

# Mexico, the weak link in Trump's campaign promises

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## Introduction

Since the Brexit referendum in the UK, whose result surprised us all, a large question looms in the minds of analysts, rulers and politicians: why did voters turn against projects that were, since World War II, the basis of international relations and of the post-World War II social pact?

Events such as Brexit, Trump's election, Le Pen's breakthrough in France and the establishment of right-wing governments in Poland and Hungary (in open defiance to the democratic principles of the European Union), though they are different in many respects, do have common features:

- the crises of the main political parties, abandoned by their constituencies,
- the rejection of political, intellectual and business establishments and the hegemonic economic doctrines of the last three decades (whether referred to as "globalization" or "economic neoliberalism"), and
- a reaction against refugees who are blamed for poverty, violence and the loss of identity.

These ideologies constitute the political phase of the economic crisis that erupted in 2008, the aftermath of which we are still experiencing: low growth, low productive investments, stagnation of productivity and real wages, concomitant with the decline in payments to labor in the functional distribution of income, not to mention the intensification of inequality in developed countries, or the Latin Americanization of the developed world (Palma, 2011). The current swing to the political right echoes the crisis of neoclassical macroeconomics, its general equilibrium models, and the methods of its teaching, which push economists and students away from real-life problems (Fullbrook, 2014; Puyana, 2015). Paradoxically, in recent years, in Latin America, the most unequal region in the world, inequality declined somewhat, although in Mexico it remains above the levels of 1980.

While the 2008 crisis called into question the fundamentals of economic theory over which the model of global growth had been sustained for the last three and a half decades, today we witness the crisis of liberal democracy and neo-liberal economics (Bauman, 2016), of the Social Democracy doctrine, the New Labor and waning The Third Way, as well as the fading out of the unrestricted support of globalization (Rodrik, 2017). Some foresee it as the end of the *Pax Americana*, or US hegemony established since the end of the Second World War and

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the world order that emerged thereafter (Roubini, 2017). For Trump, the costs of maintaining US imperialism are unacceptable; qualifying NATO as obsolete and its members as free riders and suggesting nuclear proliferation of Japan and Korea while keeping the USA “at the top of the pack” (Trump 2017) would be a sensible strategy, as it would reduce for the US the cost of defending these countries. In reality he is not an isolationist. He aims at controlling world order in his own terms: reinforcing the military power elements of the international security policy and weakening the elements of world peace, that inspired the II WW peace agreements and described in F.D. Roosevelt 1944 State of the Union Speech (Roosevelt, 1944), for whom security was not only preventing foreign aggressions but also avoiding any threats to economic, social and moral security, because a basic element of world peace is “a decent standard of living for all individual men and women and children in all Nations” (Roosevelt, 1944). Furthermore, for Roosevelt, peace depended on “...freedom from fear which is eternally linked with freedom from want” (Roosevelt, op cit.).

Exacerbated globalization has made clear the contradiction between democracy, which proclaims equality among all human beings and a capitalism that sanctions inequality, that inequality in wealth which supposedly guarantees investment and an economic growth and would end poverty. If property is the basis of freedom, the concentration of wealth impedes equality in freedom and in its exercise. One characteristic of neoclassical economics’ models and the policies it backs is its lack of support and even disapproval of democracy (Radford, 2016). The same author adds that the principle of efficient allocation under conditions of scarcity leads to rejecting every attempt of redistribution of income and wealth downwards. This rejection is consistent with Lucas (2004) for whom: “Of the tendencies that are harmful to sound economics, the most seductive, and in my opinion, the most poisonous, is to focus on questions of distribution”. All this led to the metamorphosis of economics, from a social science to a completely sanitized discipline that subordinates the state and society to the dictates of the market. In this way it came

“to reject all heresies, in any organized form, that is to say, anything that seems to threaten the sanctity of property, profits, appropriate tariff policy, or the balanced budget, or implied sympathy for unions, public property, or the poor” (Galbraith, 1974, p. 239).

Thus, adds the author,

“... converting economic theory into a non-political discipline – neoclassical theory destroyed, by the same process, its relation to the real world” (Galbraith, 1974, p. 240).

This distancing from the real world deprived economists and politicians from an understanding of the world and the will of the electorate.

Neoliberal economics and the Third Way political programmes, with its supply side model and its trickle down myths, intensified the innate tendency of capitalism toward concentration of wealth and, by eliminating the mechanisms of distribution and countervailing measures, widened the universe of losers, mainly workers, and reduced that of winners, and rewarded the latter with ever growing profits. This approach was part of the synthesis of Regan-Thatcher market liberalism and social individualism with social democracy distributive policies. The market was to be the means of tackling inequality and avoiding social disintegration. The motto of European Social Democratic parties and left of the centre parties

elsewhere was, “equal opportunities for all”, while pushing market oriented reforms in education and health. The crisis of 2008 evidenced the extent to which labor had been degraded, wages stalled and social mobility slowed, while services deteriorated and household debt prevented the deterioration of wages hurting even more. Fiscal discipline, or fiscal consolidation, evolved into a permanent austerity, enhancing the effects of the economic contraction, exacerbating inequality and deepening social discontent.

