also to reduce its economic dependence on the United States. The United States is, by far, Mexico's most significant trading partner. Over 80% of Mexico's exports are destined for the United States. In an effort to increase trade with other countries, Mexico has entered into eleven free trade agreements with 41 countries.[3] The government has used trade liberalization as one of a number of policy tools to improve economic growth and has other programs to promote economic development and to reduce poverty.

In the 111th Congress, issues of concern related to the trade and economic relationship with Mexico involve mostly issues related to the North American Free Trade Agreement (NAFTA), the effects of NAFTA, economic conditions in Mexico, and Mexican migrant workers in the United States. This report provides an overview of Mexico's free trade agreements, its motivations for trade liberalization and entering into free trade agreements, and some of the issues Mexico faces in addressing its economic challenges. This report will be updated as events warrant.

Motivations for Trade Integration

Economic motivations are generally the major driving force for the formation of free trade agreements (FTAs) among countries, but there are other reasons countries enter into FTAs, including political and security factors. One of Mexico's primary motivations for the unilateral trade liberalization efforts of the late 1980s and early 1990s was to improve economic conditions in the country, which policymakers hoped would lead to greater investor confidence and attract more foreign investment. This motivation was a major factor in negotiating NAFTA with the United States and Canada. The permanent lowering of trade and investment barriers and predictable trade rules provided by FTAs can improve investor confidence in a country, which helps attract foreign direct investment (FDI). Multinational firms invest in countries to gain access to markets, but they also do it to lower production costs.

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[1] See CRS Report RL32060, *World Trade Organization Negotiations: The Doha Development Agenda*, by Ian F. Fergusson.

[2] For more information on the specific sets of rules governing regional trade agreements among WTO members, see *Regional Trade Agreements: Rules* on the WTO website, see http://www.wto.org.

[3] World Trade Organization (WTO), Regional Trade Agreement Database, see http://www.wto.org.

Mexico has other motivations for continuing trade liberalization with other countries, such as expanding market access for its exports and decreasing its reliance on the United States as an export market. By entering into trade agreements with other countries, Mexico is seeking to achieve economies of scale in certain sectors of the economy and to expand its export market. Free trade agreements provide partners with broader market access for their goods and services. Countries can benefit from trade agreements because producers are able to lower their unit costs by producing larger volumes for regional markets in addition to their own domestic markets.[4] When more units of a good or a service can be produced on a larger scale, companies are able to decrease cost of production.

The slow progress in multilateral negotiations in the World Trade Organization (WTO) is another likely factor in Mexico's motivations to enter into FTAs. Some countries see smaller trade arrangements as "building blocks" for multilateral agreements. Other motivations are political. Mexico may be seeking to demonstrate good governance by locking in political and economic reforms through trading partnerships. Trade agreements could forge geopolitical alliances and strengthen diplomatic ties. Some analysts believe that the choice of RTA partners is increasingly based on political and security concerns and not so much on economic rationale.[5]

Mexican Trade Liberalization

From the 1930s through part of the 1980s, Mexico maintained a strong protectionist trade policy in an effort to be independent of any foreign power and as a means to promote domestic-led industrialization. Mexico established a policy of import substitution in the 1930s, consisting of a broad, general protection of the entire industrial sector. Mexico placed tight restrictions on foreign investment and controlled the exchange rate to encourage domestic industrial growth. Mexico also nationalized the oil industry during this time. These protectionist economic policies remained in effect until the country began to experience a series of economic challenges in the 1980s.

In the mid-1980s, Mexico's economy was on the verge of collapse as a result of the 1982 debt crisis in which the Mexican government was unable to meet its foreign debt obligations. Much of the government's efforts in addressing these economic challenges were placed on privatizing state industries and moving toward trade liberalization. Mexico had few options but to open its economy through trade liberalization. In the late 1980s and early into the 1990s, Mexico implemented a series of measures to restructure the economy that included unilateral trade liberalization, replacing import substitution policies with others aimed at attracting foreign investment, lowering trade barriers and making the country competitive in non-oil exports. In 1986, Mexico acceded to the General Agreement on Tariffs and Trade (GATT), assuring further trade liberalization measures that led to closer ties with the United States.

In 1990, Mexico approached the United States with the idea of forming a free trade agreement. In 1992, however, before NAFTA came into force, Mexico entered into its first agreement for free trade in goods, the Mexico-Chile FTA. Two years later, NAFTA, entered into force with much

[4] For more information on the costs and benefits of regional trade agreements, see Cohen, Stephen D., Robert A. Blecker, and Peter D. Whitney, *Fundamentals of U.S. Foreign Policy*, Westview Press, 2003, pp. 49-79.

[5] Crawford, Jo-Ann and Roberto V. Fiorentino, *The Changing Landscape of Regional Trade Agreements*, World Trade Organization Discussion Paper No. 8, 2005, p. 16.

broader provisions than the Chile FTA such as trade in services, government procurement, dispute settlement procedures, and intellectual property rights protection. In 1999, the original text of the Mexico-Chile FTA was later complemented with broader provisions, similar to those under NAFTA. Mexico's initial motivations in pursuing FTAs with the United States and other countries was to stabilize the Mexican economy, which had experienced many difficulties throughout most of the 1980s with a significant deepening of poverty, by attracting foreign direct investment. The expectation in Mexico was that FTAs would increase export diversification, attract FDI and help create jobs, increase wage rates, and reduce poverty.

Mexico's Trade Agreements

Mexico's pursuit of free trade agreements with other countries is a way to bring benefits to the economy, but also to reduce its economic dependence on the United States. The United States is, by far, Mexico's most significant trading partner. About 82% of Mexico's exports go to the United States and 50% of Mexico's imports come from the United States. Mexico's second largest trading partner is China, accounting for approximately 6% of Mexico's exports and imports.[6] In an effort to increase trade with other countries, Mexico has a total of 11 trade agreements involving 41 countries (see **Table 1**). These include agreements with many countries in the Western Hemisphere including the United States and Canada, Chile, Bolivia, Costa Rica, Nicaragua, Uruguay, Guatemala, El Salvador, and Honduras.

