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Redesigning NAFTA for the 21st Century

For the first time in history, all three countries of North America—Canada, Mexico, and the United States—held democratic national elections in the same year, 2000. Perhaps this was an omen that their political trajectories had begun to converge after two centuries in which their differences seemed far more important. The leading candidates for the highest office in each land debated issues intensely, but in all three countries, the agendas were almost exclusively domestic. The North American Free Trade Agreement (NAFTA), which had been so controversial a decade before, was barely mentioned, if at all, in any country. NAFTA's advocates did not take credit for it, although trade, investment, and social and economic integration had accelerated. Nor did the opponents of NAFTA bemoan its negative effects—the peso crisis in Mexico; the bailout organized and substantially funded by the United States; or the weak Canadian dollar. NAFTA, as politicians in all three countries informed me, was "not an issue anymore."[1]

It should have been. And it should be. NAFTA has been a scapegoat for disgruntled or uncompetitive groups in each country, but it has been a success for what it was designed to do. By reducing and eventually eliminating trade barriers among the three countries, NAFTA has gener-

1. I conducted interviews in Ottawa with leaders of the major parties in May 2000 and in Mexico in June and July 2000.

ated spectacular growth in trade and investment while improving national productivity and competitiveness. And the soaring traffic has not been just in goods. In the last year of the 20th century, people legally crossed the US-Canadian border 200 million times and the US-Mexican one 300 million times.[2] This amounts to nearly 1.4 million crossings a day. The integration that preceded NAFTA and was accelerated by it created striking opportunities for North America—but also dangerous vulnerabilities. The purpose of this book is to offer ideas on how the three governments can take advantage of the opportunities and take steps to reduce the vulnerabilities due to integration.

What's wrong with NAFTA is not what it did, but what it omitted. The agreement did not envisage any unified approach to extract NAFTA's promise, nor did it contemplate any common response to new threats. NAFTA simply assumed that the peoples of North America would benefit from the magic of a free marketplace, and that the three governments would resolve old or new problems. But in the absence of a compelling vision to define a modern regional entity, and lacking institutions to translate that vision into policies, the old patterns of behavior among the three governments remained. This meant that the US penchant for unilateralism and the Canadian and Mexican preference for bilateralism have trumped NAFTA's promise of a novel trilateral partnership.

Evaluations of NAFTA—both positive and negative—have tended to focus on the balance of trade and capital flows and the creation and loss of jobs. These are important issues, but they are hardly sufficient to take the pulse of such a complex, dynamic phenomenon. These fail, for example, to take into account the reorganization of large corporations with plants in all three countries, or the way in which environmental groups have reached across borders to press for higher standards, or the new alliances between labor unions in the United States and the Mexican government to assure the rights of migrants.

Few analysts of NAFTA have sought to learn from the experience of the longest-running, most successful regional trading scheme, the European Union (EU). Few leaders have proffered a vision of a future relationship among the North American countries. The exception is the new president of Mexico, Vicente Fox Quesada. His inauguration on 1 December 2000 represented a historic change for Mexico—the first peaceful, democratic transfer of power in the country's history. Fox has studied the European Union's experience in integrating poorer countries on its periphery, and he boldly proposed replacing the Free Trade Area with a common market. George

2. For the most recent data on the two-way traffic across the US-Canadian border, see Department of Foreign Affairs and International Trade of Canada, *Canada-US Partnership: Building a Border for the 21st Century* (Ottawa, December 2000, 2); and for the US-Mexican border, see ''Welcome to America: The Border is Vanishing Before Our Eyes,'' *Time: Special Issue*, 11 June 2001, 38.

W. Bush, the new president of the United States, and Jean Chrétien, the reelected prime minister of Canada, both acknowledged the importance of the three-sided relationship and affirmed their interest in improving it. But neither defined the path to amelioration, nor did they signal any interest in establishing a common market.

Fox was persistent, however. He invited Bush to his ranch in Guanajuato on 16 February 2001, and persuaded the new US president to endorse a joint communiqué entitled the Guanajuato Proposal, a fulsome statement of common goals and principles. "Among our highest priorities," the two presidents promised, "is unfettering the economic potential of every citizen, so each may contribute fully to narrowing the economic gaps between and within our societies." Fox and Bush went further, pledging to consult with the Canadian prime minister, and then "we will strive to consolidate a North American economic community whose benefits reach the lesser-developed areas of the region and extend to the most vulnerable social groups in our countries."[3] Fox proposed that labor be permitted to move freely in North America, though he recognized that this might not be possible for 20 years or more, given the wide divergence in incomes. He suggested a compensation fund to assist the development of the poor regions of Mexico. He and his foreign minister, Jorge G. Castañeda, modeled their proposals on Europe's experience. Bush and Chrétien promised to study these ideas.

This book aims to take the skeleton of Fox's idea and graft a body onto it. I will analyze NAFTA's successes and shortcomings, seek to draw some lessons from the European Union, and propose ways for NAFTA to incorporate and adapt those lessons.