From the growing debate over the kind of government that Trump will lead, it seems that a nightmarish *Plot Against America* might be close to becoming a reality. For some, this is all about the rise to the White House of a determined leader, willing to affect all institutions, to “deconstruct the administrative state” (Bannon, 2017). For others, Trump is a right-wing populist actor in form and language, devoid of ideology. There seems to be no doubt of his authoritarian character and his determination to shake the system, creating conflicts with world leaders, both close and distant allies, and with the judiciary power, the media, members of his party, with women, ethnic minorities, and the intelligence authorities. He also fuels conflicts in the legislative branch between the two parties, given the Republican's willingness to accept all presidential initiatives and to excuse all his outbursts and the conflicts of interest that he defiantly ignores; there is no will to engage in bipartisan politics. So far it appears that he intends to make his proposals a reality, without abandoning his peculiar way of communicating with short, direct sentences that leave a wide margin for interpretation. In his rhetoric truth is not a requirement. How far he will go is not clear. Nor is it clear whether the checks and balances of the system will be able to set brakes on him or on specific policies. The failure to have the health care reform approved could signal that President Trump has to negotiate. It is scary that the most vocal opposition came from the far right of the Republican Party.

In an anachronistic view of reality, Trump's inaugural speech sketched an American society that, besieged and weakened by the harassment of internal and external enemies, has lost its dreams, military hegemony and middle class wealth. The schools deprive American children and youth of knowledge, while the infrastructure collapses and the factories are abandoned to rust. Migration, made up of criminals and terrorists, bleeds the nation and globalization destroys the social fabric by ruining the productive sector through the export of jobs. Since *protection leads to great prosperity*, the recipe to “make America Great Again” boils down to: *buying made in America, by American workers*. Such is the government formula for economic nationalism based on *alternative realism*, in which there is no room to talk about the crisis of 2008, nor about the ravages of financial deregulation and huge mergers, all of which lead to the dominance of large corporations and financial capital in the global economy and the consequent intensification of inequality.

Today, the US economy is growing at a faster rate than similarly developed ones. The number of people receiving unemployment insurance, 1.2 million in 2015, is 70% lower than in 1996, and lower than any time since 2008-2009. With only 4.5% “unemployment” as officially defined, it is close to full employment, judging also by the fact that wages have increased and are finally close to those in 2007. This reality calls into question what it means “to bring jobs back home”. More employment? Or higher productivity, with superior technology and robotization? Certainly, the first Labor Secretary candidate is neither a champion of the workers nor the defender of labor income, minimum wages or labor unions. Trump is staffing his economic cabinet with officials from Wall Street corporations and has gone in the direction of undoing previous reforms to the financial system, approved after the crisis of 2008. This indeed is not an agenda that favors workers and the middle classes.

## **Mexico: the greatest enemy for the United States**

Regardless of whether or not Trump can realize his *economic nationalism* agenda, it is clear that he intends to carry out the vision outlined in his inaugural speech: “Decisions in trade, immigration taxes, and foreign affairs will be taken only for the benefit of American workers and American families” (Trump, inaugural speech). The three areas selected by Trump comprise several topics that generate internal and external conflicts.

**Trade.** Trump proposes reducing the trade deficit, punishing exchange manipulation and retaliating against what he regards as unfair trade practices. The main points of the new government agenda were outlined in a draft of the “annual trade policy agenda” of the United States Trade Representative (Council of Foreign Relations, 2017). To protect national interests, Trump promised to bilaterally renegotiate multilateral or bilateral trade agreements, especially NAFTA, for him “the worst agreement ever signed”. He has signaled the end to the strategy of promoting economic integration as the way to prevent the resurgence of nationalist sentiments and violent conflicts of interest. That was the idea behind the construction of the European Union and of the mega trade projects: the TPP and the TTIP, which were instruments for consolidating USA geopolitical supremacy and restoring the political balance disrupted by the emergence of China as a main political and economic player. Furthermore, Trumps intends to circumvent the WTO, considered by him a medieval institution in which the tyranny of the majority made it impossible to impose a USA hegemony (Lamy, 2003). In effect, it seems Trump’s government may not be entirely against free trade, that it is looking to redefine trade rules so as to “defend national sovereignty over trade rules and to strictly enforce USA trade laws” (Council of Foreign Relations, 2017)

**Taxes** are part of the new trade policy. He has proposed a border adjustment tax, to compensate for the value added tax some countries implement. The VAT tax has been mistakenly described as an unfair tax on imports. Secondly, Trump has proposed a revision of corporate tax, to roll back the Dodd Frank Act and to amend the Volcker Rule. These measures would favor big capital and endanger economic stability as they recreate the conditions which lead to the 2008 crisis.

**Migration** is at the same time an economic issue due to its impact on US wages and, more importantly, a matter of national security, due to Trump’s belief that those who emigrate to the United States are terrorists, violent people, rapists or drug dealers. All this reverberates in the urgency to build the wall on the southern border and in the controversial executive order forbidding the migration from seven Muslim countries. Such criminalization of immigrants echoes the stance towards Afro-American and Latino communities.

In **international relations**, or national security, there are potential conflicts with China, an emerging power with the ability to challenge US supremacy in the Pacific. There are also conflicts regarding the Middle East, North Korea and Iran, but these are not mentioned by Trump as frequently as drug trafficking and the flow of immigrants from Mexico whom he describes as “gang members, drug lords and criminals” (Trump, 2017). President Trump’s national security team confirms the militaristic stance in his campaign, as do also the large increases for the military in the projected budget. In a telephone conversation with Mexico’s President Peña, Trump offered to dispatch US soldiers to contain Mexican “Bad hombres”. The offer was made out of President Trump’s perception that Mexican civil and military authorities are unable or unwilling to do their job, suggesting Mexican state is a failed state.