Mexico has also negotiated free trade agreements outside of the Western Hemisphere and, in July 2000, entered into agreements with Israel and the European Union. Mexico became the first Latin American country to have preferred access to these two markets. Mexico has completed a trade agreement with the European Free Trade Association of Iceland, Liechtenstein, Norway, and Switzerland. The Mexican government expanded its outreach to Asia in 2000 by entering into negotiations with Singapore, Korea, and Japan. In 2004, Japan and Mexico signed the Economic Partnership Agreement, the first comprehensive trade agreement that Japan signed with any country.[7] However, the large number of trade agreements has not yet been successful in decreasing Mexico's dependence on trade with the United States.

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[6] Data compiled by CRS using Global Trade Atlas database.

[7] The Asahi Shimbun, "Japan: Free Trade with Mexico," March 12, 2004.

Table 1. Mexico's Free Trade Agreements

Agreement	Agreement Type	Coverage	Date of Signature	Entry into Force	WTO Legal Cover
North American Free Trade Agreement	FTA and EIA[a]	Goods and Services	December 17, 1992	January 1, 1994	GATT Art. XXIV and GATS V
Costa Rica – Mexico	FTA and EIA	Goods and Services	April 5, 1994	January 1, 1995	GATT Art. XXIV and GATS V
Nicaragua – Mexico	FTA and EIA	Goods and Services	December 18, 1997	July 1, 1998	GATT Art. XXIV and GATS V
Chile – Mexico	FTA and EIA	Goods and Services	April 17, 1998	August 1, 1999	GATTS Art. XXIV and GATS V
European Union[b] – Mexico	FTA and EIA	Goods and Services	December 8, 1997	July 1, 2000 (goods) October 1, 2000 (services)	GATT Art. XXIV and GATS V
Israel – Mexico	FTA	Goods	April 10, 2000	July 1, 2000	GATT Art. XXIV
El Salvador – Mexico	FTA and EIA	Goods and Services	June 29, 2000	March 15, 2001	GATT Art. XXIV and GATSV
Guatemala – Mexico	FTA and EIA	Goods and Services	June 29, 2000	March 15, 2001	GATT Art. XXIV and GATS V
Honduras – Mexico	FTA and EIA	Goods and Services	June 29, 2000	June 1, 2001	GATT Art. XXIV and GATS V
EFTA[c] – Mexico	FTA and EIA	Goods and Services	November 27, 2000	July 1, 2001	GATT Art. XXIV and GATS V
Japan – Mexico	FTA and EIA	Goods and Services	September 17, 2004	April 1, 2005	GATT Art. XXIV and GATS V

Source: World Trade Organization, Regional Trade Agreement Database, see http://www.wto.org/.

Notes: The WTO definition of a free-trade area is a group of two or more customs territories in which the duties and other restrictive regulations of commerce (except, where necessary, those permitted under Articles XI, XII, XIII, XIV, XV, and XX of the GATT) are eliminated on substantially all the trade between the constituent territories in products originating in such territories.

a. Economic Integration Agreement (EIA) as defined by the World Trade Organization.

b. Includes Austria, Belgium, Bulgaria, Cyprus, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Latvia, Lithuania, Luxembourg, Malta, Netherlands, Poland, Portugal, Romania, Slovak Republic, Slovenia, Spain, Sweden, and United Kingdom.

c. Includes Iceland, Liechtenstein, Norway, and Switzerland.

NAFTA

In 1990, Mexico approached the United States with the idea of forming a free trade agreement. Mexico's main motivation in pursuing an FTA with the United States was to help stabilize the Mexican economy and attract foreign direct investment.[8] The Mexican economy had experienced many difficulties throughout most of the 1980s with a significant deepening of poverty. NAFTA is a free trade agreement that eliminated trade and investment barriers among Canada, Mexico, and the United States. Mexico's intention in entering NAFTA was to increase export diversification by attracting FDI, which would help create jobs, increase wage rates, and reduce poverty.

Upon implementation, almost 70% of U.S. imports from Mexico and 50% of U.S. exports to Mexico received duty-free treatment. The remainder of duties were eliminated over a period of 15 years after the agreement was in effect. The agreement also contains provisions for market access to U.S. firms in most service sectors; protection of U.S. foreign direct investment in Mexico; and intellectual property rights protection for U.S. companies. NAFTA is the first U.S. agreement that addressed environmental and labor concerns by including related provision in separate side agreements to NAFTA. At the time the agreement went into effect, a number of economic studies predicted that the trade agreement would have a positive overall effect on the Mexican economy, narrowing the U.S.-Mexico gap in prices of goods and services and the differential in real wages.

Mexico-Costa Rica

The Mexico-Costa Rica FTA was signed on April 5, 1994, in Mexico City and entered into force on January 1, 1995. It was the first in a series of FTAs negotiated by Mexico loosely based on the NAFTA model of trade agreements. This agreement had been preceded by a partial scope agreement signed by the two countries on July 22, 1982 in which Mexico accorded preferential access to some Costa Rican products. The FTA with Costa Rica phased out tariffs in four stages over a fifteen-year time period. Upon implementation of the agreement, approximately 70% of Mexican goods entered Costa Rica and 80% of Costa Rican goods entered Mexico duty free. By January 1, 2004, almost 97% of trade between the two countries was duty free and by 2009, virtually all tariffs had been eliminated.[9]

In addition to the provisions on national treatment and market access for goods, the agreement contains provisions on agriculture, sanitary and phytosanitary measures, rules of origin, customs procedures, safeguards, standards, cross-border trade in services, investment, government procurement, intellectual property rights protection (IPR), and dispute resolution. Items that are not included in the agreement include energy and basic petrochemicals, telecommunications, financial services, and competition policy. The IPR chapter does not cover patents, industrial designs, and layout designs of integrated circuits.[10]

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[8] Hufbauer, Gary Clyde, and Jeffrey J. Schott, *NAFTA Revisited,* Institute for International Economics, October 2005, p. 3.

[9] Salazar-Xirinachs, José Manuel and Maryse Robert, editors, *Toward Free Trade in the Americas,* April 2001, p. 98.

[10] Decreto de promulgación del Tratado de Libre Comercio entre los Estados Unidos Mexicanos y la República de Costa Rica. See WTO Regional Trade Agreement Database, see http://www.wto.org.