The Crisis of 1994 and NAFTA's Flaw

On 1 December 1994, at the end of the first year of NAFTA, a new Mexican administration under President Ernesto Zedillo took office. Three weeks later, after allowing a 15 percent depreciation, his government let the Mexican peso float, and it sank like a stone, losing about 40 percent of its value. The first reaction by Robert Rubin, the director of the National Economic Council in the US administration of Bill Clinton—who had just been named Secretary of Treasury—was "to let the market sort it out."[4]

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3. "Toward a Partnership for Prosperity: The Guanajuato Proposal, Joint Communiqué," 16 February 2001, www.presidencia.gob.mx.

4. Cited in David Sanger, "The Education of Robert Rubin," *New York Times*, 5 February 1995, III, 1, 3. For a fuller description of what occurred, see Robert A. Pastor, "The United States and the Americas: Unfilled Promise at the Century's Turn," in *Eagle Rules? Foreign Policy and American Primacy in the Twenty-First Century*, ed. Robert J. Lieber (Upper Saddle River, NJ: Prentice Hall, 2002).

Soon after that, both governments began a long stumble that lasted more than a month before they could assemble a rescue package of $53 billion that would include $20 billion from the US Exchange Stabilization Fund. By the time the two governments reached an agreement, the initial damage had been compounded. Mexico's economy was in a shambles; its hopes of using NAFTA as a highway to the industrial world were dashed; 1 million jobs had been lost; and most of its major banks had failed.

Moreover, NAFTA was so discredited that President Clinton, who had heralded it as a model for the hemisphere just weeks before the crash, barely uttered the phrase again in that or in his next term. The issue and the agreement seemed to disappear from the policy debate, not just in the United States but in all three countries. And the ripple effects of the peso crash extended far beyond North America. One week before, 9-11 December 1994, 34 democratically elected presidents in the Americas met at a summit in Miami and promised to negotiate by 2005 a Free Trade Area of the Americas (FTAA). The decade ended with that promise unfulfilled. Indeed, President Clinton could not even extract the authority from the US Congress to negotiate any trade agreements.

This pivotal peso crisis had multiple causes. Mexico had suffered severe political setbacks during 1994, including the assassinations of the presidential candidate and secretary general of the governing Institutional Revolutionary Party (PRI). These events struck fear in the public and in the financial markets. Foreign capital began to flee. To reattract foreign investment, the Mexican government lifted interest rates and denominated its short-term bonds in dollars. By the end of the year, foreign investors had stopped buying the bonds and had begun to redeem them, causing a crisis of solvency that led to a wholesale exit of capital, much of it by Mexicans, and the resulting devaluation.

In retrospect, some analysts believed the crisis was due to the lack of transparency in Mexico's financial system. No doubt Mexico's weaknesses played a role in the crash, but one also needs to look more closely at the flow of international capital. In 1993, large amounts of money moved to emerging markets like Mexico's, but the next year, when the economies of the industrial countries recovered, the capital returned.

Some economists rang alarm bells in the fall of 1994 that Mexico's finances were overextended and its currency was overvalued, but the awkward truth is that policymakers in the three countries did not anticipate or plan for a financial crisis in the weakest member. NAFTA did not contemplate regular, high-level consultations, let alone any coordination among the three central banks or three treasury departments. The three leaders did not consult with each other. When Zedillo and his designee for finance minister traveled to Washington to meet with Clinton and his aides in November 1994, they were ready to request help from the United States, but they found Clinton utterly preoccupied by his party's loss of

Congress in elections that month. Clinton's advisors had been in contact with their counterparts, but neither side proposed ways to preempt the catastrophe that some saw coming.[5]

The peso crisis has been analyzed in great detail elsewhere.[6] It was due to an unfortunate collision between a political crisis and an overvalued peso. The premise of this book is that *the peso crisis was also a metaphor for both the success and the inadequacy of NAFTA.* The success was reflected in the expansion of trade and capital flows; the inadequacy was manifest in the lack of institutional capacity among the three governments to monitor, anticipate, plan for, or even respond to such a serious problem. NAFTA, in brief, was defined too narrowly, and the three governments paid a price for that myopia, albeit a price that varied among the three countries. Even worse, the three governments have not learned the lesson of 1994; they still apparently fail to understand the many dimensions of the phenomenon of North American integration.

The inescapable conclusion is that similar collective problems will emerge in the future, although in different guises, and that there is no institutional capacity to address them. New leaders, lacking a historical memory, may well repeat the old mistakes. After decades of trying to resist the multiple pressures toward integration with the United States, the governments of Canada and Mexico recognized that their efforts were worse than fruitless; they had become counterproductive. They reversed course and negotiated an agreement that accelerated a process of social and economic integration among natural but very unequal trading partners. The agreement eliminates trade and investment barriers, but it assumes that the social, economic, and political consequences of dismantling those walls will be trivial. NAFTA's charter (with the partial exception of the side agreements on labor and the environment) overlooked the concept of ''externalities''—that markets generate unintended but costly social, environmental, and political consequences.