Mexico is thus identified as a unique threat to the security of the United States with regard to most of the issues Trump has emphasized in his speeches and summarized in Table 1.

**Table 1** Major threats to United States national security, wellbeing and prosperity, according to President Trump

	NAFTA		Central America	European Union	North Korea	ISLAMIC STATE			CHINA	JAPAN	NATO	Germany
	Mexico	Canada				IRAN	SYRIA	IRAQ				
FOREIGN AFFAIRS												
SECURITY	X				X	X	X	X	X	X	X	
TERRORISM	X					X	X	X				
MIGRATION	X		X			X	X	X	X			
HOME SECURITY												
DRUGS	X											
VIOLENCE	X				X	X	X	X				
EMPLOYMENT	X	X		x					X			
CURRENCY MANIPULATION									X	X		X
VALUE ADDED TAX	X	X	X	X					X	X		X
TRADE DEFICIT	X								X	X		X

Source: Own elaboration

### NAFTA, a trade deal not good for the USA. Really?

According to Trump, NAFTA is the most damaging trade agreement to US interests ever signed. It is a result of astute Mexican negotiators gaining commitments contrary to American's national interest. He repeatedly highlights Mexico as the exclusive culprit (with no mention of Canada) of having deceived the US during the negotiations. Nothing could be farther from the truth. This untruthful picture of the agreement calls for an objective description of the negotiating process and an illustration of the trajectory of the Mexican economy since NAFTA, to demonstrate that Trump's criticisms are ill intended and a pretext for imposing a new round of negotiations under conditions of extreme power.

Truth is far removed from the claim that US negotiators accepted under NAFTA concessions detrimental to US national interests. The negotiations for NAFTA between Mexico and the US were between two deeply asymmetrical countries:

- a) they had radically different levels of economic development and influence in the regional markets;
- b) there were large differences in the two country's economic models and their gaps with the implicit model of the agreement;
- c) they assigned different subjective utility to the non-agreement alternative; and
- d) there were major differences in their institution building processes and traditions.

By way of Alessina's (2006) war of attrition, the debt crisis (1982), was an opportunity to enforce very radical macroeconomic reforms, liberalizing the Mexican economy, privatizing public sector enterprises, even if these were not at the roots of the crisis. President Salinas (1988-1994) and the political and technocratic elite in power, considered the signing of a free trade agreement with the US as the instrument that would make irreversible the reforms and the modernization of both the Mexican economy and Mexican society. These reforms would increase stability and investor confidence, reassuring the inflows of capital needed to maintain

economic growth (Ros, 1994).<sup>1</sup> Therefore, for the Mexican government any other alternative to NAFTA had little value, and US negotiators understood this fact very clearly. Consequently, Mexico needed to offer larger concessions as a result of the lower subjective utility assigned to the Mexican “no agreement” alternative (Wonnacott, 1994). Mexico, the smaller economy and the weaker state, took the initiative to begin negotiations; it was the seeker, looking for a safe haven for its exports, and who was willing to negotiate reciprocity by opening its economy even further, after implementing a far-reaching unilateral liberalization to joining GATT (Drache, 2001).

What were the objectives and interests of the USA behind NAFTA? The largest country (in 1994 the US economy was 17 times larger than the Mexican economy) considered that there were no important changes in prices, nor gains from specialization due to marginal changes in tariffs, because practically all Mexican exports entered the USA almost free, with a 4% average tariff. USA exports to Mexico faced several times higher border and non-border trade barriers. So, the US was interested in extracting from Mexico, on top a drastic cut of all tariff and non-tariff trade barriers, all the concessions Mexico was willing to give. And Mexico was prepared to pay all the costs just to reach the agreement (Heillener, 1991). These included trade and non-trade and even non-economic incentives that could legitimize the United States signing the free trade agreement with Mexico and it was agreed, as early as 1990, that

“Mexico would not be treated as a developing country in the negotiations, meaning that it would not receive preferential treatment in matters such as transition periods for the elimination of tariffs” (Maxwell, 2000).

Mexico granted the USA larger tariff preferences than the ones it received, and in the first year of NAFTA, 50% of the tariff advantages in the US market were lost due to trade agreements the USA signed with countries with an export offer similar to Mexico's. Since the Mexican economy was more protected and regulated, Mexico had to make larger adjustments in the form of “side payments” as entry fees in the “new issues”, which were eventually included in the agreement, namely trade in services, regulations and protection of intellectual property rights and in foreign investment, considered the jewel of the crown won by the United States (Drache, 2001). NAFTA was also a pioneer in the Investor-state dispute settlement, later incorporated into the Uruguay Round within GATT, which allows private companies to sue states for policies purportedly damaging to their interests. Furthermore, Mexico wholly and hastily liberalized agriculture and accepted that the US maintained its Farm Bill stimulus, which would later create a dumping effect, or losses to Mexican farmers of up to \$13 billion dollars in constant 2005 prices (Wide, 2009), and it is calculated that no less than 5 million rural laborers abandoned this sector, while the imported content (completely from US origin) of the apparent consumption of Mexican staples (maize, beans, barley, rice, soy, among others) grew up to 50%, sometimes even close to 80%, which constitute a serious corrosion of food security. Moreover, Mexico absorbed all the costs of the institutional changes demanded by NAFTA and adopted the North American ones. Therefore, NAFTA did not entail any cost to the United States (Clinton, 1997). In this context, the increase in Mexican exports under NAFTA is more of a consequence of, on the one hand, the revaluation of the dollar

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<sup>1</sup> Baghawti expressed an abrasive opinion about the reasons and the urgency of the Mexican negotiators to reach the agreement: Mexican architects of NAFTA have a point of view that encouraged them to look at problems from the prism north of Rio Bravo. They were impressed by the US and wanted to emulate it. They said, “The US has done well. If we join with North America, all our problems will be over” (Author's translation), Bhagwati, Jagdish N., *El Financiero*, 22 de noviembre de 1999, p. 24.