Mexico-Nicaragua

The FTA with Nicaragua was Mexico's second treaty with a country in Central America, also loosely based on the NAFTA model. It was signed on December 18, 1997, and entered into force on July 1, 1998. Upon implementation, 76% of tariffs on Nicaraguan exports to Mexico and 45% of tariffs on Mexican exports to Nicaragua were eliminated. The remaining tariffs are being phased out in four stages over a fifteen-year period. The agreement is similar to NAFTA and includes provisions on national treatment and market access for goods and services; rules of origin; agriculture; sanitary and phytosanitary measures; telecommunications; financial services; government procurement; investment; IPT; dispute resolution; customs procedures; safeguards; unfair trade practices; standards; and other provisions. It does not include a chapter on competition policy, energy, environment, labor, or transportation.[11] The IPR provisions do not cover patents, industrial designs, and layout designs of integrated circuits.[12]

Mexico-Chile

The Mexico-Chile FTA, completed in 1998, was enacted in Chile on July 7, 1999, and in Mexico on August 1, 1999. Mexico and Chile signed the expanded FTA at the 1998 Summit of the Americas in Santiago, Chile on April 17, 1998. The FTA was expected to deepen the growing trade relationship between the two countries and improve bilateral investment opportunities in both countries. The 1998 agreement replaced an earlier FTA that was reached between the two countries in 1991. It removed tariffs on almost all merchandise trade between the two countries.

The Mexico-Chile FTA includes provisions on national treatment and market access for goods and services; rules of origin; customs procedures; safeguards; standards; agriculture; sanitary and phytosanitary measures; investment; air transportation; telecommunications; temporary entry for business persons; IPR; dispute resolution; and other provisions. It does not include a chapter on energy, environment, or labor.[13] A separate agreement, which was signed simultaneously, includes provisions to avoid double taxation for companies doing business in both countries. The FTA provisions are similar to those under NAFTA, but with no labor and environmental provisions in separate side agreements. Other areas that were not included in the 1998 FTA were financial services, patents, or government procurement.[14]

Mexico-European Union

Negotiations for a free trade agreement between Mexico and the European Union (EU) began in October 1996. The agreement, formally called the Economic Partnership Political Co-ordination and Co-operation Agreement (also known as the Global Agreement), was signed in March 2000 and came into force on July 1, 2000. It was the first transatlantic FTA for the EU. The motivations for the agreement were to expand market access for exports from the EU to Mexico and attract

[11] *Tratado de Libre Comercio Chile.* See WTO Regional Trade Agreement Database, see http://www.wto.org.

[12] Salazar-Xirinachs, José Manuel and Maryse Robert, editors, *Toward Free Trade in the Americas,* April 2001, p. 99.

[13] Decreto Promulgatorio del Tratado de Libre Comercio entre el Gobierno de los Estados Unidos Mexicanos y el Gobierno de la República de Nicaragua. See WTO Regional Trade Agreement Database, http://www.wto.org.

[14] Bureau of National Affairs (BNA), *International Trade Reporter,* "Mexico and Chile Sign Off on Expanded Trade Agreement," April 22, 1998.

more FDI from the EU to Mexico.[15] On May 17, 2008, Mexico and the European Union agreed on a "strategic association" to further advance trade liberalization and to address climate change issues.[16]

The agreement includes provisions on national treatment and market access for goods and services; government procurement; IPR; investment; financial services; standards; telecommunications and information services; agriculture; dispute settlement; and other provisions. The agreement also includes chapters in which the parties agree to increase cooperation in a number of areas, including mining, energy, transportation, tourism, statistics, science and technology, environment, and other areas.[17] On industrial goods, the EU agreed to eliminate tariffs on 82% of imports by value coming from Mexico on the date of entry into the agreement and to phase out remaining tariffs by January 1, 2003. Mexico agreed to eliminate tariffs on 47% of imports by value from the EU upon implementation of the agreement and to phase out the remaining tariffs by January 1, 2007. In agricultural products and fisheries, signatories agreed to phase out tariffs on 62% of trade within ten years.[18] Tariff negotiations were deferred on certain sensitive products, including meat, dairy products, cereals, and bananas. Most non-tariff barriers, such as quotas and import/export licenses, were removed upon implementation of the agreement. Mexico agreed to phase out import restrictions of new automobiles from the EU by 2007. In government procurement, Mexico agreed to follow provisions similar to those under NAFTA to allow the EU to enter the Mexican market while the EU agreed to follow WTO rules.[19] In services trade, the agreement goes beyond the WTO General Agreement on Trade in Services (GATS). It immediately provided European service operators "NAFTA-equivalent" access to Mexico in a number of areas, including financial services, energy, telecommunications, and tourism.[20]

Mexico-Israel

After two years of negotiations, Mexico and Israel signed a free trade agreement on April 10, 2000 and implemented it on July 1, 2000. The agreement immediately eliminated tariffs on most products traded between Mexico and Israel at the time of the agreement with full tariff elimination scheduled by 2005. Policymakers expected the agreement to provide Mexico with more export access to the Israeli market, increased FDI from Israel to Mexico, and result in increased technology transfer from Israel to Mexico.

The agreement includes provisions on national treatment and market access for goods, rules of origin, customs procedures, emergency actions, competition policy, government procurement, dispute resolution, dispute resolution, and WTO rights and obligations.[21] The agreement covers

[15] Reuters, "*Cumbre-México y Unión Europea Acuerdan Acelerar Libre Comercio,*" May 17, 2008.

[16] Ibid.

[17] Global Agreement, Economic Partnership, Political Coordination and Cooperation Agreement between the European Community and its member States and the United Mexican States. See WTO Regional Trade Agreement Database, see http://www.wto.org.

[18] The Chinese University of Hong Kong, *The Mexico-EU Free Trade Agreement,* 2000, http://intl.econ.cuhk.edu.hk.

[19] Transnational Institute, Mexican Action Network on Free Trade (RMALC), *The EU-Mexico Free Trade Agreement Seven Years On,* June 2007.

[20] U.S.-Mexico Chamber of Commerce, *The Free Trade Agreement Between Mexico and the European Union,* August 2000.

[21] Free Trade Agreement Between the State of Israel and the United Mexican States. See WTO Regional Trade (continued...)