The ''dark side'' of integration also was ignored. As barriers to legitimate trade declined, the opportunities for illegitimate trade naturally increased. Governments cannot erase impediments to trade and travel between them without also facilitating drug trafficking, illegal migration, money laundering, and illicit arms sales. Indeed, this is both the supreme paradox and the most intractable problem associated with free trade areas: how can nation-states facilitate integration without widening opportunities for crime? Or conversely, how can governments retard or stop such crimes without unduly restricting legal trade?

5. This is based on interviews with senior Mexican and US government officials.

6. The most complete, balanced, and astute analysis can be found in Sidney Weintraub, *Financial Decision-Making in Mexico: To Bet a Nation* (Pittsburgh: University of Pittsburgh Press, 2000).

NAFTA's authors had incorporated a provision to allow each country to leave NAFTA if it failed, but there were no provisions to handle the "success" of freeing capital movements by institutionalizing consultation and, to the extent possible, coordination among the central banks. The three governments dealt routinely and usually bilaterally with such issues as drugs, immigration, debts, trucking, and taxes, but there were few if any mechanisms to relate these issues to each other or to NAFTA. As a result, one country's drug policies sometimes make it more difficult to address shared concerns on immigration, and policies on Mexico's repayment of its debt have the unintended effect of encouraging immigration. Because NAFTA is bereft of institutions, the three countries rarely see—let alone address—the connections between the problems or how implementing different policies may lead to their acting at cross-purposes.

An extraordinarily complex process of integration is under way, but the three countries still tend to focus on one problem or one commodity, two countries at a time. The issues are drugs and immigration; the commodities are softwood lumber, sugar, fruit, and vegetables. We continue to bilateralize and compartmentalize, though these problems only fester when we do so. We have not allowed our imaginations to recognize and seize the opportunities presented by the emergence of a formidable new region.

More than 400 million people live in the three countries of North America, which cover 21.3 million square kilometers of territory (see table 1.1). Their combined gross product in 1999 was nearly $10 trillion. In territory, population, and product, NAFTA is larger than the 15-nation European Union. There is a convergence among the countries on the rate of population growth, because Mexico's annual growth rate has declined sharply since the mid-1970s—from 3.4 to 1.9 in 1999. This growth rate still exceeds that of its northern neighbors, but Canada and the United States are virtually the only two industrial countries with net population growth—largely because of immigration—and of course, Mexico's population growth is diminished by emigration. The population profiles, however, are complementary, with Mexico's average population being much younger than its two northern neighbors. The life expectancy of Mexicans is also increasing faster than that of Americans and Canadians, but it is still 5-7 years behind. The level of education of its students remains quite low by Canadian and US standards.

Of the many bonds of economic integration among the three countries, trade is growing fastest, and NAFTA has accelerated a trend that began in the mid-1980s (see table 1.2).[7] In the past two decades, Mexico's total

7. A measure of the growing integration is the increase in trade among the three regional partners as a percentage of their total trade. Mutti looks at US-Mexican trade and calculates "trade intensity indices" (e.g., US exports to Mexico as a percentage of its total exports) and, although he finds that the intensity index for US imports from Mexico increased by about 40 percent between 1993 and 1999, it declined slightly for exports. He concludes that integration began in the 1980s and that its full effects have not yet occurred. See John Mutti, *NAFTA: The Economic Consequences for Mexico and the United States* (Washington: Economic Strategy Institute, 2001), 27-30.

Table 1.1 Indicators for the three countries of North America, 1990-99

Indicator	United States		Canada		Mexico		NAFTA		United States (as percent of NAFTA)	
	1990	1999	1990	1999	1990	1999	1990	1999	1990	1999
GDP (millions of dollars)	5,554,100	8,708,870	572,673	612,049	262,710	474,951	6,389,483	9,795,870	86.9	88.9
Per capita GDP (current)	22,216	30,992	21,610	19,744	3,048	4,896	17,616	23,951		
Area (thousands of square kilometers)	9,364		9,971		1,958		21,293			
Population (millions)	250	281[c]	26.5	31	86.2	97	362.7	409	69	69
Average annual growth rate 1990-99 (percent)	1.2		1.2		1.9					
Life expectancy at birth[a]	76	77	77	79	70	72				
Percent of GNP spent on education[b]	6.7	5.4	6.9	6.9	4.7	4.9				
Secondary school net enrollment ratio (percent)	94	96	84	95	67	66				
Total exports of goods (millions of dollars)	393,587	693,000	127,688	238,450	40,711	136,660	561,986	1,068,110	70	65
Percent of exports of goods to North America	28.4	36.2	75.3	86.4	46.4	86.0	42.8	54.7		
Total imports of goods (millions of dollars)	495,252	1,059,200	115,242	215,560	41,592	142,063	652,086	1,416,823	76	75
Percent of imports of goods from North America	24.5	29.5	66.6	70.0	50.4	62.0	33.5	41.3		

a. Data are from 1990 and 1998. The 1998 figure was computed by averaging the life expectancies for males and females.
b. Data are from 1980 and 1997.
c. Population is for 2000.