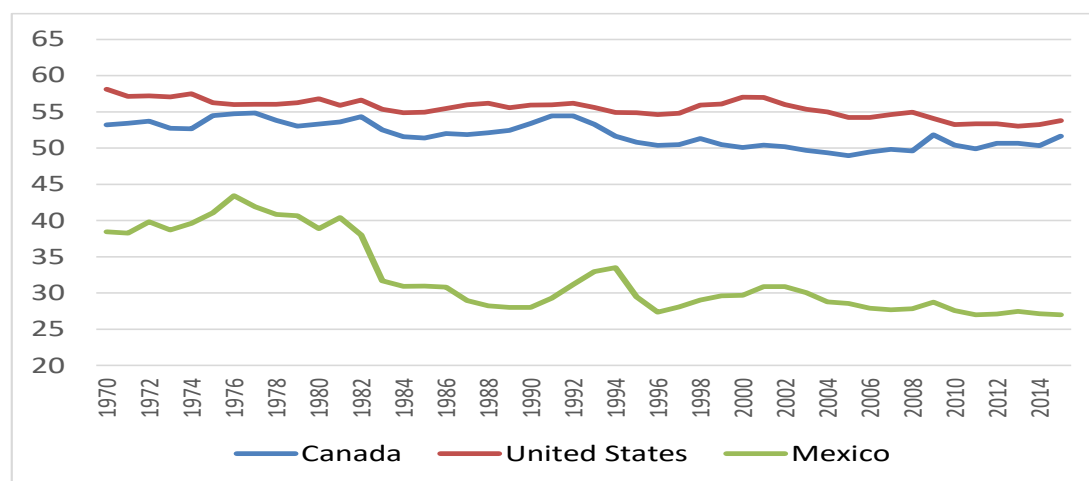
rather than the tariff reductions in favor of Mexico and, on the other, the increasing imported content of Mexican manufactured exports (USITC, 2003).

### The Mexican economy under NAFTA

Certainly, global economic liberalization went too far, especially regarding financial deregulation, large corporate mergers that nullify the market as well as the ever-growing transfer of national decision-making centers to supranational non-elected entities, of the policies that affected society, creating a sense of denationalization in everybody's daily life. All of this runs parallel to the increase in income gaps between and within countries, which accelerates mass migration and creates global humanitarian problems.

As noted, the primary objective in negotiating NAFTA was to prevent radical changes in the liberal model implemented since the mid-1980s, which amounts to not allowing society to modify economic policy through the electoral process. However, liberalization and the structural reforms eliminated or reduced state interventions on commodity, labor, and financial markets, but did not act to reduce the large concentration of capital or take measures to control its effects. From then until now, the trend of the Mexican economy has been the least favorable since the end of the 1940s, with the smallest GDP growth rates (close to 1.2% per year), with low labor and total factorial productivity, wage repression, declining tradable sectors in GDP and employment and the explosion of informal labor, which is today about 60% of the total labor force employed. If inflation has been controlled, it has been through internal devaluation and permanent fiscal austerity, amidst very low direct taxation (effective tax revenues represent 14% of GDP, excluding oil income). All this has led the economy to a low-growth equilibrium with low-income, limited aggregate demand and limited investments. This trajectory has implied a redistribution from labor towards capital, in which Mexican labor appears as the greater loser when compared to American labor (Figure 1). This change in the functional distribution of income occurred in most countries of the world, but only a few present a scale of change similar to Mexico's. Between 1980 and 2014, the share of wages fell by 11.5 percentage points, a decrease 2.3 and 3.8 times higher than the one in the United States and Canada, respectively, and the highest among OECD countries (OECD, 2016).

**Figure 1** Functional distribution of income in the United States, Canada and Mexico, 1970-2014



Source: Own calculations based on OECD.Stat2016, accessed 10 February 2017 at: <https://stats.oecd.org>

Mexican GDP expanded 3.7 times more than national wages, compared to 1.9 in the US.<sup>2</sup> This confirms that in both cases capital accumulated the profits and labor lost them, and which happened in Mexico to a greater extent. Before the reforms, between 1970 and 1980 and the supply model, the trend between the two countries was in the opposite direction. Mexican labor lost 0.5 points of income while that of the US lost three times more. The situation after the reforms in the Mexican manufacturing sector has been the same but magnified: labor productivity grew twice as much as real wages per worker. From this angle, the impoverishment of Mexican workers is greater than that of the Americans, thus, contrary to Mexico being responsible for the "... looting of other countries that make our products, steal our companies and our jobs" (Trump, 2017). The high presence of investments implies that Mexican workers handed over income in favor of external foreign capital, basically from American origin, the largest foreign investor in the country. This transfer of labor income to capital is a result of having converted the wage bill into the main element of international competitiveness, therefore a production cost to be reduced. Average real wages for 2015 represent 75% of those for 1980 and real minimum wages, only 35%. This fall in labor income has meant that average real wages in Mexican manufactures are lower than those in China and is ironically presented as an achievement in productive efficiency unleashed by liberalization and NAFTA, as explained by former Mexican Secretary of Economy and main NAFTA negotiator, Jaime Serra (Serra, 2014).