98.6% of agricultural goods and 100% of industrial goods. Mexico received immediate duty-free access on 50% of its exports and tariff reductions on 12% of its exports to Israel. Tariff-rate quotas were applied on 25% of Mexican exports to Israel. Most remaining tariff barriers on Mexican exports had a five-year phase out schedule. Israel received immediate duty-free access on about 72% of its exports to Mexico. Another 22.8% of tariffs on Israel exports to Mexico were withdrawn in 2003 and another 4.4% were withdrawn in 2005.[22]

Mexico-El Salvador, Guatemala, and Honduras

Mexico and El Salvador, Guatemala, and Honduras (Northern Triangle) signed a free trade agreement on June 29, 2000. The agreement is often referred to as the Mexico-Northern Triangle FTA, but the WTO has it listed as three separate agreements between Mexico and El Salvador, Guatemala, and Honduras. The agreements with El Salvador and Guatemala entered into force on March 15, 2001, while the agreement with Honduras entered into force on June 1, 2001. Negotiations for the FTA with all three countries began in 1992, stalled for four years, and resumed at the second Tuxtla Summit in 1996. Negotiations ended on May 10, 2000. This agreement was the final of Mexico's NAFTA-type agreements with all Central American countries. Prior to the conclusion of the Mexico-Northern Triangle FTA, Mexico had held separate partial scope agreements with each of the three countries, granting some products preferential access to the Mexican market.

The agreement includes provisions on national treatment and market access for goods and services, the agreement has similar provisions to other Mexican FTAs on agriculture; sanitary and phytosanitary measures; rules of origin; financial services; telecommunications services; temporary entry of business persons; investment; IPR; standards; dispute resolution; safeguards; and unfair trade practices.[23] Upon entry into force of the FTA, approximately 57% of Mexico's exports to the three countries received duty-free treatment. Tariffs on an additional 15% of goods were phased out over a period of three to five years. Mexico eliminated tariffs on 65% of imports from the Northern Triangle countries upon implementation and phased out tariffs on 24% of imports over a three to five year period. Thirty percent of Mexico's agricultural exports received duty-free treatment upon the entry into force of the agreement, another 12% were liberalized over a five-year period, and 41% were liberalized over a period of five to eleven years.[24]

Mexico-European Free Trade Association

Mexico and the European Free Trade Association (EFTA), composed of Iceland, Lichtenstein, Norway, and Switzerland, signed a free trade agreement on November 27, 2000. The agreement entered into force on July 1, 2001. This was the first FTA that the EFTA had concluded with an overseas partner country. Since the agreement entered into force, Mexico and the EFTA have met at least four times to explore possibilities of further trade integration, including agricultural and

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Agreement Database, see http://www.wto.org.

[22] U.S.-Mexico Chamber of Commerce, "History of Mexico-Israel Trade Relations," September 2000.

[23] Tratado de Libre Comercio México-El Salvador, Guatemala y Honduras (Triángulo del Norte). See http://www.sice.oas.org.

[24] Salazar-Xirinachs, José Manuel and Maryse Robert, editors, *Toward Free Trade in the Americas,* April 2001, pp. 99-100.

services trade. In September 2008, the two parties agreed to adopt an amendment on transportation to the agreement to help facilitate trade. They also discussed possibilities of further amendments, such as banning export duties and extending the coverage of trade in processed agricultural products.[25]

The agreement includes provisions on national treatment and market access for goods; agriculture; rules of origin; safeguards; and other provisions.[26] During the first six years, the FTA reduced the average Mexican tariff on EFTA industrial goods from 8% to zero. Mexican industrial exports to the EFTA have been free of duty since the entry into force of the FTA.[27]

Mexico-Japan

Mexico and Japan signed a free trade agreement, formally called an Economic Partnership Agreement (EPA) in September 2004. The EPA was Japan's second free trade agreement, but its most comprehensive bilateral agreement at that time. It was Japan's first agreement to include agricultural products, a factor that resulted in initial opposition in Japan. In addition to the removal of tariff barriers, it includes regulations in other areas, including labor mobility and investment.[28] One of the goals of the Mexico-Japan EPA was to restore the competitiveness of Japanese companies in the Mexican market. Mexico already had free trade with the United States and Canada under NAFTA and with the European Union through an FTA that went into force in July 2000. These two agreements had placed Japanese companies at a disadvantage due to differences in tariff rates and exclusion of Japanese companies from public-works projects in Mexico. Mexico entered the agreement to increase Japanese investment in Mexico, and, thus, create jobs, expand Mexican exports to Japan, expand technology transfer from Japan, and strengthen Mexican industrial competitiveness.[29]

The agreement includes provisions on national treatment and market access for goods; sanitary and phytosanitary measures; standards; rules of origin; customs procedures; safeguards; IPR; dispute settlement; financial services; and government procurement. The agreement also includes chapters in which the two countries agreed to increase cooperation in a number of areas, including vocational education and training, agriculture, tourism, and the environment.[30] The two countries agreed to eliminate tariffs on almost all industrial products within ten years. Tariffs were eliminated immediately in the following areas: electronics, household electric appliances, capital goods, and automobiles. By the year 2015, tariffs will be eliminated on 90% of goods that accounted for 96% in total trade value between the two countries. Prior to the EPA, only 16% of Japanese exports to Mexico entered duty free into the Mexican market, while 70% of Mexican exports to Japan entered duty free. In agriculture, Mexican officials initially called for trade concessions in beef, oranges, pineapples, and leather products, but later agreed to an expansion of Japanese import quotas over a five-year period for pork, beef, chicken, oranges, and orange juice.

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[25] The European Free Trade Association (EFTA) Secretariat, *EFTA and Mexico to Amend Free Trade Agreement*, September 2008.

[26] Free Trade Agreement between the EFTA States the United Mexican States. . See WTO Regional Trade Agreement Database, see http://www.wto.org.

[27] *Mexico-EU Trade Links*, "Mexico-EFTA Free Trade Agreement: After Six Years," July 2007.

[28] *The Asahi Shumbun*, "Japan, Mexico Ink Landmark Accord," September 20, 2004.

[29] Press Center Japan, "Japan and Mexico Agree on Conclusion of Free-Trade Agreement," March 31, 2004.

[30] Agreement Between Japan the United Mexican States for the Strengthening of the Economic Partnership. See WTO Regional Trade Agreement Database, see http://www.wto.org.

