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# Post-NAFTA North America

## Reshaping the Economic and Political Governance of a Changing Region

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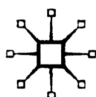

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*To Madeleine Bondy, whose love keeps me breathing, walking and exploring*

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# Foreword

Some continue to debate the North American Free Trade Agreement (NAFTA), which came into force in 1994 and created the largest market in gross product in the world. Advocates view it as benefiting all three countries, and critics, as costly, but that debate should be over. The far more important question today concerns the agenda that has emerged in North America since NAFTA and as a result of its impact on Canada, Mexico, and the United States in the past fourteen years. The three governments of North America have failed to address this question. Fortunately, Isidro Morales has done so in this imaginative book.

To secure its approval, NAFTA's advocates promised more than it could deliver, but NAFTA did succeed in what it was designed to do. Its stated goal was to reduce and eventually eliminate trade and investment barriers among the three countries of North America. Although there remain some problems of compliance on trucking and a few agricultural products, the goal of freer trade has been largely accomplished, and the results are indisputable. Trade has tripled, and foreign investment has quintupled, accelerating the economic and social integration of the three countries. The three segmented national markets have been gradually transformed into a continental market – large though not exactly seamless.

The enlargement of three national markets into a continental one created new opportunities and problems, and this is the North American agenda of the future. The three economies are synchronizing, but the three governments have not yet considered ways to coordinate their macroeconomic policies. Trade has tripled, and 75 per cent of that trade is on roads, but the three governments have not yet considered, let alone proposed, a plan to invest in infrastructure and build new highways and intermodal transportation connections. Old problems like undocumented immigration or inadequate investment in long-term energy have been exacerbated by greater societal and economic integration and weaker governance.

The reasons for such little progress on the new North American agenda are manifold. First, the three governments have **failed to project the importance** of North America to their constituencies. Second, all three, but particularly the United States, have **failed to organize their governments** to address this new agenda in a constructive and

far-sighted way. Each issue requires a trade-off between specific, sub-national interests and the broader interest in North America, and if these issues are not pressed up to the heads of government with real options, the Congress or lower levels of the bureaucracies will always resolve them in a parochial way. Third, the three governments have **failed to create trilateral institutions and procedures** that would allow the three countries to propose a continental agenda and address problems in a trilateral way. As a result, when the three leaders meet in summits, as they have been doing, their agenda is bilateral (US-Mexico and US-Canada). The continental agenda is absent except for a photo-opportunity among the three amigos.

This failure of leadership has meant that the 'North American advantage' has eroded. Indeed, transaction costs have soared between the three countries of North America above the tariffs that were eliminated as a result of the free trade agreement. Some of these costs are due to security concerns that stem from 9/11, but most are related to protectionism – e.g., on trucks – and to the failure to tackle new barriers to trade. A North American car, assembled with parts from all three countries, has to cross the borders many times with significant delays and costs each time, particularly because few trucks from Mexico are permitted into the United States. In contrast, a container from China only has to cross the border once. The 'shallow integration' of NAFTA produced a 9.8 per cent increase in trade among the three between 1994 and 2000, but that was insufficient to compete with China in the 21st century. Since 2000, the rate of growth in trade has slowed to 3 per cent. New approaches are needed to recapture the North American advantage.

So, in brief, it is vitally important to focus on what has been learned from NAFTA, how it has changed the three countries, and what needs to be done to take full advantage of proximity. Morales has re-examined the North American space, the new agenda, and the architecture to address the security, economic, and cultural challenge. This is part of a new generation of books on the future continental agenda. And it comes none too soon.

Robert A. Pastor is Professor of International Relations and Director of the Center for North American Studies at American University in Washington, D.C. He is the author of *Toward a North American Community: Lessons for the Old World for the New* (Washington, D.C.: Institute for International Economics, 2001).

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I would also like to thank the publishers of my previous work for giving me their permission to reproduce some material already appearing in their prestigious books and journals. Chapter 2 draws from previous material published in my book chapter: 'NAFTA: The Governance of Economic Openness', in Isidro Morales, Guillermo de los Reyes, Paul Rich (eds), (1999) *Civil Society and Democratization*, pp. 35–65 (Thousands Oaks: Sage Publications). Chapter 3 is a more mature version of my article published as 'NAFTA: The institutionalisation of economic openness and the configuration of Mexican geo-economic spaces', *Third World Quarterly*, 1999, Vol. 20, No. 5, pp. 971–993. The analysis of energy issues developed in Chapters 4 and 6 were previously explored in the following articles: 'The New Strategic Positioning of Canada within North America: The Energy Factor', in Andrew F. Cooper, and Dane Rowlands (2006) *Canada Among Nations. 2006. Minorities and Priorities*, pp. 269–291 (Montréal and Kingston: McGill-Queen's University Press) and 'Mexico's Energy Policy Options in North America's Continental Energy Markets', published electronically by the Center for North American Studies at American University (http://www. american.edu/ia/cnas/publications.html). I thank all these publishers for granting me their permission to reproduce and use part of the material already appearing in their respective publications.

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# List of Abbreviations

| | |
|---|---|
| AAGR | Annual Average Growth Rate |
| AC | Andean Community |
| AD | Antidumping |
| ADSM | Alternative Dispute Settlement Mechanism |
| ASEAN | Association of South East Asian Nations |
| BAPU | Binational Alien Protection Unit |
| Bb | Billion Barrels |
| BPG | Binational Planning Group |
| CA | Central America |
| CACM | Central American Common Market |
| CARICOM | Caribbean Common Market |
| CBI | Caribbean Basin Initiative |
| CBP | Customs and Border Protection |
| CBTPA | Caribbean Basin Trade Partnership Act |
| CCCE | Canadian Council of Chief Executives |
| CEO | Chief Executive Officer |
| CET | Common External Tariff |
| CFE | Comisión Federal de Electricidad |
| CFLI | Coalition for Fair Lumber Imports |
| CUSFTA | Canada–US Free Trade Agreement |
| CVD | Countervailing duties |
| DEA | Drug Enforcement Administration |
| DHS | Department of Homeland Security |
| DOC | United States Department of Commerce |
| DR | Dominican Republic |
| DR-CAFTA | Dominican Republic and Central America Free Trade Agreement with the United States |
| DSB | Dispute Settlement Body |
| ECC | Extraordinary Challenge Committee |
| EFTA | European Free Trade Area |
| EIA | Energy Information Administration |
| EPA | Energy Policy Act |
| EU | European Union |
| FAST | Free and Safe Trade |
| FBI | Federal Bureau of Intelligence |
| FDI | Foreign Direct Investment |