Sources: World Bank, *World Development Report* (1992 and 2001) for GDP, per capita GDP, area, life expectancy, percentage of GNP spent on education, qand secondary school net enrollment ratio. Trade data are from International Monetary Fund, *Direction of Trade Statistics Yearbook* (1990); World Trade Organization, *International Trade Statistics, 2000*, http://www.wto.org/english/res_e/statis_e/stat_toc_e.htm; Bureau of Transportation Statistics, *North American Transportation in Figures*, 2000, http://www.bts.gov/itt/natf.html; International Monetary Fund, *Direction of Trade Statistics Yearbook*, 1990; and Inter-American Development Bank, *ESDB Query Facility, 2000*, http://database.iadb.org/esdbweb/scripts/esdbweb.exe.

trade increased seven times; Canada's and the United States', more than three times. More significantly, all three countries' trade with each other increased at a far more rapid rate than world trade (see table 1.3). Canada and Mexico rely on the United States to purchase more than 80 percent of their exports, and the United States now sells more than a third of all its exports to its two neighbors. A thick web of commerce, finance, and interdependence has been spun across the continent of North America. But the challenge of integrating three such disparate economies is clearly beyond the capacity of NAFTA, as it is currently constituted.

Lessons from the Old World

Even as Canadians and Mexicans struggled to shore up their distinct currency crises, Europe was trying to combine 12 or more currencies into 1—a feat of heroic proportions in a world in which islands of 10,000 people demanded sovereignty. Across the ocean sat the longest-lasting, most successful experiment in integration among sovereign states—the European Union[8]—and yet only a few considered drawing any lessons from its experience.[9] This is partly because the origin, purpose, and composition of the European Union were quite different from those of NAFTA. The European Union was born of two cataclysmic wars and a fervent desire for peace; its purpose and model was to build a community; and its members were more equal in size and power than was true of NAFTA. In addition, many Americans were skeptical as to whether the experiment with a unified currency would succeed, and they also viewed the thick EU ''social safety net'' as a cause of Europe's higher unemployment and therefore as hardly a model worth replicating.

There are two other reasons why the EU ''model'' was viewed as having limited relevance. First, the income disparity between Mexico and its two

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8. Europe's Common Market began as the European Coal and Steel Community in 1951 and was transformed by the Treaty of Rome into the European Economic Community (EEC) in 1957. Later, it became the European Community (EC) and subsequently, after the Treaty of Maastricht in 1991, the European Union (EU). I will use ''EC,'' ''EU,'' or the Union to refer to the European entity.

9. A few did ask the questions, but the answers were very preliminary. See, e.g., Albert Fishlow, Sherman Robinson, and Raul Hinojosa-Ojeda, ''Proposal for a North American Regional Development Bank,'' paper prepared for a conference sponsored by the Federal Reserve Bank of Dallas (14 June 1991); Donald J. Puchala, ''The European Communities and the North American Free Trade Area,'' paper prepared for a conference on NAFTA at the Carter Center of Emory University (12 February 1992); and Robert A. Pastor, *Integration with Mexico: Options for US Policy* (New York: Twentieth Century Fund, 1993), chap. 5.

Table 1.2 North American trade with the world, 1980-99
(in millions of current dollars)

Country	1980	1990	1999
Exports			
Canada	67,730	127,688	238,450
Mexico	18,031	40,711	136,660
United States	220,781	393,587	693,000
Total	306,542	561,986	1,068,110
Imports			
Canada	61,004	115,242	215,560
Mexico	21,087	41,592	142,063
United States	256,959	495,252	1,059,200
Total	339,050	652,086	1,416,823
Total trade (exports and imports)			
Canada	128,734	242,930	454,010
Mexico	39,118	82,303	278,723
United States	477,740	888,839	1,752,200
Total	645,592	1,214,072	2,484,933

Sources: World Trade Organization, *International Trade Statistics, 2000*, http://www.wto.org/english/res_e/statis_e/stat_toc_e.htm; US Bureau of Transportation Statistics, *North American Transportation in Figures, 2000*, http://www.bts.gov/itt/natf.html; International Monetary Fund, *Direction of Trade Statistics Yearbook, 1990*; and Inter-American Development Bank, *ESDB Query Facility, 2000*, http://database.iadb.org/esdbweb/scripts/esdbweb.exe.

wealthy northern neighbors is much wider than that between poor and rich European countries, and therefore the prospect of reducing it seemed remote. Second, NAFTA is just a free trade area, whereas the European Union passed that threshold decades ago, on its way to becoming a customs union (with a common external tariff), a common market (with free movement of labor and capital), and finally an economic and monetary union.

Nonetheless, having identified the differences, one could still profit from analyzing the EU experience. The European Union reduced the volatility that disproportionately harmed its weak economies. And, during 40 years of trial and error, the Union significantly narrowed the disparities in income between its rich and poor members. The question, therefore, is not whether the Union developed the ideal model, but whether there are elements of its experience that NAFTA could learn from, adapt, and adopt. We will examine Europe's policies to see which ones worked best to narrow the gap between rich and poor countries and which policies were least effective.

