



U.S. Trade Policy in the Western Hemisphere

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The United States, under the North American Free Trade Agreement, already is moving to eliminate trade barriers between Canada, Mexico, and the United States. My emphasis, therefore, will be on U.S. trade policy toward the rest of the Western Hemisphere.

Performance of NAFTA

First, however, a few words about NAFTA because its progress has influenced thinking about hemispheric free trade. Those who opposed NAFTA at the outset are continuing a drumbeat against the agreement. As is generally known, the opponents of NAFTA point to the collapse of the Mexican economy in 1995, the alleged loss of jobs due to direct investment in both Mexico and Canada, and the large U.S. merchandise trade deficits with each of the two countries.

I do not wish to engage in a lengthy discussion of NAFTA here, but I have done so in a book published recently by the Center for Strategic and International

Studies, entitled NAFTA at Three: A Progress Report. I wish to make just a few points. The massive loss of jobs alleged to have resulted from NAFTA is made against the backdrop of record job-creation in the U.S. economy of some 2.5 million a year since the agreement has been in effect. The U.S. "problem," as the Federal Reserve sees it, is too much job-creation.

The total documented U.S. job loss due to increased imports from Canada and Mexico is about 120,000 for the three plus years NAFTA has been in place. The United States has created as many jobs every two weeks as have been documented to be lost because of imports from Canada and Mexico over the entire existence of NAFTA. And this does not count the jobs created by increased exports to those two countries. The reality is that job-creation in the United States depends overwhelmingly on developments in the domestic economy.

Looking just at Mexico, two-way trade was \$81.5 billion in 1983, the year before the agreement went into effect. Last year, 1996, two-way trade was almost \$130 billion. All of the increase was not due to NAFTA, but much of it was. U.S. exports to Mexico in 1993 were \$42 billion and last year they were \$57 billion. Canada and Mexico are our first and third most important trading partners.

The United States did have a large deficit in merchandise trade with Mexico last year, amounting to \$16 billion. The merchandise trade deficit with Canada was \$23 billion. The argument that this led to the loss of jobs is belied by the facts of U.S. job-creation. The U.S. Federal Reserve Board has conducted monetary policy since NAFTA has been in place on the assumption that the United States has full employment. This, in essence, means that the U.S. economy as a whole could not have created more jobs without stimulating inflation. Under these circumstances, the imports from Canada and Mexico provided greater choice to consumers without overall job loss.

Some people lost jobs in competing industries. Some workers were unable to take advantage of the job-creation of the U.S. economy. But the way to deal with

these problems is through better adjustment programs, not to deny choice to 260 million consumers.

The U.S. merchandise trade deficit with Mexico can be explained mainly by the combination of U.S. economic growth and economic decline in Mexico in 1995. By now, the Mexican economy is recovering. A bilateral merchandise trade balance is not normally a meaningful measure. It omits trade in services, which is about 20 percent the size of merchandise trade; the United States generally exports more services than it imports from the two NAFTA partners, but this also depends on income growth. Looking at trade with a single country uses a shifting bilateral measure instead of the global picture of U.S. trade. And, most important, focusing on the merchandise trade balance, whether bilateral or global, shifts blame to others for outcomes produced at home.

The United States inevitably will have a deficit in the current account of the balance of payments as long as it invests more than it saves. We must, under these circumstances, import capital to finance the investment and, the way the balance of payments is measured, this translates into a current account deficit to compensate for the capital account inflow. The largest single element of the current account is merchandise trade. Those who believe that the sky is falling because the United States has a bilateral or global trade deficit (and it is not clear to me why they believe this) should focus on the real causes (inadequate U.S. saving) and not blame foreigners for our own shortcomings.

Free Trade in the Americas

Enough on NAFTA. I would like to turn to the rest of the hemisphere. In the interest of brevity, I will limit myself to ten reasons for seeking free trade in the Americas.