| | |
|---|---|
| FERC | Federal Energy Regulatory Commission |
| FFMLN | Frente Farabundo Martí de Liberación Nacional |
| FTA | Free Trade Area |
| FTAA | Free Trade Area of the Americas |
| FTC | Free Trade Commission |
| GATS | General Agreement on Trade in Services |
| GATT | General Agreement on Tariffs and Trade |
| GDP | Gross Domestic Product |
| ICE | Immigration and Customs Enforcement |
| ICSID | International Center for the Settlement of Investment Disputes |
| IDB | Inter-American Development Bank |
| ILO | International Labor Organization |
| IMF | International Monetary Fund |
| INA | Immigration and Naturalization Act |
| INEGI | Instituto Nacional de Geografía, Estadística e Informática |
| INS | Immigration and Naturalization Service |
| ITAC | Integrated Threat Assessment Center |
| ITC | United States International Trade Commission |
| LAC | Latin American and Caribbean or Latin America and the Caribbean |
| LFC | Luz y Fuerza del Centro |
| LNG | Liquefied Natural Gas |
| Mb | Million barrels |
| MCFD | Million cubic feet daily |
| MDF | Mexican Development Fund |
| MEA | Monetary Enforcement Award |
| MERCOSUR | Mercado Común del Sur (Common Market of the South) |
| MFN | Most Favored Nation |
| MNC | Multinational Company |
| MOFA | Ministry of Foreign Affairs |
| MOU | Memorandum of Understanding |
| MSC | Multiple service contract |
| MW | Megawatts |
| NAAT | North American Aviation Trilateral |
| NAC | North American Commission |
| NADB | North American Development Bank |
| NAEF | North American Energy Fund |
| NAEWG | North American Energy Working Group |
| NAFTA | North America Free Trade Agreement |

| | |
|---|---|
| NAIF | North American Investment Fund |
| NATO | North Atlantic Treaty Organization |
| NEB | National Energy Board |
| NERC | North American Electricity Reliability Council |
| NERO | North American Electricity Reliability Organization |
| NGO | Non-Governmental Organization |
| NORAD | North American Aerospace Defense Command |
| NSP | National Strategic Plan |
| OASISS | Operation Against Smugglers Initiative on Safety and Security |
| OPEC | Organization of Petroleum Exporting Countries |
| OTM | Other than Mexican |
| PAN | Partido Acción Nacional |
| PEMEX | Petróleos Mexicanos |
| PP | Partnership for Prosperity |
| PPP | Plan Puebla-Panamá |
| PRD | Partido de la Revolución Democrática |
| PRI | Partido Revolucionario Institucional |
| PSEPC | Public Safety and Emergency Preparedness Canada |
| REO | Regional electricity organization |
| SIC | Special Interest Countries |
| SENTRI | Secure Electronic Network for Travelers Rapid Inspection |
| SPP | Security and Prosperity Partnership |
| SST | State Sponsors of Terrorism |
| TPA | Trade Promotion Authority |
| TRIMS | Trade Related Investment Measures |
| TRIPS | Trade Related Intellectual Property Rights |
| UNCITRAL | United Nations Commission on International Trade Law Arbitration Rules |
| UNCTAD | United Nations Conference on Trade and Development |
| US | United States |
| USBP | United States Border Patrol |
| USNORTHCOM | United States Northern Command |
| USTR | United States Trade Representative |
| WB | World Bank |
| WCSB | Western Canadian Sedimentary Basin |
| WMD | Weapons of mass destruction |
| WTO | World Trade Organization |

# Introduction
# Post-NAFTA North America: Reshaping the Economic and Political Governance of a Changing Region

Since the North American Free Trade Agreement (NAFTA) came into ruling, it has been perceived by their respective political elites and public opinion, at least in Canada and Mexico, as a mechanism geared to the integration of the three economies. Canadians talk about formalizing, through NAFTA, the continentalization of their economy, that is, the deepening of their integration south of the border rather than diversifying the economic links with other countries. The continentalization process aimed to raise Canadian productivity and living standards in Canada. Mexicans talk, since 1992, when negotiations for a NAFTA were completed, of renewing their path towards economic growth thanks to north-bound integration. NAFTA locked in an outward-oriented economic model that substituted the state-centered import-substitution strategy that prevailed in Mexico after World War II until the mid eighties.

What this book argues is that NAFTA was conceived differently in the US; at least differently than it was conceived either in Canada or in Mexico. For Americans NAFTA was not conceived as an integration mechanism, but rather as a trade policy device aiming to reinforce 'export-enhancing' policies that Washington has been pushing, at both unilateral and multilateral levels, since the mid seventies. NAFTA was nested as a middle ground between US multilateral positions pursued within the General Agreement on Trade and Tariffs (GATT), and later the

World Trade Organization (WTO), and unilateral trade measures debated and adopted by US Congress. Between these two options, the so-called 'regional' one emerged in the mid eighties, when the US and Canada entered into free trade talks that eventually spilled over to include Mexico.

My second argument is that NAFTA is more than a simple trade regime. It is mainly a disciplinary machinery which partners abide by through arbitrated litigation or unilateral sanctions. Since it was nested as a third front on US trade diplomacy, it embodies the same values, principled mechanisms and disciplinary coverage defended by US elites on both the multilateral and unilateral fronts at the time. NAFTA conveys corporate-led and market-oriented values, all of them present in Washington's agenda under ongoing trade negotiations at the WTO. NAFTA also aims to 'level the playing field', a major trade policy goal pursued by Washington on the unilateral front. By this, Washington understood that if trade partners wanted to benefit from 'free' access to the US market, trade partners had to abide by and play by the new rules of the game promoted and/or negotiated by Washington on both unilateral and multilateral fronts.

To level the playing field meant not only to liberalize markets according to the standards of American 'openness', but also to remove non-trade barriers, or what were then called 'structural impediments' to private businesses. Most of the time this has meant to limit state intervention in the economy, either on productive, trade or investment matters. This explains why NAFTA rather conveys a disciplinary mechanism, the goal of which is to induce institutional convergence according to the American 'benchmark'; a standard of economic governance that was crafted since the emergence of the 'Washington consensus' and the neoliberal wave that has shaped key American public policies since the 1980s. The target of this 'disciplinary' mechanism is not markets, but states. NAFTA values, principled mechanisms and institutions aim to 'discipline' the state vis-à-vis markets, firms, and their own legislation in specific fields such as labor and environmental standards. The enforcement of this disciplinary ruling is accomplished through panel arbitration and/or economic retaliation. Since this disciplinary mechanism was nested in parallel to the initiation of the Uruguay Round negotiations, the scope and coverage of NAFTA reflects well the new US trade agenda of the time.