### **Who depends on whom?**

Another fictitious argument is that disadvantageous trade with Mexico, China and other countries made the US economy dependent on such partners.

The US economy is considerably less open than that of Mexico, Canada and China, and practically all OECD countries. The external index of an economy (the total trade of a country as percent of its GDP) shows the degree of openness of an economy to global competition, that is, how much of its product is imported and exported. The United States appears as a relatively self-contained economy with relatively limited penetration of its domestic market by imports and comparatively limited exports. Mexico and Canada are the most open and China is relatively closed, as shown in Table 2. With an external coefficient of 72.8% of GDP (37.5% imports and 35.4% of exports), the Mexican economy is 2.6 times more open to competition in domestic and external markets, than the American one. Even Canada appears less open than Mexico. So it is hard to understand how the US could be dependent on Mexico or China. Whereas Mexico depends much more on trade, for the US the domestic demand is more significant.

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<sup>2</sup> Mexico was, amongst the 36 countries listed in the OCDE data base, the country with the biggest labour losses in primary distribution of income, after Ireland and Portugal and closely followed by the United Kingdom which occupied fourth place.



**Table 2** Canada, Mexico and the USA: External Coefficient of their economies, 1990-2015, as % of GDP

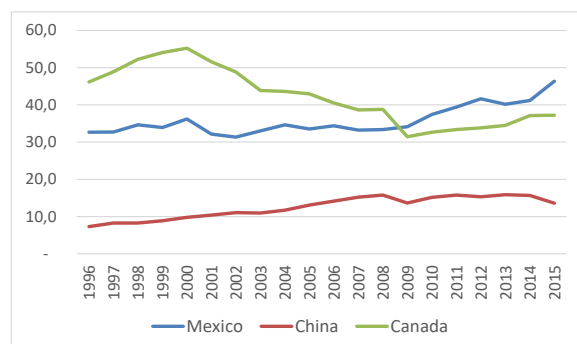
	Canada		China		Mexico		United States	
	1990	2015	1990	2015	1990	2015	1990	2015
Imports	24.9	33.8	10.7	18.6	19.7	37.5	10.5	15.4
Exports	25.1	31.5	14.0	22.1	18.6	35.4	9.2	12.6
Total	50.0	65.4	24.7	40.7	38.3	72.8	19.8	28.0
Trade Balance	0.2	-2.3	3.4	3.5	-1.1	-2.1	-1.3	-2.9
Average	1.1		1.7		-0.5		-1.6	

Source: Own calculations based on World Bank; WDI, 2016

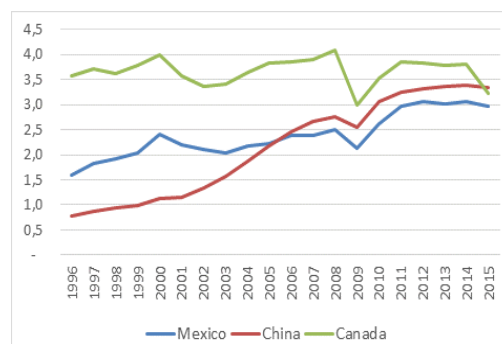
In the context of the aforementioned trade openness, we define dependence as the weight of reciprocal trade in the GDP of each participating country. As shown in Figure 2, about 3.5% of the GDP in the US is linked to trade with China and about 3% to trade with Canada and Mexico (Panel B). The dependence from the opposite side (Panel A) is surprising, if not alarming. 46.4% of Mexican GDP depends on trade with the US, a dependency 15.7 times more than the one US has from Mexico. In contrast, China's dependence with respect to US trade is almost three times lower than that of Mexico, while the Canadian is 10 points below. With these parameters in mind it is hard to accept the claim that the US depends on Mexico. On the contrary, what stands out is the asymmetrical dependence of Mexico on USA economy

**Figure 2** Dependency of the economies of Mexico, Canada, China and the United States, as % of GDP, 1996-2015

**Panel A**  
From USA regarding Mexico, China and Canada



**Panel B**  
From Mexico, Canada and China regarding USA



Source: Own calculations based on World Bank, WDI 2016

Second, the diversification of markets of origin and destination of exchange moderates US commercial dependence. Only three countries account each for more than 10% of total imports (China 21%, Canada 13% and Mexico 12%) and exports (Canada 18%, Mexico 15% and China 7.3%). Contrasting these proportions with Mexico's, the United States is the primary destination of 85% of its external sales and the origin of 40% of imports. Note also the imbalance in trade with China, which accounts for 21% of USA imports and only 7.3% of US exports. This asymmetry is most noticeable considering that the Chinese economy is 7.4 times larger than the Mexican and could capture a larger proportion of US exports. In 2016, the trade deficit of the US with China was 18 times greater than the Mexican one, reaching up

to 319.3 billion dollars. In this context, the Mexican trade surplus with the United States grew from between 18 to 58 billion dollars between 1996 and 2016, a trend explained by the automotive sector, which accounted for 79.3% of the imbalance, followed by electronics. Mexican total sales of automobiles and auto parts account for 26% of total US automotive imports, but only 2.3% of its total imports.