1. As the United States dawdled on taking steps toward negotiating a Free Trade Area of the Americas, facts were being created on the ground by other countries. Argentina, Brazil, Paraguay, and Uruguay formed and deepened MERCOSUR, the Common Market of the South. Other subregional economic groupings were reinforced in the Andean countries, Central America, and the Caribbean. Many countries entered into bilateral and plurilateral free-trade agreements. Chile and Bolivia associated themselves with MERCOSUR. MERCOSUR is flirting with the idea of a free-trade agreement with the European Union.

This means that U.S. products already are facing discrimination in exporting to South and Central America, and will face even more in competition with products from other countries in Latin America, and perhaps even in Europe. This can be significant for many products and can affect U.S. agricultural and manufactured exports. The only way to overcome this handicap is by entering into free trade ourselves. There is no other realistic option. Members of this Congress who oppose free trade must explain to exporters in their districts why they must compete in the hemisphere under a handicap.

2. This is our hemisphere. U.S. exporters capture more than 40 percent of the Latin American and Caribbean market, compared with proportions one-third to one-half as large in other hemispheres, such as Europe and Asia. Thus, as hemispheric countries grow economically and suck in imports, the effect is considerably greater for U.S. traders than is similar growth in Asia or Europe. The failure to enter into hemispheric free trade sacrifices this natural advantage in what has been our most favorable market.

Omitting Canada and Mexico, for which free trade already exists, U.S. exports to hemispheric countries were almost \$53 billion in 1996. The merchandise trade balance with this region was positive by about \$3.5 billion, but this, in my view, is not in itself an important consideration. What is worth keeping in mind is that as Latin America prospers, and it inevitably will in light of the responsible economic policies being followed in the main countries of the region, its large population represents a significant and growing market. Why would we want to give it away?

3. The United States exports more than goods; we also sell services. When the anti-free traders make their arguments, they invariably omit U.S. exports of telecommunication services, movies, videos, insurance, banking, transportation, and a host of other services. These service sales are estimated to be about 20 percent the value of merchandise exports. The most dynamic U.S. exports are related to services, such as those deriving from the information revolution that is largely a U.S. creation. The precedent for inclusion of services in trade agreements was established in NAFTA and carried over, although less comprehensively, in the Uruguay Round of the General Agreement on Tariffs and Trade. The best way to assure an open market for U.S. service exports to Latin

America and the Caribbean is through a hemispheric free-trade agreement encompassing these activities.

4. A modern free-trade agreement does not stop at trade in goods and services, but goes beyond that to examine internal measures that impede trade. Trade negotiations no longer are limited to tariff reduction, as is evident from the 11 working groups set up in the hemisphere after the Miami Summit meeting of December 1994 to deal with other issues.

NAFTA includes provisions on investment, government procurement, the protection of intellectual property, standards for industrial goods, sanitary and phytosanitary standards, customs procedures, and dispute settlement, among other matters. The NAFTA parallel agreements contain understandings on environmental and labor protection and, while I realize that these are controversial, the disagreement relates primarily to the use of trade sanctions for carrying them out, not to the underlying desire to deal with these issues internationally. I hope that persons of good will on both sides of the aisle in the Congress do not hold up the benefits of hemispheric free trade by their inability to resolve their differences on these issues.

5. The Uruguay Round brought U.S. tariffs down to about 3 to 4 percent on average, while those in Latin America and the Caribbean range from 10 to 25 percent. Even the 3 to 4 percent range is overstated because of the many nonreciprocal tariff preferences granted by the United States to developing countries generally, to nations in the Caribbean Basin, and to those in the Andean region. The price for the United States to obtain access to Latin American and Caribbean markets in a hemispheric free-trade negotiation is a bargain. There are, of course, higher U.S. tariffs and other barriers on sensitive products, just as there are prohibitive restrictions on the importation of many products elsewhere in the hemisphere. The most arduous negotiations will be on these products, but this does not negate the conclusion that the United States would get more trade-barrier reductions than it would have to give up in hemispheric free-trade negotiations.
6. The prevailing economic development model in Latin America and the Caribbean changed radically during the 1980s, from closed markets based on an import-substitution model, to open markets that stress the imperative of exporting. These changes were urged for many years by the United States. Nations largely closed to foreign direct investment now actively seek such investment from the United States and other industrial countries. We are no longer negotiating with countries that look inward, but rather with a hemisphere that has become globally engaged.