The virtual disappearance of the issue of NAFTA from the politics of the three countries suggests that NAFTA may have descended to the peculiar resting place that controversial issues, like the Panama Canal

Table 1.3 Trade within North America and intraregional trade as percent of total world trade, 1980-99

	Exports						Imports					
	1980		1990		1999		1980		1990		1999	
Country	**Dollars**	**Percent**	**Dollars**	**Percent**	**Dollars**	**Percent**	**Dollars**	**Percent**	**Dollars**	**Percent**	**Dollars**	**Percent**
Canadian trade with												
Mexico	547	0.8	562	0.4	1,100	0.5	153	0.3	1,497	1.3	6,420	3.0
United States	53,614	79.2	95,611	74.9	205,020	86.0	46,208	75.7	75,286	65.3	144,430	67.0
Total	54,161	80.0	96,173	75.3	206,120	86.4	46,361	76.0	76,783	66.6	150,850	70.0
Mexican trade with												
Canada	153	0.8	458	1.1	6,420	4.7	547	2.6	458	1.1	1,100	0.8
United States	13,149	72.9	18,418	45.2	111,100	81.3	19,773	93.8	20,491	49.3	87,000	61.2
Total	13,302	73.8	18,876	46.4	117,520	86.0	20,320	96.4	20,949	50.4	88,100	62.0
United States trade with												
Canada	46,208	20.9	83,674	21.3	163,900	23.7	53,614	20.9	91,380	18.5	201,400	19.0
Mexico	19,773	9.0	28,279	7.2	87,000	12.6	13,149	5.1	30,157	6.1	111,100	10.5
Total	65,981	29.9	111,953	28.4	250,900	36.2	66,763	26.0	121,537	24.5	312,500	29.5
NAFTA total[a]	133,444		227,002		574,540		133,444		219,269		551,450	

a. Differences between intraregional imports and exports in 1990 and 1999 reflect differences in national trade accounts.

Sources: World Trade Organization, *International Trade Statistics, 2000*, http://www.wto.org/english/res_e/statis_e/stat_toc_e.htm; US Bureau of Transportation Statistics, *North American Transportation in Figures, 2000*, http://www.bts.gov/itt/natf.html, International Monetary Fund, *Direction of Trade Statistics Yearbook*, 1990; and Inter-American Development Bank, *ESDB Query Facility, 2000*, http://database.iadb.org/esdbweb/scripts/esdbweb.exe.

treaties, go after terrible predictions about their impact are proven wrong or forgotten. It simply left the public's radar screen.

Scholars, however, have continued to examine NAFTA, and several have looked at the European Union's experience for lessons. Let us review some of the literature. In *The New American Community*, Rosenberg views NAFTA as just one small step toward an entity that encompasses all the nations of the Americas and is almost indistinguishable from the European Union. His experience has been in Europe—not in the Americas—and thus it is not surprising that he borrows extensively from Europe's treaties and institutions and does little to adapt them. Indeed, his proposal verges on being almost a literal translation of the European Union into American, with an occasional modest change in language. For example, he suggests that an alternative name for a unifying Commission could be the ''Executive Branch,'' but its role would be the same as that of the European Commission. It would initiate legislation, ensure the compliance of the three governments, administer common policies, and negotiate trade agreements with countries in other regions. The ''Executive Branch'' would be organized like the European Commission, with directorate-generals and cabinets. As in Europe, the Council of Ministers would be the principal decision-making body, deciding on legislation, coordinating members' economic policies, and so on.[10]

Several studies have focused on EU regional policies. Sweet offers a comprehensive description of the regional policies of Europe and also of the three governments of North America. He traces US regional policy back to the Franklin D. Roosevelt administration's New Deal, but describes its fuller development during John F. Kennedy's and Lyndon Johnson's administrations. Since then, and particularly since Ronald Reagan's administration, the federal government has given less attention to helping poor regions. Nonetheless, the US General Accounting Office still lists 340 federal economic development programs administered by 13 executive departments and agencies, with an annual core budget of about $6 billion.[11] He then describes Canada's policies toward its provinces, Mexico's policies toward its rural areas, and the European Union's regional and cohesion programs. He examines various European funds and evaluates their benefits and costs, concluding that the EU Structural Funds ''led to a significant improvement in the economic performance of most recipients.''[12]

10. Jerry M. Rosenberg, *The New American Community: A Response to the European and Asian Economic Challenge* (Westport, CT: Praeger, 1992), esp. chaps. 8 and 9.

11. Morris L. Sweet, *Regional Economic Development in the European Union and North America* (Westport, CT: Praeger, 1999), 257.