These are scheduled to be revised in 2010, the fifth year of the agreement. The value of Mexico's agricultural products exempt from import tariffs was reportedly expected to be less than 50% of its total agricultural exports to Japan.[31] The agreement also allowed for a duty-free quota for motor vehicles and steel upon implementation, with a phase-out scheduled over time. Japan's auto and steel companies were expected to benefit the most from these provisions.[32]

Partial Scope Agreements

Mexico has a number of partial scope agreements, which are integration agreements with more limited free trade coverage than a free trade agreement (see **Table 2**). Mexico is a party to the Agreement on the Global System of Trade Preferences Among Developing Countries (GSTP). The GSTP was established in 1988 as a framework for the exchange of trade preferences among developing countries to promote trade among developing countries. The agreement provides tariff preferences on merchandise trade among member countries. It is a treaty to which only Group of 77 member countries may enter.[33] The text of the agreement was adopted after a round of negotiations that was concluded in Belgrade in 1988. The agreement, which entered into force on April 19, 1989, was envisaged as being a dynamic instrument which would be expanded in successive stages in additional rounds of negotiations and reviewed periodically.[34] A second round of negotiations was proposed in the early 1990s to expand trade preferences, but negotiations faltered as members failed to ratify the agreement. In June 2004, GSTP participants launched a third round of negotiations. Forty-four countries have acceded to the agreement.[35]

Mexico is a signatory to the Latin American Integration Association (ALADI), which was established by the Treaty of Montevideo in August 1980 and entered into force on March 18, 1981. ALADI replaced the Latin American Free Trade Association established in1960 with the goal of developing a common market in Latin America. ALADI members include Argentina, Bolivia, Brazil, Chile, Colombia, Cuba, Ecuador, Mexico, Paraguay, Peru, Uruguay, and Venezuela. Signatory countries have sought economic cooperation amongst each other but have made little progress toward forming a common market. They maintain a flexible goal of encouraging free trade without a timetable for instituting a common market. Members approved a regional tariff preference arrangement in 1984 and expanded it in 1987 and 1990.[36]

In addition, Mexico is a member of the Protocol Relating to Trade Negotiations among Developing Countries (PTN). The PTN is a preferential arrangement involving Bangladesh, Brazil, Chile, Egypt, Israel, Mexico, Pakistan, Paraguay, Peru, Philippines, Republic of Korea, Serbia, Tunisia, Turkey, and Uruguay. It was signed in December 1971 and became effective on February 11, 1973.

[31] *Nikkei Weekly*, "FTA with Mexico Paves Way for Talks with Asian Nations," March 15, 2004.

[32] *The Asahi Shumbun*, "Japan, Mexico Ink Landmark Accord," September 20, 2004.

[33] The Group of 77 (G-77) was established on June 15, 1964 by seventy-seven developing countries, signatories of the "Joint Declaration of the Seventy-Seven Countries," issued at the end of the first session of the United Nations Conference on Trade and Development (UNCTAD) in Geneva.

[34] United Nations Conference on Trade and Development, Press Release, "Global System of Trade Preferences," June 16, 2004.

[35] Ibid.

[36] Latin American Integration Association (ALADI) website, see http://www.aladi.org.

Table 2. Mexico's Partial Scope Agreements

Agreement	Coverage	Date of Signature	Entry into Force	WTO Legal Cover
Global System of Trade Preferences Among Developing Countries (GSTP)[a]	Goods	April 13, 1988	April 19, 1989	Enabling Clause
Latin American Integration Association (ALADI)[b]	Goods	August 12, 1980	March 18, 1981	Enabling Clause
Protocol on Trade Negotiations (PTN)[c]	Goods	December 8, 1971	February 11, 1973	Enabling Clause

Source: World Trade Organization, Regional Trade Agreement Database, see http://www.wto.org/.

a. Includes Algeria, Argentina, Bangladesh, Benin, Venezuela, Bolivia, Brazil, Cameroon, Chile, Colombia, Cuba, Ecuador, Egypt, Former Yugoslav Republic of Macedonia, Ghana, Guinea, Guyana, India, Indonesia, Islamic Republic of Iran, Iraq, Republic of Korea, Democratic People's Republic of Korea, Libyan Arab Jamahirlya, Malaysia, Mexico, Morocco, Mozambique, Myanmar, Nicaragua, Nigeria, Pakistan, Peru, Philippines, Singapore, Sri Lanka, Sudan, Tanzania, Thailand, Trinidad and Tobago, Tunisia, Vietnam, and Zimbabwe.

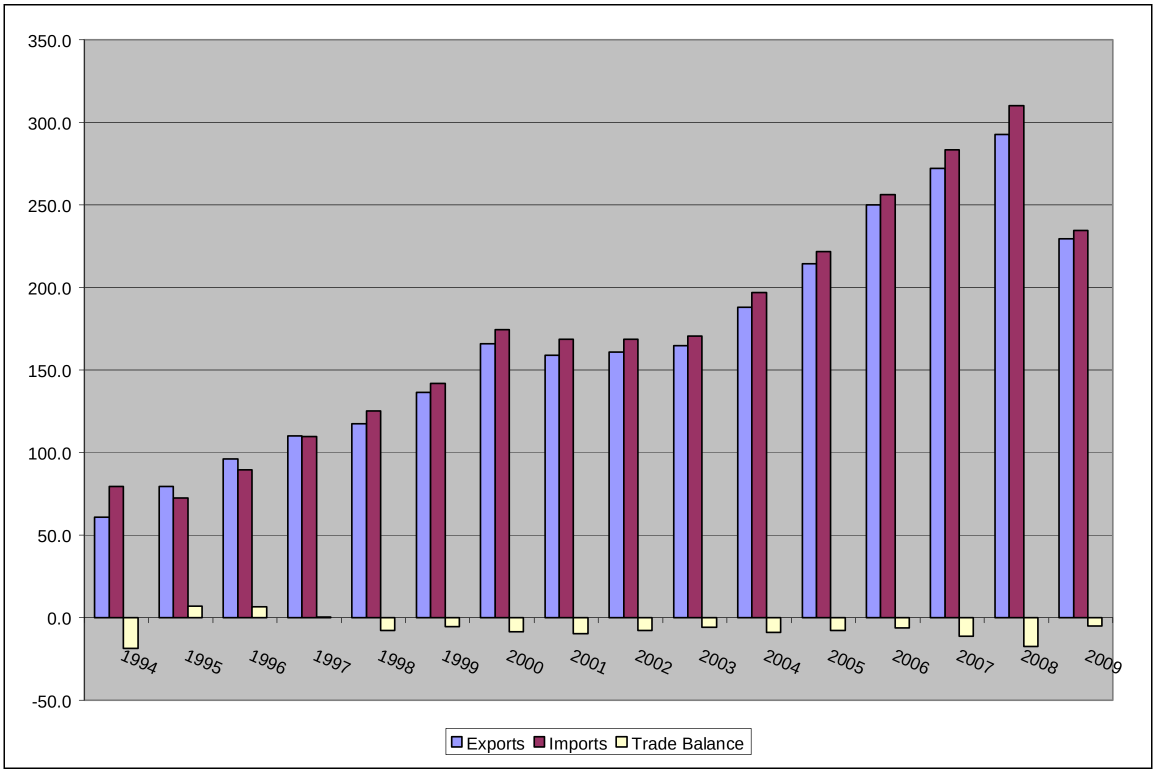
b. Includes Argentina, Venezuela, Bolivia, Brazil, Chile, Colombia, Cuba, Ecuador, Mexico, Paraguay, Peru, and Uruguay.