The idea of hemispheric free trade, which would have been rejected out of hand 15 years ago, was greeted with enthusiasm when first proposed by President Bush in the Enterprise for the Americas initiative in 1990. There is now less enthusiasm in the hemisphere, largely because the United States has given little indication that it really intends to follow through. Negotiation for hemispheric free trade requires the granting of fast-track authority to the administration and the failure to achieve this raises skepticism in the hemisphere about U.S. trade intentions.

7. Those who oppose an open U.S. market in exchange for open markets elsewhere in the hemisphere are, in essence, modern-day Luddites. They reject the reality of globalization under which investment moves out of the United States as well as into it. They would prefer that the United States produce all kinds of products, those that require low skills and provide only low wages, rather than emphasize those industrial and service activities that require skilled personnel and new technologies. They can no more succeed than could the Luddites and still retain a vibrant, high-wage, productive U.S. economy. U.S. companies are not alone in seeking opportunities for foreign investment and coproduction as the way to enhance trade competitiveness. Western European countries and Japan are doing the same. U.S. companies have a long history of investment in Latin America and the Caribbean and this is one reason why they dominate most hemispheric markets. The United States cannot close itself off from the imperatives of globalization and still remain prosperous; and there is no region where this reality is more germane than in our own hemisphere.
8. Today, almost for the first time in the history of the Americas, all countries in the hemisphere, save Cuba, are democratic. Many of the democracies are frail. Many have electoral and other flaws. Many countries in the hemisphere lack universal educational opportunities, have weak judicial systems, and tolerate excessive corruption. But the essential building block is there in the form of democratically elected governments and legislatures and the conviction that further development of their democracies is the path of the future. This situation does not exist in widespread fashion in other regions, other than Western Europe. Hemispheric free trade can thus take advantage of two features that hardly existed earlier, economic policies based on market principles and political structures based on democratic aspirations.
9. Two points mentioned earlier in the discussion of NAFTA should be emphasized, one on jobs and the second on merchandise trade deficits. There is no evidence that an open market prejudices U.S. job creation. We have witnessed this in recent years, when jobs were created at record levels in the United States at the very time of maximum U.S. openness to imports and during the three years of NAFTA's existence. There is now examination among U.S. economists as to whether and how much an open market prejudices the wages of low-skilled U.S. workers, but

- there is little disagreement on the point that U.S. job-creation depends overwhelmingly on domestic economic policy. The argument that hemispheric free trade would lead to massive job losses in the United States has as little basis as the contention that NAFTA would lead to substantial net job losses.
10. The United States must have a current account deficit as long as it invests more than it saves at home. There are two key parts to the current account of the balance of payments, trade in goods and trade in services, and the United States today exports more services than it imports. This makes it inevitable that the deficit will show up in the merchandise trade account. Blaming government negotiators, or open markets, or the unfairness of other countries, or whatever, will not change this reality. The corrective is straightforward — to save more, if we do not wish to reduce investment. Raising U.S. savings by eliminating the budget deficit should help reduce the merchandise trade deficit.

The United States is a global trader. It will have bilateral deficits with some countries and surpluses with others. The United States now has a modest surplus in merchandise trade with Latin America, other than Mexico. However, these bilateral and regional numbers are subject to change, almost year by year, depending on the relative strengths and weaknesses of economies. Protectionism does not get at the root issue of trade balances, the cries of protectionists notwithstanding.

About the Author

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