**Table 3** Percentage share of Mexico and China in United States trade, 2000-2016

	US Imports From Mexico	US Imports From China	US Exports To Mexico	US Exports To China
2000	11.17	8.22	14.32	12.08
2004	10.61	13.38	13.59	4.22
2008	10.27	16.06	11.75	5.42
2010	12.02	19.08	12.79	7.19
2011	11.91	18.09	13.40	7.02
2012	12.20	18.71	13.99	7.15
2013	12.37	19.42	14.32	7.71
2014	12.53	19.88	14.83	7.63
2015	13.12	21.50	15.71	7.72
2016	13.50	21.12	15.96	7.85
China/Mexico		1.6		0.5

Like no other sector, automobile manufacturing reflects the problems of global value chains: approximately 40% of the exported value are inputs, components and parts, imported from the US companies. An additional 20% is imported from Japanese, Korean and European USA subsidiaries. Mexican manufacturing exports are intensive in imported value added, which varies in the different branches, Table 4.

**Table 4** What is exported? Import content in Mexican and Chinese exports

SECTORS	MEXICO		CHINA		Difference (MX-CH)	
	1995	2011	1995	2011	1995	2011
1 Agriculture, Forestry, Fisheries	8.51	14.54	5.81	7.50	2.70	7.04
2 Mining and extraction	4.50	5.72	9.33	14.87	-4.83	-9.15
3 Foods, beverages and tobacco	14.34	18.50	8.38	11.27	5.96	7.23
4 Textiles and products	21.02	25.85	17.84	14.68	3.18	11.16
5 Leather	16.33	21.02	18.92	14.73	-2.59	6.29
6 Wood and products	12.47	14.96	16.14	16.86	-3.67	-1.89
7 Paper, pulp and printing	18.69	21.16	14.44	18.77	4.25	2.39
8 Coke, refined oil products, nuclear fuel	6.34	8.03	20.68	43.55	-14.34	-35.52
9 Chemicals and products	12.93	16.25	15.35	24.36	-2.42	-8.11
10 Plastics and rubber	24.76	32.29	18.05	23.38	6.71	8.91
11 Other non metallic minerals	10.44	12.56	10.87	16.92	-0.43	-4.36
12 Basic metals	23.37	27.38	15.52	27.32	7.85	0.06
13 Machinery	30.68	34.52	14.85	23.46	15.83	11.05
14 Electric and optical equipment	54.40	61.31	22.25	30.37	32.15	30.94
15 Transportation equipment	34.84	36.79	16.32	22.92	18.52	13.86
16 Manufacturing and recycling	28.93	33.34	15.47	14.77	13.46	18.56

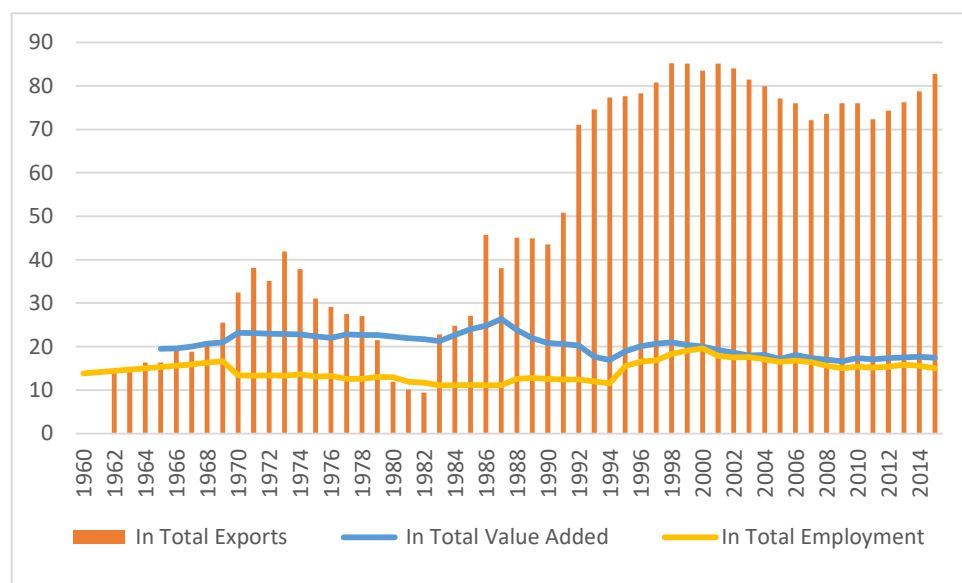
Source: Own elaboration based on World Input Output Database (WIOD) matrices.

Exports with highest imported content are precisely those activities with greater technological content and greater presence of foreign investors. Those are precisely the activities in which the Mexican trade surplus with the US is higher: electrical, electronic and optical equipment,

transportation, machinery. In contrast, Chinese external sales contain less imported content, except for some commodity-intensive products.

The highly imported content of Mexican manufacturing exports implies an intensified propensity to import and with more severe external restrictions intensified: for each point of increase in GDP, the imports increased by almost 5%. The final effect is a weakening of the link between growth in manufacturing exports, sectoral and total GDP, and employment (Puyana, 2015) a trajectory evident from Figure 3.