c. Includes Bangladesh, Brazil, Chile, Egypt, Israel, Republic of Korea, Mexico, Pakistan, Paraguay, Peru, Philippines, Serbia, Tunisia, Turkey, Uruguay.

Mexico's Merchandise Trade

Since trade liberalization, Mexico's trade with the world has risen rapidly, with exports increasing faster than imports. Mexico's exports to all countries increased 465% between 1993 and 2008, from $51.8 billion to $292.6 billion. The 2009 economic downturn, however, resulted in a decline in the value of exports to $229.6 billion (see **Figure 1**). Mexico's imports from all countries increased from $65.4 billion in 1993 to $310.1 billion in 2008, but then fell to $234.4 billion in 2009. Mexico's trade balance went from a deficit of $13.5 billion in 1993 to surpluses of $7.1 billion in 1995 and $6.5 billion in 1996. Since 1998, Mexico's trade balance has remained in deficit, reaching $17.5 billion in 2008 and then declining to $4.8 in 2009. Mexico's top five exports in 2009 were crude petroleum oil, flat panel screen TV's, automobiles, mobile telephones, and gold products. Mexico's top five imports were gasoline, TV parts, electronic parts, mobile telephones, and automobiles (see **Table 3**).

Figure 1. Mexico's Merchandise Trade with All Countries



Source: Compiled by CRS using data from Mexico's Ministry of Economy.

Table 3. Composition of Trade: 2009

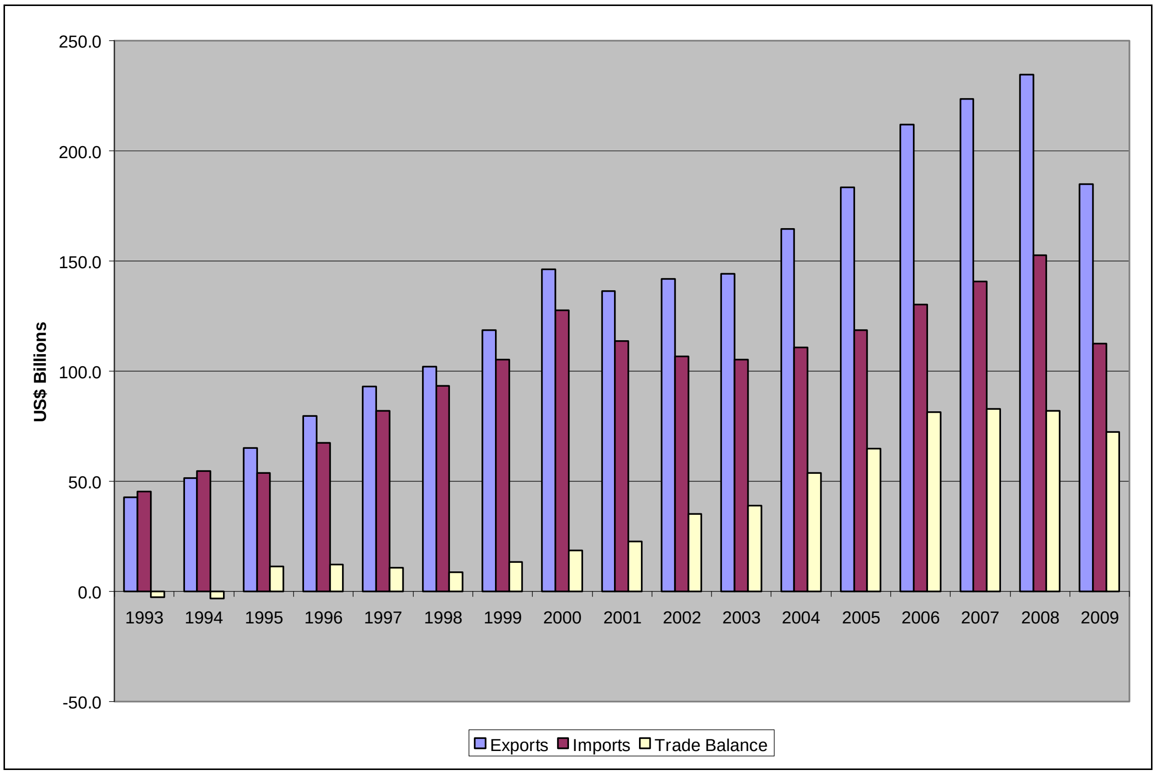
Mexico's Exports		**Mexico's Imports**	
Product (HTS 8-digit level)	**Value** (Billions US$)	**Product** (HTS 8-digit level)	**Value** (Billions US$)
Crude Petroleum Oil	25.9	Gasoline	8.3
TV apparatus with flat panel screen	15.7	Parts for TV apparatus	6.6
Automobiles	11.3	Electronic parts	3.9
Mobile Telephones	9.4	Mobile telephones	3.3
Gold products	3.6	Automobiles	2.4
Total	229.6	Total	234.4

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

Trade with the United States

Mexico's trade with the United States also increased rapidly since trade liberalization, with exports to the United States increasing more rapidly than imports. Exports to the United States increased from $42.9 billion in 1993 to $234.6 billion in 2008, but then fell to $184.9 billion in 2009 (see **Figure 2**). Mexico's imports from the United States increased from $45.3 billion in 1993 to $152.6 billion in 2008, and then decreased to $112.4 billion due to the global recession. Mexico's trade balance with the United States went from a deficit of $2.4 billion in 1993 to a surplus of $72.5 billion in 2009.

Figure 2. Mexico's Merchandise Trade with the United States



Source: Compiled by CRS using data from Mexico's Ministry of Economy.

