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## FREE TRADE IMPACTS ON U.S. AND SOUTHERN AGRICULTURE: DISCUSSION

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The initiative to begin negotiations toward a North American Free Trade Agreement (NAFTA) in June of 1990 provided the potential for a major step forward in the journey toward sustained economic growth and development for Mexico and increased market opportunities for the U.S. and Canada. A successful NAFTA would result in the world's largest trading zone, 25 percent larger in GDP than the EC and an area which would consist of 362 million people with a combined output of almost \$6 trillion.

A major component of the proposed NAFTA, and one that will present both opportunities and challenges, is agriculture. While many agricultural interests are excited about the opportunities provided by a successful NAFTA, others view a possible agreement with skepticism and/or concern. In addition to agriculture, a great many other interests see benefits and/or the potential for expanded market opportunities from a NAFTA. However, just as in agricultural circles, not everyone views the prospective agreement in a positive light. Very briefly we would like to: (1) comment on some foreign policy related benefits of a successful NAFTA, (2) review some criticisms of a NAFTA raised during the debate over extension of the Fast Track Authority, and (3) review the Burfisher et al. paper on the impacts of NAFTA on southern agriculture.

### FOREIGN POLICY ELEMENTS OF A SUCCESSFUL NAFTA

In most international policy debates in the U.S., agricultural interests are just one set of the many voices that receive a hearing during the decision-making process. In testimony before the Senate Foreign Relations committee back in April, 1991, Robert Zoellick of the State Department was asked if the decision to enter into the NAFTA talks was motivated by economic policy or foreign policy interests. He replied yes and yes. Such is the nature of the international policy process.

In his testimony he outlined several reasons why a NAFTA is in the best interests of the U.S., defined from a foreign policy perspective. First, it will provide for an integration of North America that will

provide the foundation for increased cooperation and cohesion among neighbors who share a historic relationship not free from conflicts. This is especially true for Mexico where significant anxiety and distrust of its large neighbors to the North exist. This is not surprising since most Mexicans remember that almost one half of what was once Mexico was consumed by the U.S. from 1836 to 1853.

A second benefit suggested was increased integration to address a host of North American problems. Among those areas pointed out were migration, narcotics, and environment, which are not hindered by national borders.

A third point was the possibility for greater cooperation and agreement on foreign policy issues. Many examples can readily be brought to mind, especially related to U.S.-Mexican disagreements in the past, such as the difference of views over conflicts in Central America (e.g., El Salvador and Nicaragua) as well as Mexico's relations with Cuba. To highlight the potential for cooperation, the example of Mexico's increase in oil extraction following the Iraqi invasion of Kuwait, despite capacity constraints, was used.

The fourth foreign policy consideration outlined involved the signal a successful NAFTA would send to the rest of Latin America. It is no secret that the Bush administration has a vision of an Initiative for the Americas which would bring greater coordination to all the nations of Central and South America. While there is no lack of appreciation of the enormous problems that would have to be addressed, a successful NAFTA would provide an example that the possibility for such an effort exists.

Another foreign policy concern not outlined in Mr. Zoellick's testimony but evident in discussions with senior Mexican officials and others in the U.S. is that a successful NAFTA is essential in insuring that the reforms and progress begun in the De La Madrid era and expanded by President Salinas continue. The benefits for the Mexican people that can come from recent reform initiatives will take time to materialize. The successful completion of the NAFTA negotiations will demonstrate continuing international po-

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litical success for the reformers. Such success will be essential to maintain popular support in the selection of the next Mexican president who will be responsible for continuing the reform process.

## GENERAL CONCERNS

Throughout the debate over the extension of the Fast Track authority for NAFTA, several points of concern were repeatedly raised by opponents of the negotiations. Most often they were in reference to loss of jobs, or the environmental degradation that would surely result from any NAFTA. A careful examination of these issues is warranted.

**Labor Issues.** Central to the argument of most opponents to the authority to enter into NAFTA negotiations was that such an agreement would allow cheap Mexican labor to take away American jobs. A narrow vision of NAFTA as a zero sum game results in this conclusion. It assumes that a job created in one area takes a job away from somewhere else. There are at least a couple of reasons that suggest this position is faulty.

First, not much currently prevents U.S. companies from relocating to take advantage of low labor cost. The average tariff on Mexican imports is under 4 percent, and there is little restriction on investment for export purposes. Yet there has not been a flight of U.S. jobs to Mexico. In fact, a 1988 International Trade Commission study of 323 U.S. firms indicated that their Mexican assembly operations increased the competitiveness of their U.S. production, which resulted in the maintenance and creation of U.S. jobs. Department of Commerce estimates indicate that over 100,000 jobs have been created in the U.S. to support Maquiladora facilities.