**Figure 3** Share of manufactures in total GDP and exports, 1960-2014



Source: World Bank, WDI, 2016, accessed February 18 2017. The decline in GDP manufacturing is associated with a smaller but significant decrease in employment starting in the year 2000. This is the reason why sector productivity has not grown as would be expected by the progress of the sectors' openness, similar to that of total GDP (Romero, 2014). The deindustrialization of the Mexican economy is real, despite its volume of exports.

The trade of manufactured goods between Mexico and the US is vertical intra-industry exchange, in the sense that the two countries exchange goods classified in the same tariff category, which are differentiated by quality and intensity of factors: Mexico exports to the US goods with lower economies of scale and low technological content for lower income markets, and imports the same goods but of more technological sophistication and with higher prices. The effects would be similar to those of inter-industry, Heckscher-Ohlin-type trade (Puyana, 2003). With these considerations, taxes on companies that produce in Mexico and export to the US, either in the form of a Border Adjustment Tax or import taxes, would raise prices in a differentiated manner, punishing mostly consumers in the lower income group. Mexican manufacturing production is found in the most labor-intensive fragments of the production process of the global value chains and represents a tiny share of the value of each product. Therefore, its return to the US will not represent a huge increase in jobs creation but could imply some inflation, especially when considering it parallel to a large plan of public investment.

## What to do?

Two facts look certain: first, Trump and his team will follow through on campaign promises; second, the US presidency is advocating economic nationalism aiming to protect USA production and employment through the relocation of global value chains.<sup>3</sup> This change of focus has left a void for the Mexican leadership, be it in the public or the business sector. The American president pretends to legitimize chauvinist nationalism, presenting it as economic protectionism in defense of employment and reasserting that previous governments forgot to defend the national interest. As if the USA were a developing, commodity-dependent country, Trump says that the US suffers from the effects of an “impoverishing trade” which de-industrialized, turning the country to a low-value manufactures assembling economy. De-industrialization is not a phenomena resulting from trade, but from a higher degree of development, higher per capita income and the consequent change in the structure of demand. Trump’s ideological positions which guide the formulation of the trade strategy (USTR, 2017) emerge from the false premise,

“... that if other Nations are encouraged to raise their standards of living, our own American standard of living must of necessity be depressed” (Roosevelt, op cit.).

So Mexican society received with astonishment both the change of the USA economic policy and the repeated aggressions of Trump the candidate and the president, and refuses to accept them. Notwithstanding the grievances, President Peña invited Trump and gave him the president’s platform. Today, a month after his inauguration, the public rejection of the threats of the USA president and the lukewarm Mexican official answers, resonates stronger by the day. The vast majority of Mexicans reject the idea that defense of national dignity and national sovereignty should be interpreted as support for the government or the major political parties or those responsible for the deterioration of the living conditions of the population. The demand for clearer and more energetic attitudes and responses is growing and pushing the government to reject any kind of threats and intimidations and to suggest it would suspend cooperation in migration, drug trafficking and terrorism even to abandon the NAFTA negotiations table if the USA insists in imposing taxes on Mexican exports and on USA investments in Mexico.

Since the US presidential primaries, Mexico has been living in an environment of uncertainty, declining growth and sharp devaluation of the Peso. Different proposals have emerged to resist the crises, which show the deep division in Mexican society. There is unanimity on two issues: first, not to pay for the wall, which is an act of antagonism and xenophobia irreconcilable with the deepening economic integration and ongoing collaboration on security and drug trafficking issues; second, to defend the rights of deported Mexicans, offer them services and assistance of all types, once they arrive in the country, and oppose any measure to tax or to freeze Mexican workers’ remittances. So much for the consensus.

Dissent revolves around whether or not to renegotiate NAFTA or whether to take Trump’s policies towards Mexico as the opportunity to revise the development model. In any case, the desirability of diversifying external markets is emphasized as well as reintegrating productive chains and strengthening the internal market, which are at odds with NAFTA. Past economic trends, employment wages, inequality and poverty reinforce the need for changes in

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<sup>3</sup> “National Trade Policy Agenda for 2017”, presented to Congress in March 2017.

economic policies, with or without NAFTA. Table 5, which summarizes and groups the views of diverging representative sectors of the society.<sup>4</sup>

**Table 5** Views of Mexican society in the face of changes in US policy towards Mexico and NAFTA

Sector Reaction or proposal	Renegotiate and Defend free trade			No to a NAFTA renegotiation		To Transform Current Economic Model					TOTAL
	To Negotiate NAFTA	Defending free trade	Rejecting border tax	Not renegotiate NAFTA without mutual benefits	Abandon NAFTA and opt WTO	Diversify markets	Strengthen internal market	Decrease taxes	Protect Agriculture	Industrial policy, infrastru.	
Gobierno	11	9	9	6	3	9	1	1	2	1	52
Actores políticos	8	10	1	4	10	9	2	2	1	1	48
Empresarios	17	5	1	3	4	17	4	3	8	5	67
Sindicatos, movimientos sociales y ONGs	1	0	0	2	5	0	1	0	3	1	13
Academia	6	3	2	2	3	14	9	1	4	4	48
<b>TOTAL</b>	<b>43</b>	<b>27</b>	<b>13</b>	<b>17</b>	<b>25</b>	<b>49</b>	<b>17</b>	<b>7</b>	<b>18</b>	<b>12</b>	<b>228</b>
Actor responses, absolute values	83			42		73			30		228
Actor responses, porcentual shares	36,4			18,42		32,02			13,2		100

Source: Author's elaboration.