These two arguments are developed in the first two chapters of this book, which at the same time embody the first part of my work. Chapter 1 aims to explain NAFTA in the broader context of economic globalization

and the consolidation and/or emergence of regional trade regimes during the past 25 years. It traces the 'nesting' of the third track approach in US trade diplomacy, and suggests that regional disciplinary governance through institutional convergence to a market- and corporate-led agenda has become a major soft power device for the US, for transforming the state-market relations of its major trade partners. Chapter 2 analyzes in detail the major components of this disciplinary machinery targeting state involvement vis-à-vis markets and firms. It also highlights its own limits and possible evolution.

The following two chapters constitute the second part of the book, focusing on the reshaping of the economic and social space of North America. Thus, Chapter 3 opens and develops a new argument. Although NAFTA was mainly conceived as a disciplinary policy mechanism by the US, it has entailed policy shocks both north and south of the US. These policy shocks have prompted firms and market actors to adapt their production and exchange strategies within the enlarged market. This chapter thus explores how trade and investment patterns have evolved at the continental level and the key role played by US-based multinational firms. Chapter 3 also explores how these new cross-border patterns of trade and investments have consolidated a so-called 'continental' hub in northern North America, and at least two major cross-border 'spokes' along the US–Mexican border. The chapter explores the functionality and consequences of this emerging North-American spatiality in geo-economical terms. It confirms the consolidation of a resource-based economy in the north, with complex intra-industry connections in key high-tech sectors, and a space of manufacturing relocation in the south, still linked to cheap labor processing activities clustered around *maquilas*. It finally highlights the eventual emergence of a southern 'periphery', featuring non-competitive industries (mainly in agriculture) fueling migratory flows.

Chapter 4 of this book analyzes Mexico's 'post-NAFTA' evolving agenda since Mexico became the first country to articulate, at the highest political level, a two-tier program, the backbone of which was the formalization of cross-border labor markets between Mexico and the US, and the need to re-launch development policies outside the formula of the 'Washington consensus'. This chapter explores why Mexico failed to advance this agenda and got instead the erection of a 'barricaded' border aimed to deter growing flows of illegal workers, and a bilateral 'partnership for prosperity' deal, one of whose major goals became the targeting of migrants' remittances for 'development' purposes. Since the reduction of illegal migration and the need to strengthen development

policies remain Mexico's key priorities in its new geo-economic positioning, a last section of this chapter also reviews the domestic debate between oil politics and development policies.

The remaining two chapters constitute the third part of this book, centered on the new geopolitical dimension of North America, mainly after the terrorist attacks in New York and the Pentagon, in September 2001. In this part I argue that the 'war on terror' declared by George W. Bush, and the redefinition of priorities in both US domestic and foreign policies, have subordinated any advancement of integration commitments in North America to Washington's security concerns. Thus, we witness the growing securitization of North America's economic space after September 2001, as epitomized by the launching of a 'smart borders' strategy geared to ensure 'free' and 'safe' trade and by the emergence of a so-called Security and Prosperity Partnership (SPP). The latter is a more ambitious mechanism aiming to build a favorable policy environment for enhancing cooperation in areas in which security of the region is at stake.

Thus, the fifth chapter of this book explores the principles and challenges of this new security architecture centered on the functioning of 'intelligent' borders and a new partnership redefining North America's security frontiers. In fact, this chapter suggests that any possibility for 'deepening' the post-NAFTA agenda must match the interests and priorities of the US. This is clearly suggested in the growing 'securitization' of either bilateral or trilateral issues among NAFTA partners. In other words, the chapter suggests that similarly to how NAFTA was nested, a post-NAFTA 'policy environment' is still being commanded by US strategic interests, under which either Canada or Mexico accommodate their own. However, the major argument of this chapter is that the new geopolitical configuration emerging after the terrorist attacks to the US homeland in 2001 is becoming managed through a growing governmentalization of material and human flows, rather than a real political integration at the trilateral level.

The last chapter of the book explores a typical trend and debate of many a trade regime: should it be deepened and/or widened? North America has not remained apart from this trend and debate, as witnessed by a further continentalization of energy markets, commanded this time by the Washington–Ottawa axis, and the signature of the Dominican Republic, Central American Free Trade Agreement (DR-CAFTA), which has meant a de facto enlargement of NAFTA. This chapter suggests how NAFTA remains a powerful tool in the hands of the US government in order to spread out the disciplinary mechanism and its policy implications

to the rest of the Americas. Since the early nineties, NAFTA was presented by Washington as a model to be exported to the rest of the Americas. Since 2002, when President George W. Bush got the Trade Promotion Authority (TPA) from Congress, hemispheric negotiations have attempted to reach a NAFTA-like document, wherein the core of the NAFTA values, principles and disciplines are present.

Since hemispheric negotiations have proved to be more difficult than bilateral and/or trilateral ones, the US has rather promoted a 'hub and spoke' approach in order to advance its goals. These bilateral or minilateral approaches have proved to be very beneficial to the US, in spite of the low amount of trade that is at stake. In some way they represent a sort of US-led 'NAFTA-plus' deal, in the sense that they are 'second generation' agreements, the goal of which is still disciplinary, that is, they aim to level the playing field in the Americas according to the American standard, and to constrain state involvement in the economy. This also proves that the 'regional option' still embodies intrinsic advantages to the US. Depending on the partners, bilateral or 'minilateral' deals, à la NAFTA, could be struck more rapidly than multilateral ones, are wider in their coverage, are more effective in their supervision and more difficult to circumvent. Furthermore, minilateral deals have 'systemic' effects on the rest of the partners, since they prompt them to negotiate with the US either on the multilateral front or the bilateral one.