Second, the effects of a successful NAFTA will result in a greater U.S. access to the Mexican market, a market where income and employment will be enhanced, and where \$.70 of every import dollar is spent in the U.S. Greater access to a favorable market may lead to increased opportunity for U.S. business. Indeed, studies by the Department of Labor suggest that an FTA would add between 44,500 jobs over 5 years and 64,000 jobs over 10 years. An MIT study suggests a higher return—20,000 to 30,000 jobs for each additional billion dollars in exports—leading to as many as 150,000 new U.S. jobs over 3-4 years.

It can be expected that if a successful NAFTA is concluded, it will provide a boost to the economies of all three countries. As a result it would lead to overall growth in employment and income, not to a shift in prosperity from one region to another.

**Environmental Issues.** Many groups have made claims that the result of a NAFTA will be serious deterioration of the physical environment of Mexico

and the border areas of the U.S. as firms rush to Mexico to escape tough environmental standards in the North. These firms would then have a competitive advantage in comparison to those in the U.S. or Canada because they would operate free from the cost of environmental regulation. Such claims stir the emotions of everyone concerned about the protection of the environment and the potential competitiveness of U.S. and Canadian industry. They are, however, based on assumptions that do not respect existing Mexican law and/or enforcement of environmental protection or the prospects for enhanced environmental quality that would come with increased economic prosperity resulting from a successful NAFTA.

In 1988, Mexico enacted the General Law for Ecological Equilibrium and Environmental Protection. Much of this law is based on U.S. standards. It covers air, water, and soil pollution; contamination by hazardous materials and waste; pesticides and toxic substances; the conservation of ecosystems; ecology reserves; and the use of national resources. The law establishes administrative sanctions and criminal penalties for noncompliance. It not only recognizes the need to impose standards on existing facilities and conditions but also requires environmental impact assessments for all new public or private investment projects.

The commitment of the current Mexican government to environmental protection and improvement of environmental quality in Mexico is evidenced by their actions. Between 1989 and 1991, some 980 temporary and 82 permanent closures of industrial facilities for failure to comply with environmental laws have been ordered. Measures to reduce air pollution in Mexico City have begun with the elimination of leaded gasoline and requirement of catalytic converters on taxis, and more recently, with the closing of Mexico's largest oil refinery because of air pollution.

While these antidotal actions are examples of the Mexican government's commitment to correcting environmental problems, the continued diversion of resources indicates their future plans. The budget for the Mexican Secretariat of Urban Development and Ecology (SEDUE) has increased eight-fold between 1989 and 1991 (from \$5 million to \$39 million). In anticipation of a World Bank loan, SEDUE has plans to add 50 to 150 new inspectors in the industrial cities of Guadalajara, Mexico City, Monterrey, and Tijuana. In addition, SEDUE is in the process of working with the U.S. EPA to develop an integrated environmental plan for the Mexico-U.S. border area, the first stage being 1992-1994.

The efforts to address existing environmental problems within Mexico are increasing, although these efforts are hampered by limited resources. The enactment of significant legal requirements for compliance with environmental standards for new investment assures that future problems will be lessened. Given these conditions it is difficult to imagine firms being motivated to relocate to Mexico with the idea that they will escape the constraints of compliance with regulations designed to maintain environmental quality. Indeed it seems more likely that a successful NAFTA will lead to better environmental quality in Mexico by virtue of a more prosperous economy having greater resources to devote to enforcement and monitoring efforts.

### **ESTIMATES OF OVERALL EFFECTS OF A NAFTA**

Some analysis of the potential effects of a NAFTA have been referred to in the discussion on labor; in addition, a few other studies or preliminary results of research efforts have been released. The Burfisher et al. study that will be discussed later deals with specific commodities. A brief glimpse at some of the more macro-oriented research results provides a good starting point.

At least three economic studies have provided some projections regarding the potential effects of a NAFTA for the U.S. The first is a study conducted by the U.S. International Trade Commission (ITC). The ITC study covered sectorial, regional, and general economic effects. Labor market effects were computed using a computable general equilibrium (CGE) model. The sectorial analysis was conducted using partial equilibrium models, interviews with experts, and qualitative assessments of non-price factors. The results were reported only in qualitative terms.