While 19% of persons prefer to renegotiate NAFTA, many government and business actors (27 or the 11%) opt to “modernize”<sup>5</sup> NAFTA, and to preserve the free trade ideology that sustains the supply side economic model. They also reject import and export taxes, domestic and foreign. All-in-all pro free trade position comprises 36.4% of answers. This position stems from the premise that Mexico is an important part of the NAFTA region, a fully integrated production area that exports to the world. In that context, any protectionist measure would weaken the region's competitiveness in the world. Therefore, they propose to seize the opportunity to deepen liberalization and expand NAFTA to areas not initially included, such as communications, the energy sector, as well as to extend agreements to the electronic sector, intellectual property, including anti-corruption rules. To strengthen its preferences, the government integrated a group of experts to define the negotiating strategy and lead the negotiations, with the same economists who negotiated the NAFTA in the first place. The group has already stated the main tenets. First, to educate society in the benefits of NAFTA, which has already realized to a greater extent than expected its foremost initial goal: to expand exports. Second, to reiterate that the greatest beneficiaries of the agreement are the consumers, without mentioning how these are first and foremost also producers and workers. Third, to extend NAFTA including themes agreed for the TPP and also discussed in the TTIP, eliminating all restriction to trade and to capital. It is still in doubt whether these proposals to “modernize” NAFTA would not intensify the wage repression experienced by the Mexican labor sector since the reforms and NAFTA, and as some critics of TTP and TTIP suggest (Bivens, 2015; Felbermayr, et al., 2013).

The business sector, with its 67 responses appears divided. While some 10% of them propose to negotiate NAFTA, around 16% takes a moderate stance, either rejecting the negotiations in the face of uncertainty and fear that the results will be negative or seeking to expand markets, strengthen the domestic market and to redefine sectoral policies, industrial, agricultural, energy and technology policies.

<sup>4</sup> These are the opinions expressed in articles from the most widely circulated daily and weekly newspapers and in specialized journals, between September 15, 2016 and March 15, 2017. They include 175 notes and articles of some 228 people coming from government, political leaders, representatives of unions, NGOs, academics and entrepreneurs.

<sup>5</sup> Modernize is the euphemism for renegotiate, since so many people rejects the idea of negotiations.

A diverse group (academia, politicians, and unionists) advocates renegotiating the agreement on condition that it is beneficial to the country and under certain circumstances, namely not building the wall, not imposing border adjustment taxes or any other taxes. To reach positive agreement for Mexico, or if the US decides to abandon NAFTA, the preferred alternative is to go the WTO. Finally, there is a relevant group of political, intellectual and academia actors, proposing not to negotiate, abandon NAFTA and go to the WTO.

A consensus emerges, with 45% support for the need to reform the current economic model, with or without a renegotiation of NAFTA, with industrial policies that reintegrate productive chains, generate added value and national employment, as well as provide protection to agriculture, all with a view to strengthening the market. Finally, the diversification of the destination of export markets gains strength. Some of these proposals would clash with government preferences, but echo Trump's policy. Almost all of these priorities contradict the liberal NAFTA economic policy model.

It is our opinion that Mexico must seize the current opportunity, redefine the policies outlined in NAFTA, and undo the mistakes made in the initial NAFTA negotiations and the structural reforms of the mid-1980s. The answer to this external shock, induced by the stubborn will to change the norms that had governed bilateral relations for the last 24 years, could be the opportunity for a serious reform to the model of national development. There will be losers and winners, it is true. Depending on the players who would lead the changes it would be expected that the balance will not be adverse to labour as it was for the last 30 years.

With oil running out and the US restricting investments and imports of goods made in Mexico, and repressing remittances, the country would not have the resources to invest, accumulate capital and expand production. As in world crises and wars, it is necessary to change course, reindustrialize Mexico and strengthen agriculture.

Following are some premises for change, emerging from our own recollection and reading public opinion in Table 5:

- i) To figure first the direction of the country and its economy and, in this context, establish the space of relations with the US and the rest of the world;
- ii) The trajectory of the national economy must rest on sustained and sustainable growth, the generation of more and better jobs to reverse the decline of labor in the functional distribution of income, and reduce inequality;
- iii) Protect agriculture, to ensure food security, as the US, EU, Japan and China already do, reversing the imported content of consumption of maize, beans, rice, soybeans and other primary food products;
- iv) An agricultural policy with increases in yields and productivity, not oriented exclusively to exports, but to ensure food security and supply inputs to manufactures;
- v) To launch an active industrial policy that incorporates labor and added value, promotes research and, in reaction to the border tax and the import tax, a tariff policy that eliminates negative effective protection and protects national value added;
- vi) To structure an energy policy for development, in which the oil that still remains and is to be found becomes a development factor and integrating clean and alternative energies;



- vii) To reject elements accepted in the TPP, either as a negotiating strategy with the US or as a policy to expand Mexico's export markets, in the economic restructuring process. That would only aggravate the structural problems generated by the way NAFTA was negotiated. They will deepen the now questioned denationalization of the economy;
- viii) In this context, the academy, unfastened from political and economic power centers, must study and explain reality and propose objective interpretations and lines of action.

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