# Part I

# The Nature and Limits of Regional Disciplinary Governance in an Era of Globalization

# 1
# The Challenges of Globalization for US Economic Leadership: the Nesting of Regionalism in Washington's Neoliberal Trade Agenda

## Introduction

The core argument of this chapter is that the regionalization process formalized under the North American Free Trade Agreement (NAFTA) was crafted as part of a major strategy of US trade diplomacy for advancing and expanding a new market-oriented regulatory framework for dealing with the major institutional and economic transformations provoked by globalization trends. Those transformations feature the reorganization of corporate competitive strategies (mainly by multinational companies – MNCs), as well as a new disciplinary body for regulating market access in trade, investment and other related issues. In the first and second sections of this chapter I shall review the major traits featuring economic globalization and their impact on states' authority and capabilities for managing domestic and global markets. I contend in those sections that a sort of 'networked' governance system seems to be looming in the productive and financial arenas, corresponding to the regionalization of markets and the networked production organized around MNCs at the global level. In the third section of this chapter I discuss how US leadership has been renewed in world economic affairs by advancing and reinforcing a principled neoliberal agenda in the emerging structures of networked governance. For the US, regional or 'minilateral' deals, such as NAFTA, are called for to play a

major role for better internalizing global rules at the bilateral level. Thus, regional clubs are becoming major institutional mechanisms upon which new governance mechanisms are being grounded, mainly in the commercial, production, and investment domains. The section also explores how Washington conceived NAFTA as an interface between multilateral and unilateral trade policies, geared towards impacting the agenda on global trade negotiations.

## Globalization and the emergence of the network economy

Nobody doubts that the term 'globalization' has become the buzzword for explaining the new trends in the international political economy of the past decades. The term has become so popular as to be used by journalists in their respective op-eds, by diplomats in their negotiations and by politicians in their speeches. Is globalization a historical breakthrough? Is it a peaking point in which capitalism finally becomes extended world-wide? Is globalization by any chance announcing new transnational architectures of governance? Or is it just a fashionable word, a new way of naming what previously was explained in terms of internationalization and growing interdependence processes?

In its popular meaning, say within the journalistic jargon, globalization refers to a state of exacerbated interdependence in which domestic processes, either in the economic, political, financial, or cultural realms, interact with transnational trends provoking a mutual reinforcement or rejection. Ricardo Petrella has attempted to measure these transnationalization processes in seven areas: financial markets; world-wide production of firms; technology diffusion; patterns of 'global' consumption; the emergence of a 'global' economic and political order; and the reduced capacities of governments for shaping the economic order (Petrella, 1996: 64). However, such a general meaning of the term becomes elusive because it refers to processes of technological, commercial and cultural expansion that have eventually prevailed in the past, although in different times and regions.

Economic historians have already studied and explained similar processes of technological change followed by periods of economic expansion and reorganization. Fernand Braudel, in his magnificent work about the emergence and consolidation of capitalism in the European space, convincingly shows how market forces progressively incorporated new territories and populations, outside the European core, in order to structure what he called a 'world-economy', that is, a

cross-border economic system in which production, exchange and labor became governed and specialized (Braudel, 1979). Other studies point to a 'first wave' of global trends from 1870 to 1913, approximately, featuring a wide commercial opening and expansion, financial transnationalization and high volumes of migratory flows, only cancelled by the outset of the First World War (UNCTAD, 1994: 119–22). Karl Polanyi even argued that the nineteenth century became the triumph of what he called 'disembedded' market forces, in contrast to what prevailed in previous periods of capitalism or other forms of production, in which market and exchanges remained highly 'embedded' in the social, political and cultural practices of societies. Thus, the decoupling of markets from national – we could say now 'local' – social and political practices earmarked this first wave of economic transnationalization (see Ruggie, 1982: 385).

Is globalization thus the definite implosion of capitalist production world-wide, earmarked by the downfall of the Soviet Union and the emergence of China as a new economic power? Though some authors have featured globalization in this sense (Dussel, 1999), other ones have rather highlighted some qualitative changes in the governance and organization of market economies. The changing role that MNCs have had in shaping world-wide production, trade and economic relations has become a major feature of the globalization era. Susan Strange had already suggested, more than a decade ago, that MNCs had to be approached as true international actors pursuing a 'corporate diplomacy' vis-à-vis societies and states (Strange, 1994). Though this practice has not yet fully developed, Strange was elaborating on some post-realist and international political economy debates arguing that states were no longer the sole unit of analysis in contemporary international relations. Currently, a new wave of studies has problematized the rise of globalization from the standpoint of the new corporate strategies pursued by MNCs in terms of production and exchange during the past decades.

According to thorough analyses done and released by United Nations Conference on Trade and Development (UNCTAD)'s Division on Transnational Corporations and Investment during the past 15 years, today's globalization cannot be solely understood as the exacerbation of economic interdependence led by an accelerated increase in transnational trade and investment flows. This growing interdependence is rather the consequence of major changes operating at the organizational level of firms' production.

Due to the impact of information technologies – mainly in the digitalization and electronic processing of data of any kind – and the

growing liberalization of markets and of competition for increasing market shares world-wide, MNCs have transformed the organization of their value chains, moving from hierarchical and national-based production strategies to a rather networked system, where horizontal interactions become intertwined with vertical ones (UNCTAD, 1994: 136–46). While hierarchical structures of organization maintained a relatively clear and easy functional specialization between parent companies and their affiliates, within a horizontal and complex organization system hierarchical functions become blurred and affiliate firms function rather as an interface with the parent firm and the rest of its affiliates, even with local and/or subcontracting firms (Dunning, 1993: 190–219; Dicken, 1993: 189–213). While in corporate hierarchical structures of organization value chains became vertically integrated at the international level, in the second strategy value chains rather become scattered and fragmented according to specific functions and to locational and spatial advantages perceived by MNCs.[1] This process of fragmentation and relocation has decentralized corporate managerial decision and has facilitated the building of 'strategic alliances' of all sorts among firms. It is rather this type of firm restructuring and its impact in the relocation and transnationalization of their value chains that feature, for some authors, the new traits of globalization trends (UNCTAD, 1994: 137–8).

This reorganization of value chains, combining horizontal networks and the relocation of functions and activities, has impacted and will continue to impact the nature of the world economic and political order. By so doing, MNCs have not only impacted or modified government policies as suggested by Susan Strange, but they have become core agents of globalization. The emerging world economic order has ceased to remain in the hands of state-centered actors, as was the case during the Bretton Woods system emerging immediately after the Second World War. At present, market actors and powerful MNCs have become major actors participating in the shaping and building of a new economic architecture.