12. Sweet, *Regional Economic Development*, 130.

López Roldán, a Mexican scholar, recognized that the Mexican government's regional policy could not transfer the kinds of resources to poor regions as did its neighbors and the European Union. Of course, NAFTA did not envisage any policy for the poor regions of Mexico, but he recommends that the North American governments establish a system of structural funds to reduce disparities.[13]

Grinspun and Kreklewich view NAFTA as a product of a neoliberal economic philosophy and the hegemonic power of the United States and its corporations. The authors accept that the challenge is no longer whether to integrate with the world economy but rather how, and they propose that new institutions be established to strengthen popular participation and balance the unhealthy weight of multinational corporations. They point to the regime on intellectual property rights to show that large corporations have imposed a set of rules that serve their interests rather than the public's. The rules limit the free flow of information, technology, and trademarks to the detriment, in their view, of poor people and countries. The authors are not very specific as to how to achieve a new equilibrium—except to say that Europe's experience has been better balanced, partly because of its institutions and its social charter.[14]

MacMillan returns to the original question of relevance but reaches a very different conclusion. She sees the European Union and NAFTA as so different that one cannot extract meaningful lessons. The Union is more legalistic, with supranational institutions like the European Court of Justice that can insist on the supremacy of EU law over national law. Moreover, the Union has its own tax base, albeit a relatively small one, and common policies on agriculture, antitrust, and so on. NAFTA has none of these.[15]

Gianaris examines the evolution of the European Union and NAFTA and its policies on trade, industrialization, joint ventures, and fiscal and monetary affairs, but he stops short of drawing a comparison or asking whether lessons from one region's experience are useful for the other.[16] Similarly, the United Nations Economic Commission for Europe commis-

13. Mario López Roldán, "Tres Experiencias Europeas en Materia de Integración Económica Regional que Pueden Ser Utiles para Mexico en el Process de Integración de America del Norte," Madrid, photocopy (January 1996).

14. Ricardo Grinspun and Robert Kreklewich, "Institutions, Power Relations, and Unequal Integration in the Americas: NAFTA as Deficient Institutionality," in *Economic Integration in NAFTA and the EU*, ed. Kirsten Appendini and Sven Bislev (New York: St. Martin's Press, 1999).

15. Gretchen M. MacMillan, Managing Economic Convergence in the EU, in *Toward A North American Community: Canada, the US, and Mexico*, ed. Donald Barry (Boulder, CO: Westview Press, 1995).

16. Nicholas V. Gianaris, *The North American Free Trade Agreement and the European Union* (Westport, CT: Praeger, 1998).

sioned studies on the integration process within Europe and between the European Union and a number of Eastern European countries. A chapter was added on the US-Canadian Free Trade Agreement (FTA), but no explicit comparisons were made that might help the reader draw some lessons.[17]

In summary, the literature has grown on the subject of the European Union and how its programs might help North America. A more practical question is why Canadians and Mexicans have not insisted on drafting a social charter—or, until Fox, why they have not sought funds to reduce disparities. Canadians have given considerable thought to the concept of "social cohesion," and its implications for trying to build a community within Canada, but they have not applied this concept to Mexico or a North American Community.[18] One would think that, to compensate for their relative weakness, Canadians or Mexicans would seek ways to collaborate and pursue North American answers to collective problems. But that has not been the case. Why?

From the periphery of the continent, it is hard to see over the US elephant. Since the onset of NAFTA, Canada's and Mexico's trade with the United States has grown from about two-thirds to more than 80 percent of their total trade. Interviews with leaders in both countries whose political philosophies are spread across a wide spectrum led me to conclude that both countries are utterly absorbed with their own problems. To the extent that they look at the world, they invest most of their energy in their bilateral relationship with the United States.

Canadians and Mexicans initially approached each other, hoping for an informal alliance against the colossus, but they soon realized that this was not a productive approach. Each was averse to being used to serve the other's purposes, and the United States took offense at being the target of their collaboration. Each then retreated to the bilateralism of the past. Neither country has shown much interest in establishing trinational institutions, in part because they suspect that the United States is uninterested and that their proposals would not prosper. The United States, whether as a government or society, has not displayed an excess of imagination on North American issues, perhaps believing that its economic weight and the existing configuration of the relationship assures outcomes favorable to its interests.

All this could change if Fox persists with his agenda for a common market. The United States—with its large, growing Mexican American

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17. United Nations Economic Commission for Europe, *Economic Integration in Europe and North America* (New York: United Nations, 1995).

18. See The Standing Senate Committee on Social Affairs, Science, and Technology, *Final Report on Social Cohesion* (Ottawa, June 1999); and Jane Jenson, *Mapping Social Cohesion: The State of Canadian Research*, Study F03 (Ottawa: Canadian Policy Research Network, 1998).

population—cannot afford to ignore his proposal, and might see an advantage in taking it seriously. If the United States begins negotiating a deeper relationship with Mexico, Canada cannot afford to sit on the sidelines. In brief, *Fox might introduce a new dynamic* into a static equation.