Trade Trends Since Liberalization

Mexico's reliance on the United States as a trade partner appears to be diminishing, although slightly. Between 2004 and 2009, the U.S. share of Mexico's total imports decreased from 56% to 48%, while the share of total Mexican exports going to the United States decreased from 89% to 81%. Though it has decreased somewhat, the share of Mexico's total exports that go to the United States remains consistently high. Mexico's share of the U.S. market has lost ground since 2002. In 2003, China surpassed Mexico as a top supplier of U.S. imports, and Mexico now ranks third, after China and Canada, as a source of U.S. imports.

Between 1996 and 2008, Mexico's total exports doubled from $96.0 billion to $292.7 billion (see **Table 4**). In 2009, Mexico's total exports decreased 22% to $229.6 billion. While the United States has the highest market share of Mexican exports, the value of exports to other FTA countries has increased considerably since trade liberalization, with exports to Israel experiencing the highest percentage increase, though the value of trade with Israel remains relatively low. Other key export markets for Mexico are the European Union, Japan, and Guatemala.

Table 4. Mexico's Exports by FTA Partners

(Millions US$)

Partners	1996	1998	2000	2002	2004	2006	2008	2009
NAFTA	82,017	103,668	149,784	144,889	167,814	216,976	241,687	193,254
Costa Rica	209	290	354	373	387	522	922	652
Nicaragua	61	65	123	93	151	522	371	221
Chile	781	736	549	323	443	905	1,589	1,053
European Union	3,555	3,988	5,799	5,626	6,818	10,967	17,080	11,353
Israel	13	24	67	56	62	91	220	85
El Salvador	177	246	307	292	317	497	772	463
Guatemala	375	623	574	548	673	935	1,388	1,195
Honduras	107	146	149	156	182	285	459	377
EFTA	200	132	131	172	119	154	643	478
Japan	1,251	552	1,115	1,194	1,191	1,594	2,068	1,615
Non-FTA Countries	7,258	7,123	7,169	7,324	9,842	16,477	25,467	18,874
Total	96,004	117,593	166,121	161,046	187,999	249,925	292,666	229,620

Source: Mexico's Ministry of Economy with data from *Banco de México*. Compiled by CRS.

Mexico's total imports increased from $96.0 billion in 1996 to $292.7 billion in 2008, and then declined to $229.6 billion in 2009. Imports from NAFTA trading partners increased from $82.1 billion in 1996 to $241.7 in 2008, decreasing to $193.2 billion in 2009 (see **Table 5**). Imports from its other FTA trading partners, particularly from Honduras and Chile, have also increased significantly since 1996. In 2009, NAFTA countries ranked first as sources of imports ($119.7 billion), followed by the European Union ($27.2 billion), and Japan ($11.4 billion). Mexico's imports from non-FTA countries also increased rapidly, however, from $7.3 billion in 1996 to $70.8 billion, as shown in **Table 5**.

Table 5. Mexico's Imports from FTA Partners

(Millions US$)

FTA Partners	1996	1998	2000	2002	2004	2006	2008	2009
NAFTA	69,280	95,549	131,551	111,037	116,154	137,687	162,066	119,737
Costa Rica	58	87	180	416	852	789	777	923
Nicaragua	12	14	27	27	52	78	119	106
Chile	171	552	894	1,010	1,464	2,470	2,593	1,651
European Union	7,800	11,846	15,057	16,950	21,657	28,938	39,160	27,204
Israel	79	137	297	250	402	429	524	416
El Salvador	19	25	20	36	50	59	71	71
Guatemala	77	81	91	117	230	356	501	500
Honduras	5	12	13	25	66	123	255	177
EFTA	484	648	851	872	1,074	1,386	1,693	1,371
Japan	4,132	4,537	6,466	9,349	10,583	15,295	16,326	11,397
Non-FTA Countries	7,352	11,885	19,011	28,590	44,226	68,442	86,047	70,832
Total	89,469	125,373	174,458	168,679	186,810	256,052	310,132	234,385

Source: Mexico's Ministry of Economy with data from *Banco de México*. Compiled by CRS.

Ninety-five percent of Mexico's exports are headed to countries with which it has FTAs, and 88% of total exports go to its NAFTA trading partners (see **Table 6**). Exports to the European Union accounted for 6% of Mexico's total exports in 2009. The share of Mexico's imports coming from NAFTA trading partners declined from77% of its total imports in 1996 to 51% of total imports in 2009 (see **Table 6**). The share of Mexico's imports from the European Union increased from 9% in 1996 to 12% in 2009, while the share from non-FTA countries increased from 8% to 29%. Imports from Japan accounted for 5% of Mexico's imports in 2009, while imports from all other FTA partners accounted for 3%. Although Mexico does not have an FTA with China, Mexico's imports from China increased considerably during this period. Imports from China increased from $760 million in 1996 to $32.5 billion in 2009.

Table 6. Market Share of Exports and Imports by FTA Partner

	1996	1998	2000	2002	2004	2006	2008	2009
Export Market Share[a]								
NAFTA	85%	88%	90%	90%	89%	87%	83%	88%
EU	4%	3%	3%	3%	4%	4%	6%	5%
Japan	1%	0%	1%	1%	1%	1%	1%	1%
All Other FTA Partners	1%	1%	1%	1%	1%	1%	1%	1%
Non-FTA Countries	8%	6%	4%	5%	5%	7%	9%	5%
Import Market Share[a]								
NAFTA	77%	76%	75%	66%	62%	54%	52%	51%
EU	9%	9%	9%	10%	12%	11%	13%	12%
Japan	5%	4%	4%	6%	6%	6%	5%	5%
All Other FTA Partners	1%	1%	0%	2%	2%	2%	2%	3%
Non-FTA Countries	8%	9%	11%	17%	24%	27%	28%	29%

Source: Compiled by CRS using data from Mexico's Ministry of Economy.

a. Totals may not add due to rounding.

Economic Policy Challenges for Mexico

Though Mexico's total exports have increased substantially since it began trade liberalization, the United States continues to be the dominant export market for Mexican goods. The reliance of Mexico on the United States as an export market makes the country more susceptible to economic conditions in the United States. The global financial crisis, which resulted in a downturn in the U.S. economy, resulted in the deepest recession in the Mexican economy since the 1930s. The economy contracted by 6.9% in 2009, while the peso fell 25% against the dollar in the first ninth months of 2009.[37] 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.[38] Estimates for 2010 project that the economy will grow by about 3% to 4%, though much of this will be due to growth in the export sector and not to domestic demand.