First of all, MNCs have become agents, *par excellence*, of world-wide technology innovation and diffusion. The boom in corporate mergers during the nineties, mainly in the electronics and high technology industries, is witness of this need to catch up with the innovation risk. (*The Economist*, 1995). Inter-firm deals have also increased since those years, without necessarily involving equity transactions, as is the case in corporate franchises and technology cooperation agreements, mainly among companies located in industrialized countries (UNCTAD,

1997: 12–15). By transforming their corporate strategies with the support of information technologies, MNCs have also transformed labor organization and spaces, in as much as some authors have talked of a transition from 'fordist' labor organization patterns to those Japanese-inspired called lean or flexible (Womack and Jones, 1994). Transnational firms have also become nationally uprooted, in the sense that the country in which the parent firm is located is not always determinant in the organization and decisions of the affiliates. They are denationalized and conveying transnational 'mores', in terms of patterns of consumption, behavior, and expectations. In some ways, they pretend to symbolize the new post-modern identity: a group of people scattered all over the world, the identity of which is individualistic-oriented, framed by technical and electronic processed information, and living in the temporality of flows.

The growing and progressive internalization of market transactions has become another major trait of the reorganization of corporate strategies under MNCs. Currently, around two-thirds of global trade in merchandise and services are under the hands of MNCs. Some 33.3 per cent of world transactions are being done under intra-firm exchanges. An additional 32.6 per cent of world trade is also in the hands of MNCs, although it is being done under inter-firm or arms-length transactions. Just 34.1 per cent of world trade is being done under arms-length transactions (UNCTAD, 1995: 193). Furthermore, most of MNCs' sales are not being done through foreign trade, but through direct sales within the markets in which they are located. In 1994, exports of affiliated companies amounted to only 28 per cent of their overall sales (UNCTAD, 1997: 17), that is, more than two thirds of international transactions done by MNCs were channeled not through foreign trade, but by local sales done through their affiliates. This growing internalization of foreign trade, performed more through local sales of affiliates rather than through foreign exchange, highlights well the impact of MNCs in the reorganization of productive chains world-wide and their multiple functional connections.

The 'network enterprise', as Manuel Castells called it, is at the grounds of this complex functional integration of value chains impacting global sales and exchanges. This organization model features a system of communications and functions, the goal of which is to be connected with other poles of autonomous organizational systems which pursue specific goals (cf. Castells, 1997: 171). The network firm model does not follow a unique pattern, as Peter Dicken has explained very well (Dicken, 1993: 211). We may figure out that the network model overlaps

sometimes with the classical hierarchical model that prevailed in the past, or that multiple network systems end up by building up new complex hierarchies. The backbone of this new organizational system is the interconnections between nodes, that is, between fractions of systems that pursue specific goals, such as Castells has suggested. Interconnections range from the simplest to the most complex, according to the type and size of a firm. They are, in some way, network systems encompassing variable geometries. The size is defined by the number of nodes embraced by a network, and the volume by the complexity of the tasks performed by each node.

The emergence of the network enterprise has facilitated the fragmentation and scattering of chains and productive functions world-wide. In some cases, they are at the basis of more complex systems forming a network of networks. This has accelerated as well inter-firm technological cooperation in order to share the risks of technological change, as in the case of information technology industries and pharmaceuticals (UNCTAD, 1997: 25). The network firm model also encompasses subcontracting and inbound activities interconnected with affiliates, e.g. in the automobile sector, in order to exploit locational advantages. Thus, the network of networks reorganizes the scattered chains of a firm exploiting locational advantages world-wide on one hand, and on the other their interconnections with other 'fragments' of firms pursuing different goals and tasks (i.e. reducing the costs and incertitude of technology innovation, reducing the costs by subcontracting, supplying after-sale services, etc.).

This organizational revolution has spread out, and will continue to evolve and grow, thanks to the incorporation of new information technologies in production processes. More and more production chains are incorporating knowledge and information technologies in their respective processes (Davis and Botkin, 1994). For some authors, this has prompted the shift between one technological age and another one; from one where the access to cheap energy resources was crucial for productive activities to a new one where the access to information resources, processed electronically or via cyberspace, is becoming more and more decisive in upgrading the competitiveness and productivity of firms (Castells, 1997: 61). According to Castells, globalization is announcing a new era, featuring the rise of the 'informational society', and which has become grounded in a new technological paradigm encompassing the following traits: i) electronically processed information has become the basic input of the overall economy; ii) the diffusion of information technologies has become generalized impacting social

processes and organizations; iii) the network system is becoming the organizational model not only for firms and other productive activities, but also for political, social and cultural processes as long as they incorporate new informational technologies (Castells, 1997: 61).

The emergence and eventual consolidation of the informational economy, in which knowledge and processed information become crucial for increasing the competitiveness and productivity of firms and the overall economy, has also transformed the notions of space and time. In terms of space, the informational economy (and society) is differentiating local spaces from those built around a network. Networks operate and interconnect in geographic and non-geographic spatialities, which become enlarged or shrunk according to the number of interconnections and the complexities of nodes. In most of the cases the network system operates in what Jan Aart Scholte has called the 'supraterritorial' space (Scholte, 2000: 46–7), or the cyberspace, that is, interconnections linked by electronically processed information flows which are not territorialized. Castells has named these interconnections as conforming a 'space of flows' through which digitalized data, images, sounds and symbols are exchanged among fragmented units scattered on a worldwide basis.

By contrast, the space of place is attached to a specific territoriality and historical time. Local polities could maintain their particular memories in spite of being cross-cut by global flows. They could even challenge the identities and power relations embedded in the space of flows. There is already a whole literature that has attempted to explain and problematize the interaction between global and local spaces, in the sense that global trends have always a local impact and that local/global reinforce mutually (Stallings, 1995). Although Castells does not reject this idea, he highlights the differences between global and local spaces. The space of flows operates in an ambiguous territoriality, and depending on cases, in a virtual supraterritoriality (i.e. financial markets); at the same time, the exchange of information, signs and symbols effectuated through this spatiality become ordered synchronically, that is, uprooted from any narrative or diachronic order capable of referring them to the local memories to which they were attached. On the other hand spaces of place are not only well defined geographically, but remain the source of their own memories and historical narratives from which they construct their identities (Castells, 1997: 376–468). In that sense, globalization can be understood as a process, or myriad of processes conveying a transformation of the spatial organization of social relations and exchanges, from which transnational or interregional flows

are unleashed, and networks of interaction, functions and power are created (cf. Held and McGrew, 1999: 483).