If and when the Bush administration persuades Congress to approve trade-promotion authority (previously described as "fast-track"), trade negotiations in the Americas will experience a jump-start. For the past several years, the principal trading initiative in the hemisphere has originated with the four countries of Mercosur. Chile and Bolivia associated with it. On 31 August and 1 September 2000, the Brazilian president invited all of his freely elected colleagues from South America to open discussions on a South American Free Trade Area (SAFTA). It was reported that Brazil hoped the talks would strengthen South America's bargaining power vis-à-vis the United States and NAFTA. On 1 December 2000, however, Chile turned away from Mercosur—in part because tariff rates were high—and initiated trade talks with the United States, despite the fact that the US president does not have authority to complete such an agreement. The Chilean decision is a reflection of the overweening power of the US market. The United States generates 76 percent and its two neighbors add 9 percent of the combined gross product of all the Americas.[19] When the Congress grants the president authority, the negotiations for the FTAA will become serious very quickly.

Organization of the Book

In chapter 2, to explain the limitations and the potential of NAFTA, I identify parameters for comparing NAFTA with the European Union and with two Asian entities, Asia-Pacific Economic Cooperation and the Association of South East Asian Nations—each of which is based on a model that addresses the global challenge of integration in ways unique to its region. One principal challenge of the 21st century is to find effective mechanisms for integrating developing countries into the global economy. Foreign aid is essential to lift countries from poverty, but the path toward sustainable economic growth requires trade, and one path toward that goal is to connect with a major trading scheme—the European Union or NAFTA. A recent World Bank report concluded that "selecting high-income countries as partners is often likely to be the best option for developing countries," but to ensure that such schemes respond to the needs of the poor countries "will require the creation of mechanisms to

19. See World Bank, *World Development Indicators 2000* (Washington: World Bank, 2000), table 7.1, 252-53.

ensure an equitable distribution of gain.''[20] That is one more reason why NAFTA needs to be redesigned: to develop new policies to reduce income disparities.

Chapter 3 describes and evaluates the European Union's regional and cohesion policies. What led the Union to place such value on reducing disparities? Which programs were most effective, and why? What lessons can be drawn for a North American community? Chapter 4 examines NAFTA and its evolution, asking what problems have emerged and what opportunities have been missed.

The heart of the book resides in chapters 5 and 6, where I try to respond to NAFTA's limitations with in-depth proposals for a deeper relationship. Much of the analysis is based on lessons that I extract from the European Union and adapt to the special circumstances of North America. The goals of NAFTA need amending, and I describe the institutions that should be established and how their mandate would differ from those in the European Union. Then, I identify and suggest North American policies for infrastructure and transportation, trade, and macroeconomic policies and a common currency. Chapter 6 offers North American plans for customs and immigration, energy, regional development, and education. Of course, many other sectors are in need of comprehensive, continental consideration, but the ones in these chapters are illustrative of what could be done.

In chapter 7, I address the question of whether the entire exercise is quixotic. A trilateral approach has often foundered on the preference of Canada and Mexico for bilateralism and the United States' disposition to go it alone. I offer some ideas for how the governments can be reorganized to consider a trilateral approach. But are the governments ready to give up their sovereignty and develop common approaches? Are they prepared to establish new common institutions? To answer these questions, I explore historical and contemporary understandings of ''sovereignty'' and consult public opinion surveys. The rather surprising conclusion is that the people of North America are way ahead of their leaders. A majority of the public in all three countries is willing to support North American political union if they could be convinced that it would improve their lives and not threaten their cultural identity.

At the end of chapter 7, I develop three grand options for North America, and then explain why a fourth incremental, practical option should instead be chosen. That fourth option should aim to ''deepen'' the relationship among the three countries along the lines sketched in chapters 5 and 6.

Finally, chapter 8 looks beyond NAFTA to the Free Trade Area of the Americas, and beyond that to implications for the world's political

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20. World Bank, *Trade Blocs: A Policy Research Report* (New York: Oxford University Press, 2000), x-xi.

economy. Should the United States deepen its relationship with its neighbors or widen it first to include the nations on its periphery? How should NAFTA relate to the FTAA and to the World Trade Organization (WTO)? Which path ought to have priority? I argue that we ought to pursue a deeper NAFTA, a wider FTAA, and global trade talks at the same time, because each is addressing a distinct set of issues. Moreover, the fact that the United States has three sets of options will generate competition and, it is to be hoped, more progress in all the talks.

Should NAFTA Be Deepened? Is This the Moment?

Although there are groups within each NAFTA member state that would prefer to renounce or fundamentally alter the agreement, the three governments are all reasonably satisfied with it. And they have reason to be: Their trade and investment with each other have expanded far more rapidly than with the rest of the world, and many of their corporations have become continental and more competitive. And yet everyone knows the dangers of complacency. In a rapidly changing world, one cannot expect to maintain one's place, let alone grow, if one sits still. As Will Rogers once said: "Even if you're on the right road, if you sit down, you can get run over." *There are seven compelling reasons why the three governments of North America need to reevaluate NAFTA and seize this moment to explore aggressively new paths to deepen the relationship.*