The ITC report concluded that the U.S. would gain from a NAFTA because of expanded trade opportunities, lower prices, increased competition, and savings resulting from larger scale production. Real output and wages for both higher and lower skilled workers was expected to increase.

The Department of Labor commissioned Dr. Clopper Almon at the University of Maryland to direct a cooperative project with the University of Guanajuato examining the industrial effects of a free trade agreement between Mexico and the U.S. The large macro model forecasts employment, production, prices, exports, and imports in all sectors for the period 1989 through 2000. The model predicted an increase in real GNP in the U.S. and moderate increases in exports and employment due to a NAFTA.

A study for the U.S. Council of the Mexico-U.S. Business Committee by Peat Marwick presented the results of a CGE model using 1988 as a base year. The study indicates how employment, wages, incomes, rates of return on capital, exports, and imports would have been different in 1988 had an NAFTA been in effect. The results are consistent with the Clopper Almon study. Modest improvements in real income, wages and return on capital were predicted.

### **ESTIMATES OF EFFECTS OF NAFTA ON SOUTHERN AGRICULTURE**

The rest of this paper focuses on the Burfisher et al. study. The study was to focus on the impact of NAFTA on southern agriculture. Based on this criterion the study was found to be lacking. However, the study did provide some insight into potential impacts on U.S. agriculture. Furthermore, the study did provide a useful literature review of agricultural studies at a national level concerning NAFTA.

Only section IV of the Burfisher et al. study addresses NAFTA's implications for the South. The study used parameter estimates from previous national studies as inputs into the USMP regional agricultural model, an internal USDA comparative static-spatial equilibrium model. That is, changes in imports and exports from other NAFTA studies were treated as exogenous inputs into their model. This implies treating trade with Mexico exogenously. What would happen to the analysis if Mexico had been included as one of the regions in the USMP model?

As stated earlier, this study was found lacking in addressing NAFTA implications on southern agriculture. Their USMP model excluded fruits and vegetables, and peanuts, which are important southern agricultural commodities. Their results show an increase in grain production the southeast. Yet the southeast is considered a marginal producer of grains and soybeans. Ignoring peanuts has critical implications on the results. For example, crop rotation is needed in peanut production. Many times a farmer may not earn a profit on his rotated crops, but the crop is planted due to the need for the rotation for peanuts. If peanut acreage drops due to NAFTA, such a drop will have an impact on other crop acreage. One may argue that peanuts are not widely grown in Mexico. However, if the U.S. farm bill is modified to meet NAFTA conditions, peanuts could be grown in Mexico.

In their modeling, the authors implicitly assume that the current economic relationships will still hold after the NAFTA agreement. This is a very strong assumption which could lead to opposite results. We

will use New Zealand's trade liberalization as an example. In 1984, New Zealand adopted a liberalization policy. Real agricultural prices declined in magnitude from 15 to 63 percent. One would expect a significant drop in agricultural production. However, New Zealand's aggregate agricultural supply has grown by 2 to 4 percent since 1984. The low producer price from trade liberalization does not simply cause a movement down the supply curve. Instead, it changes the whole incentive system, including factor prices. Before trade liberalization, there is often a large gap between efficient and less efficient farms. Free trade will speed up the adoption of new technology and lead to structural changes in the agricultural sector as efficient farmers expand to absorb the land, machinery, and workers released by the less efficient farmers moving out of the sector. No one can expect a simple economic model to capture the total effect of trade liberalization.

### SUMMARY AND CONCLUSION

A successful NAFTA would result in the world's largest trading zone. Agriculture presents both opportunities and challenges in concluding a NAFTA agreement. One must realize, however, that agricultural interests are among many voices listened to during the decision-making process.

There are many legitimate concerns over the potential effects of a NAFTA that must be investigated. The facts must be made available to decision makers during the negotiating process. It does little good, however, to express fears about the imminent demise of a particular industry or deterioration of the quality of life for some reason or another without a thorough investigation of the existing situation and/or likely outcomes. In many cases, as with the labor and environmental issues, to do so will overstate the case for alarm.

The bottom line concerning the impacts of NAFTA on southern agriculture will be how competitive are the southern commodities relative to the products from Mexico. Most of the impact studies have been from a national perspective. The Burfisher et al. study attempted to examine potential impacts on southern agriculture. However, they fell short. Besides the lack of southern commodity coverage, there seems to be an inconsistency in the results. Most of the major NAFTA studies show little national income increase for Mexico. Yet, some of the individual products like beef and vegetables show large increases based on increased income. We, as researchers, need to make sure our analyses are consistent and not just assume they are correct because the model said so.

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