A whole body of literature has already highlighted the importance of 'local' advantages in order to capitalize (or minimize) their exposure to 'global flows'. Michael Porter, in his seminal research work, explains how the 'competitive advantages' of firms heavily depend on nation-based conditions. Porter proposes a model depicting the 'ideal environment' – his famous 'diamond' encompassing four key fundamentals – in order to explain the conditions of possibility for a firm to develop and increase competitive advantages (Porter, 1990, 1998). Though Porter's studies still remain controversial,[2] what the empirical part of his work convincingly shows is the importance of 'local' economic, institutional and social conditions for explaining the emergence and expansion of 'global' firms.

The mutual relationship between global and local spaces also explains the emergence and consolidation of what has been called the 'Triad'. This concept refers to a geo-economic spatiality rather than a geopolitical one. It is the economic and social space conformed by the US, the constantly moving European Union (EU), and Japan. This economic space concentrates more than half of overall manufacturing and services production, and more than half of commercial exchanges, investments and financial transactions. The Triad space is interconnected with other economic spaces, either by geographic contiguity or not, that have in common their trade and investment connections with one or more poles of the Triad. This is the case of Canada, Mexico and other Latin American and Caribbean (LAC) countries in relation with the US; of Eastern Europe and northern Africa in relation with the EU; and of South East Asia and Oceania in relation with Japan (UNCTAD, 1995: 3–19).

The very existence of the Triad, as a territorialized cluster of flows and assets, is a major indicator that global trends, in spite of operating in the supraterritoriality of flows, concentrate and operate within territorialized and delimited spaces. Thus, globalization is not a generalized and/or universalized state of affairs. Globalization is a process, or network of processes, that originated in and expanded from the Triad, and that remains heavily concentrated in that very same space. In fact, globalization trends and pressures are unevenly distributed within that Triad itself. Braudel has already shown that the historical expansion of capitalism is always uneven, not only outside the economies in which technological and productive innovation takes place, but also within the very space of innovation (Braudel, 1979: 25–33).

If we assume that globalization has become a new stage in the expansion and organization of world capitalism, this expansion ought not to be homogeneous within the Triad itself; we may also assume that a sort of 'periphery' is being reconfigured in relation to the pace of technological and organizational diffusion. A similar process follows with the interconnections established by the Triad with 'outer' spaces. This uneven expansion both within and without the Triad explains in many ways the disruptive impacts of globalization, in such a way that different temporalities and spatial orders could overlap, unleashing and exacerbating social tensions in specific territories. The North American economic space, as we shall see in Chapter 3 of this book, does not escape these trends. Globalization is thus a process unleashing contradictory forces; on one hand the space of flows integrates value chains, economic spaces, interests and temporalities; on the other it releases centrifugal forces that disintegrate and fragment social spaces and temporalities that remain territorially defined.

## Globalization and the challenges to state-centered governance

### The transformation of the world economic order

The unfolding of globalization forces, starting somewhere around the sixties (Scholte, 2000: 74), progressively eroded the basis under which the international economic order was cemented after the Second World War. It must be clear that the world order that finally collapsed was that centered on the East-West divide of the Cold War, in which the governance of market economies of the West became clustered in what was called the 'order of Bretton Woods', and socialist economies became part of Soviet and centralized dirigisme. If globalization ended up with a world order, it was in fact the suppression of this major divide in the world economy of two major antagonistic economic blocs. The unfolding of globalization did not mean, however, the natural universalization of the Bretton Woods institutions. It rather provoked their transformation.

The Bretton Woods order was geared, in general terms, to the macroeconomic stability of market economies by managing the progressive and sector-specific liberalization of international trade while supplying a financial regime of fixed exchange rates ultimately pegged and adjusted to the US dollar. This order went into crisis at the turn of the seventies, once the International Monetary Fund (IMF) moved into a regime of 'floating rates' with the parallel devaluation of the dollar, and the members of the emerging Triad escalated protectionist measures in

order to restructure their respective economies to the changing situation. The floating rates regime became an additional barrier to trade exchanges and functioned as a conveyor belt for exporting inflationary pressures to the whole system, contributing to the 'boom and bust' cycles of the time.

In parallel to the Bretton Woods crisis, financial markets started to become decoupled from what economists call the 'real economy', that is, the sphere of production and circulation of commodities and services. This decoupling obeyed the deregulation of the Eurodollar financial market; deregulation that was followed by the US as soon as the impact of the technological revolution became apparent. In fact, the first 'signs' of globalization were manifested in the financial sphere, long before it impacted the 'real sphere' (Strange, 1988, 1994). The progressive deregulation of financial markets in major financial centers of the Triad increased the liquidity of the system and the volatility of investment flows, mainly those destined to portfolio and securities (Cerny, 1997). This growing supply of money, linked to the centrifugal forces unleashed by globalization, favored the re-positioning of the so-called 'emergent economies' in Asia, Latin America and, with the fall of the Berlin wall, in Russia and some East European countries. These 'emergent markets' began to fund their economic restructuring and expansion by having access to private banking loans and attracting, in most cases with no institutional oversight, portfolio investments. Those economies became rapidly exposed to the volatility and speculation of 'global' financial markets.

The multilateral institutions emanating from Bretton Woods[3] did not collapse, but attempted to adapt their ruling, procedures and normative goals to the shaking circumstances, without being successful in restoring the environment of stability and economic growth that prevailed from the end of the Second World War up to the turn of the seventies. A transition period was initiated, featuring uncertainty and lack of definition, which phased out in the mid eighties, when the Uruguay Round of trade negotiations under GATT was initiated. During those transitional years, it became highly popular among academics and op-eds writers to talk about a supposed economic decay of US hegemony. The clear sign of that decay became the inability of the US to decline the status quo ante or to move beyond the Bretton Woods order (Gilpin, 1987; Keohane, 1984).

In fact, the Bretton Woods institutions were built and sustained under US military, economic and political-strategic hegemony. US hegemony became the guarantee for the West and US allies of their security and of the geopolitical equilibrium vis-à-vis the Soviet bloc. At the same time,

the Bretton Woods institutions, under the mechanisms of the GATT, negotiated the progressive opening of manufacturing trade among the market economies. This opening was possible under US leadership, since the US economy was not destroyed during the war and stood as the most competitive and diversified at the time. This allowed the US to launch multilateral negotiations for tariff reduction under the principles of 'Most Favored Nation' (MFN), non-discrimination and reciprocity; principles that were handled very pragmatically (that is, with plenty of exceptions) in order to assure that trade opening did not harm the post-war reconstruction efforts of the allies. In the final event, the governance of the multilateral trade system was backed by US unilateral and asymmetrical opening in exchange for the economic, ideological and political support of the allies. The GATT and the Bretton Woods institutions marked, however, the transition from an economic order devastated by mercantilist, protectionist, nationalist practices and the war, to a new liberal regime featuring a gradual and sectoral opening of manufacturing industries, in a world context featuring low financial mobility and transnational production commanded by MNCs organized under hierarchical systems.