First, NAFTA has not changed the pattern of the United States' relations with its two neighbors. This relationship is driven by deep-seated emotions and highly organized domestic interests, and most of the hard problems are addressed in forums that lack trinational rules. Some interests seek protection from competition—such as dairy and textiles in Canada; corn and services in Mexico; and lumber, sugar, and trucking in the United States. Other groups seek to deflect attention from local problems, such as when the United States seeks answers to its drug problems by condemning Mexico, or Mexico criticizes US immigration policies for its unemployment problem. Many of these problems are confronted again and again in ways that erode the relationship. In the end, the asymmetry of power makes solutions difficult, and often leaves a bitter taste. The only way to change these old habits is to submit them to a new structure—one based on rules rather than power or a sense of inferiority. The best time is at the beginning of national administrations, when there is a honeymoon period, and that opportunity is multiplied by three because the three leaders were recently inaugurated within months of each other.

Second, NAFTA has failed to deal with the contradictions inherent in the problem of integrating such diverse economies and societies. The most basic contradiction is that the elimination of barriers to trade in legal goods also makes it easier to smuggle illegal goods, and the steps normally taken by a government to prevent smuggling inevitably impede the exchange of legal goods. As the United States tries to stop drugs from coming across its borders, and as Mexico tries to stop illicit guns coming from the United States, legitimate businesses have to pay for the delays—often more than the amount of the tariff that was eliminated. There are ways to cope with these contradictions, but they require new formulas for cooperation.

Third, to sustain and to strengthen a cooperative spirit, the three governments should explore common approaches to other foreign policy issues. They might begin with developing a single approach to trade policy as it relates to global trade talks and third countries. Cuba might provide a second opportunity. Since Fidel Castro came to power in 1959, the three governments have adopted very different approaches to Cuba. None have been successful, except in irritating the others. It might not be possible for the three to bridge the differences, but their relationship would benefit and their policies would be more effective if they succeeded.

Fourth, the three governments need to discuss controversial issues like a common currency. As the three economies become more highly integrated, major shifts in foreign exchange rates have a huge impact on trade and on domestic businesses. Insofar as exchange rates are fundamentally undervalued, they could lead to unwarranted industrial restructuring, or they could aggravate protectionism. US efforts to countervail Canadian wheat and lumber products are due in part to Canada's undervalued currency. A single currency would solve many of these problems, but it might create others. That is a plea to address the issue now rather than delay until a full-blown crisis strikes.

Fifth, the three countries are undergoing a profound process of social integration because of immigration. For Canada and the United States, immigration has become a growing source of population growth and employment. For Mexico, emigration and remittances have a pervasive psychological and financial effect. No issue looms as important for Mexico in 2001 as immigration. But the United States will need to take into account the distributive consequences and the social tensions inherent in immigration before responding to Fox's proposals for more visas. Even as US leaders express their condolences on the death of illegal migrants in the Arizona desert, an increasing number of Arizona ranchers take the law into their own hands. The many-sided issues of immigration can only yield a coherent response if the three governments first place them in a broader context.

Sixth, innumerable opportunities have not been addressed because we are looking at the relationship from the wrong direction. For example, although more than 75 percent of the goods exchanged by the three countries each year are carried by trucks, a trucker must cross 64 separate jurisdictions in North America, and the variation in safety standards and working conditions is so wide that it becomes impossible for the trucker to keep his costs low. NAFTA would benefit from a forum and an office whose responsibility would be to devise a North American plan for transportation and infrastructure, and for other issues as well.

Seventh, the most compelling practical reason to approach NAFTA with a different mindset is its original premise's lack of realism. The agreement was negotiated as if the three countries were of equal size and economic weight. That unrealistic assumption permitted a rule-based formula to eliminate trade and investment barriers, and in the long term, that is probably the best approach. In the short term, however, it ignored the uneven economic development, different vulnerabilities, and wide disparities in income and employment among the three countries.

These wide disparities ought to focus the minds of the countries' leaders, for several reasons. They are the principal motives for migration among the well-off (''brain drain'') and the poor alike, thus contributing to a widening gap separating Mexico from its neighbors. No solution to the immigration problem is possible without a significant reduction in the gap between incomes in Mexico and in the United States. It is also difficult to conceive of a sense of community until there is a greater balance in the relationship between the one poor and two rich countries of North America. And without such a sense of community, it will be difficult to deal with problems, such as water shortages or transnational crime. The fact that integration is not reducing the gap is not an argument against integration; it merely suggests that additional steps are essential. The main argument for deepening NAFTA, however, is the simplest: *Problems can no longer be contained in any of the three countries, and new opportunities benefit all three*.

For all these reasons, the United States and its neighbors have an opportunity at this moment in history to create a *community of diversity* and to build a *model that gives a boost to the middle class of the developing world*. The United States does not need to reach across the world to seize that opportunity because it is right at its borders. Nor is the World Trade Organization (with its more than 142 member countries) likely to be the best forum. A trinational unit might be the optimal level at which to experiment with new approaches. The proposal by Fox offers an agenda, but new institutions are needed to organize the issues, provide concrete ideas, and stimulate leaders to make bold decisions.