Mexico is facing increasing challenges in addressing issues related to productivity and the competitiveness of its exports. Some economists believe that countries in Latin America need to become more competitive in the global economy in order to promote economic growth and

[37] International Monetary Fund (IMF), *Public Information Notice*, "IMF Executive Board Concludes 2010 Article IV Consultation with Mexico," March 16, 2010, p. 2.

[38] Ibid.

reduce poverty. They argue that if Latin American countries are going to prosper, they must improve labor skills and technology to be more competitive in the global economy.[39] Over the past several years, Mexico has been facing increasing competition from China and other Asian economies in the manufacturing sector. In 2003, China replaced Mexico as the second-highest source of U.S. imports. This has presented challenges to Mexico's manufacturing sector and some economists argue that Mexico has fallen behind in its comparative advantage in exporting in industries with intermediate wages and technological sophistication.[40] They argue that Mexico must invest more in education and telecommunications infrastructure to increase productivity and remain competitive.

The emergence of China in the global marketplace has drawn comparisons between the industrial policies of China and Mexico. Some analysts argue hat Mexico should make more progress in scientific research to attract and create high-tech industries, such as China has done. They believe that China's policy to help attract foreign direct investment, which initially consisted of special zones with preferential fiscal and customs policies and later modified to establish scientific and technical research facilities, should serve as an example to Mexico's industrial policy. They state that Mexico's approach has been a combination of fiscal and customs policies to enhance its comparative advantage of sharing a 2000-mile border with the United States, but that Mexico did little to promote scientific and technical research. They add that Mexican programs have not fostered or encouraged research and development activities to facilitate the creation of technological enterprises.[41]

A primary motivation for entering into free trade agreements is to improve economic conditions and create jobs. In the case of Mexico, an additional key motivation has been to address the issue of poverty by creating jobs for the poor. Mexico has made an effort to make trade agreements a tool for promoting economic development and combating poverty, but it is only part of the overall effort of the Mexican government to address these issues. Mexico has implemented a compensatory policy to address poverty through its *Oportunidades* program (formerly known as Progresa). This program provides cash transfers to families in poverty who demonstrate that they regularly attend medical appointments and can certify that children are attending school.[42] The program has been successful in bringing more economic stability to the country and reducing poverty but it has not helped the country's productivity and may not be a long-term solution. Some argue that such programs result in a dependence for cash transfers and do not help poor workers obtain formal sector jobs with prospects for increasing productivity.[43]

[39] *Miami Herald,* "The Left's Favorite U.S. Nobel May Surprise his Fans," by Andres Oppenheimer, August 16, 2009.

[40] Latin America/Caribbean and Asia/Pacific Economics and Business Association, *Economic Integration and Manufacturing Performance in Mexico: Is Chinese Competition to Blame?,* by Ernesto López-Córdova, Working Paper No. 23, December 2004.

[41] *Mexico Now*, "Mexico's and China's Programs to Attract Foreign Investment," by Ramiro Villega and Migual A. Díaz Marín, pp. 52-55.

[42] Santiago Levy, *Progress Against Poverty,* Brookings Institution, 2006.

[43] Levy, Santiago, *Good Intensions, Bad Outcomes: Social Policy, Informality, and Economic Growth in Mexico,* Brookings Institution Press, 2008, pp. 1-6.

Implications for U.S. Interests

Mexico's numerous free trade agreements and its trade liberalization policy are of interest to U.S. policymakers because of the implications for U.S.-Mexico trade, economic stability in Mexico, and the overall relationship of the two countries. There is an interdependent relationship between the two countries, as highlighted by the sharp downturn in the Mexican economy in 2009 that resulted from the global financial crisis and the slowdown in the U.S. economy. Economic conditions in Mexico are important to the United States because of the proximity of Mexico to the United States, the close trade and investment interactions, and other social and political issues. Another implication for the United States is the effect of Mexico's FTAs on U.S. exports to Mexico. The liberalization of Mexico's trade and investment barriers to other countries has resulted in increasing competition for U.S. goods and services in the Mexican market. However, trade flows are also affected by other factors such as exchange rates, economic growth, and investor confidence, and it is difficult to isolate these effects.

A number of studies suggest that while Mexico's trade liberalization policy, mainly NAFTA, may have brought economic and social benefits to the Mexican economy as a whole, the benefits have not been evenly distributed throughout the country. Wages and employment tend to be higher in states experiencing higher levels of FDI and trade. In terms of regional effects, initial conditions in Mexico determined which Mexican states experienced stronger economic growth as a result of trade liberalization. States with higher levels of telecommunications and transportation infrastructure gained more benefits than poorer states with lower levels of education, infrastructure, and institutional capacity. This affects the United States because Mexican workers who have lost their job due to trade liberalization may migrate to other areas in Mexico or to the United States to seek jobs.[44]

To address issues affecting trade, U.S. policymakers may consider closer cooperation with Mexico to develop complementary policies to ensure that all segments of the two countries benefit from economic integration. The United States and Mexico, along with Canada, have increased cooperation on economic and security issues, but there may be additional options that could be considered by both countries.[45] One issue on which a number of economists and other analysts have agreed upon is that Mexico needs to invest more in education, infrastructure, and institutional strengthening to benefit more fully from freer trade. A possible option to address this issue is to create a bilateral or trilateral fund for development that focuses on building infrastructure, improving education and human capital, and creating more opportunities for research and development. U.S. and Mexican policymakers have informally talked about expanding the mandate of the North American Development Bank (NADBank).[46] A number of Members of the U.S. Congress and elected officials from Mexico have discussed the possibility of expanding the mission of the NADBank to go beyond environmental and border issues and consider creating an infrastructure fund that would be managed by NADBank to provide investment in infrastructure, communications, or education.

[44] For more information, see CRS Report RL34733, *NAFTA and the Mexican Economy*, by M. Angeles Villarreal.

[45] See CRS Report RS22701, *Security and Prosperity Partnership of North America: An Overview and Selected Issues*, by M. Angeles Villarreal and Jennifer E. Lake.

[46] NADBank and its sister institution, the Border Environment Cooperation Commission (BECC), were created under a bilateral side agreement to NAFTA called the Border Environmental Cooperation Agreement (BECC) to address environmental infrastructure problems along the U.S.-Mexican border.

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