In other words, the nesting of a liberal order at the end of the Second World War did not conform to the transnationalization of technology, of financial markets or production, as it happens to be in the present time. The liberal order aimed to overcome the mercantilist practices of the past and to confront the geopolitical pressures of the time; that is, it aimed at reinforcing the capitalist bloc mainly in its most exposed regions of the East–West confrontation: Western Europe and Japan. The final outcome was what John Gerard Ruggie called, 'embedded liberalism', that is, an international system betting to liberal principles – market economies, trade liberalization, liberal democracies – but 'embedded' in the social, cultural and political practices and narratives of nation-states (Ruggie, 1982). Within this order, states remained the 'gate keepers' of all policies and commitments, and the 'shelters' of last resort for market and social actors. States remained sovereign in their economic policies, even for opting out from multilateral commitments, and became the buffers between the expanding liberal order that was set out after the war, and their domestic economies and polities.

Consequently, the GATT remained a 'soft law' agreement, that is with broad principles and general commitments; low consistency within itself, in the sense that core principles such as MFN, reciprocity and no discrimination could easily be circumvented; and with no delegation of authority in order to enforce rules agreed upon.[4] The legal softness of

the agreement remained consistent, however, with the flexible liberal order that all western economies wanted to build up. If this multilateral trade regime was successful in opening markets during most of the Cold War years, it was due to US economic strength and leadership for bearing the costs of opening its own market more rapidly than its partners. In fact, the bulk of US tariff reduction was done during three periods: 1947–52, 1967–72, and 1972–77 which roughly correspond to the first three rounds of the GATT (Geneva, Annecy and Torquay), and the Kennedy and Tokyo rounds. US estimated *ad valorem* tariff shrank from 40 per cent in 1947 to 4.9 per cent at the end of the Tokyo Round (Bradford, Grieco and Hufbauer, 2005: 82–3).

## The emergence of a multi-layered governance international architecture

The crisis of the Bretton Woods order began in the seventies, when US leadership and commitment to the principles of 'embedded liberalism' started to wane. 'Contingent protectionism' became à la mode from that time (using and abusing of escape clauses, antidumping (AD) and countervailing duty (CVD) measures), two oil shocks ended up by transmitting world-wide inflationary pressures, exacerbated by the high liquidity created by the globalization of financial markets. The then European Community emerged as an economic power, as well as Japan; and market actors, mainly MNCs, private banks and institutional investors, became powerful agents pressing for 'regime change' at that time. The irruption of globalization forces, as explained in the first section of this chapter, not only put pressure on the rationale of the post World War order, but in many ways challenged the authority and faculties of states, as the principal and ultimate units sustaining the system.

Indeed, if globalization conveyed a reconfiguration of time and space, it consequently entailed a dislocation in social organization. It has provoked not only a tension between the global space and the local one, but also a reconfiguration of political, social and cultural relations. One of these major transformations has been the fragmentation of the state's power and authority. Today, state authority and legitimacy are not bounded to a specific territoriality, as the classic concept of sovereignty used to be (Held and McGrew, 1999: 497). State authority is being overlapped, in its own territory, and beyond it, by multi-leveled layers of authoritative institutions that remain well differentiated in spite of being intertwined with the state. At the same time, the end of the Cold War has dramatically modified the notions of security as well as the rationale of regional blocs. The old notions of balance of power,

multipolarism, and other state-centered categories attempting to explain an economic and political order are being more and more challenged. New concepts, paradigms, and analytical frameworks are being introduced or redefined in order to understand new transformations; the empowerment of non-state and denationalized actors; the emergence of the space of flows and timeless time and their tensions with local territories and memories; and the transfer of power and authority from the state to other non-government actors or institutions operating at the sub- and trans-national levels. The emergence of a post-sovereign governance architecture is in the making, and seems to overlap with traditional state-centered regulatory mechanisms (Scholte, 2000: 132–51).

Indeed, the notion of a multi-layered governance architecture is becoming more accurate for explaining the new relationship that globalization is establishing between states, power, markets, institutions, and non-government actors. We could define cross-border governance as the capacity for steering, shaping, managing, yet leading the impact of transnational flows and relations in a given issue area, through the interconnectedness of different polities and their institutions in which power, authority and legitimacy are shared (cf. Rosenau, 1997).[5]

A major trait of this type of governance, as a strategy for organizing polities, is that in most cases power and authority is exercised as a means for steering, shaping and inducing a certain behavior, or a certain approach, in order to deal with transnational problems, rather than imposing a coercive action. Governance is being exercised, at the transnational level and within the institutional traits already described, by 'co-optive' and 'soft' power[6] mechanisms rather than 'hard' ones; by the progressive legalization of new norms and principles under regional regimes rather than by state to state 'deterrence' or confrontation between geopolitical blocs. Hence, institutional attributions and capabilities are distributed, though in an asymmetrical way, throughout a net of linkages. Linkages and the distribution of attributions and capabilities are mainly done through the codification and enactment of rules, treaties and organizations, in which the degree of compliance is flexible and variable. Common norms, shared values and principles, as well as the knowledge and information that support them are also crucial in these emerging architectures of cross-border governance.

The emergence of a multi-layered governance architecture has certainly challenged the traditional notion of territorial-based state sovereignty, but it does not mean the end of the state and its authority. Statehood and government authority are bound to be redefined in the

global era. The experience of the EU epitomizes this major redefinition of the state's functions and capabilities. Under the principle of subsidiarity there is a permanent devolution of a state's faculties and obligations to sub-state units, some of them constituting cross-border polities; at the same time, there is a constant delegation of power and faculties from state units to interstate and supranational organizations. However, a multi-layered governance architecture does not mean that states are becoming simple agents of transnational interests, say, corporate and market actors (Cox, 1994), neither does it mean that fragmentation and diffusion of states' authority is converging toward the construction of mega-states, as Castells seems to perceive the evolution of the EU after the Maastricht treaty (Castells, 1998: 310–34). The diffusion and sharing of power and authority among distinct 'stakeholders' (that is, actors other than government) does not eliminate state politics and policies, but it entails asymmetrical impacts on states' capabilities. Depending on the regime or issue area where cross-border governance is exercised, some states' agencies see their capabilities reduced or enhanced.

As Jan Scholte has correctly observed, the irruption of the global era does not mean that everything is moving and changing. There are in fact various elements of continuity from the 'old' order and the new emerging one. As this author suggests, regulation in a post-sovereign world has mainly occurred in a bureaucratic way. Governance, either at the sub-national or trans-border level has continued to involve organizations that are large, permanent, formal, impersonal and hierarchical (Scholte, 2000: 157). This is particularly true with principled- and technocratic-based forms of governance. In contrast to other types of governance, in which the role of charisma, religious values, patronage networks, and corporatist political behavior are crucial, principled bureaucratic governance is grounded and legitimized under knowledge-intensive mechanisms for representing and intervening targeted behaviors, populations or 'issues' to be governed. If a major trait of 'modern' states was to install and reproduce knowledge-based and responsive bureaucracies, globalization seems to reproduce this pattern in sub-state and international organizations, regardless of whether they are government-based or not. If principled bureaucratic governance seems to be maintained and reproduced at the global level, the role of science-based knowledge as a means for shaping and re-shaping power relationships seems to be also another element of continuity for the global era. In other words, cross-border governance institutions entail not only a fragmentation of power and authority towards multiple

polities, most of the time under legal mechanisms, but they also convey a growing governmentalization of specific issue areas.

By governmentality I understand the basic power relationship between two units, or individuals, the goal of which is to regulate and/or discipline conduct. In his monumental and seminal work, Michel Foucault suggested that in modern western societies this art of guiding behavior has been heavily invested by scientific knowledge and observatory practices aiming at establishing norms and standards of performance. Individual deviances, social patterns, population trends are being established and intervened thanks to this capillary objectivation of individual and social behavior. Scientific-based governmentality makes of human beings and populations a space of multiple calculations in order to extract from them a truth, or a utilitarian or convenient outcome.[7] Although the governmentalization of social behavior became embedded in state-society relationships, it seems that at the turn of the 21st century, multilateral organizations and regimes are universalizing this technology, provoking what Laura Zanotti (2005) has called the governmentalization of the international order.[8]

This is in part the case in the commercial arena, which is being more and more ruled under the principles of 'good governance' under which states' policy outcomes have become restrained, penalized and calculated according to a new growing legalization body of 'trade disciplines'.[9] This is certainly the case in other domains such as migration (see Chapter 5 of this book), development and human rights issues, fields in which individual and social behaviors are directly targeted for policy purposes. If the governmentalization of fragmented and/or 'national' populations was aimed at 'normalizing' patterns of individual or social behavior according to measurable and 'scientific' based standards during the past two centuries in the western world, it seems that the current and growing governmentalization of 'regional' or 'global' agendas aims at 'standardizing' social and policy outcomes according to 'benchmarks', 'best practices', and 'good governance' institutions being spread out world-wide.

Hence, if knowledge-embodied-bureaucratic structures of governance seem to be reinforced and reproduced by the spread of globalization, it could be argued that the core of power relationships in the global era will be in fact the constant re-objectivation and 'science-based' intervention of issues, populations and individuals, framed and targeted as 'global' issues or subjects. If, according to Foucault, the emergence and consolidation of a disciplinary-science-based-governance of fields and subjects appeared long before the consolidation of modern states, and

has progressively pervaded modern state machineries, I could argue that these rational-intensive mechanisms are currently becoming the backbone of post-sovereign global governance architectures.[10]

Last but not least, if globalization is challenging state capabilities, fragmenting its authority within its own statehood and beyond it, and diffusing power and legitimacy to non-state actors (the so-called 'privatization' of authority), this does not mean that the sovereign power is completely passé. States could reinforce their governance capabilities by delegating authority and power to sub-nation units, transnational institutions and/or supranational ones (as in the case of the EU). But all these complex and sometimes overlapping governance relationships could reinforce, yet invigorate, sovereignty-based strategies and policies. In other words, post-sovereign governance architectures overlap and coexist with sovereign-based architectures. Though tensions and clashes may appear in the interconnections, mutual reinforcement of the two regimes may be anticipated. This is in fact what is happening in the North American space, where post-sovereign governance mechanisms have been introduced at the economic level, but sovereign-centered strategies have been reinforced at the migratory and security domains. As Joseph Nye had clearly foreseen almost two decades ago, global/regional governance architectures are best suited for those strong sovereign countries, such as the US, whose leadership became confronted, with the end of the Cold War, with challenges rather than with 'challengers' (Nye, 1990).[11] If control over policy outcomes has become more relevant than control over states (or political elites), 'co-optive' and 'soft' power technologies of governance have become more important for the ('good') governance and governmentality of international affairs.

## The renewal of US leadership under networked-governance regimes

A major trait of the post-Bretton Woods order emerging from the past two decades is that to an inter-state system still prevailing in the political and strategic fronts, a sort of 'networked' governance system seems to be looming in the productive and financial arenas. In other words, the emerging economic order seems to be grounded more in a system of institutional networks, rather than a system anchored on inter-state cooperation and confrontation. This does not mean that inter-state conflict/cooperation will disappear from the system, but that national agendas in some specific issue areas (such as trade, investment, finance,

human rights, environment, etc.) will become more and more designed according to the logics and operation of this networked governance. This has become the case in global trade affairs, where a sort of 'corporate-oriented' agenda, speculating on a further liberalization of markets in new areas such as government procurement, agriculture, investments and services, combined with a strong protection of corporate property rights, became nested in a growing networked system of trade governance during the last two decades. The US has certainly become the major leader pushing for this agenda, which aims to 'disembed' market forces mainly from state policies but also from 'local-based' social and historical narratives. As I shall argue in the second chapter of this book, NAFTA became a major breakthrough in US trade policy in order to push for this new corporate-led agenda at the regional and networked level.

This corporate-led agenda has been scrutinized by networked civil society groups and denounced as a short-sighted 'neoliberal' model of governance for dealing with globalization trends (see for instance Stiglitz, 2002), and it still lacks a consensus not only amongst the 'stakeholders' involved, but within the different interconnections of the networked system. However, amongst the Triad partners and their multiple interconnections with their partners, there is a generalized support for market-led policy changes. This is in fact what is at stake in the renewal of the Bretton Woods institutions since the last two decades, once the Uruguay-Round was set up. This is what is at stake in the refurbishing of past models of economic cooperation and integration such as happened in Europe, Asia (such as the Association of South East Asian Nations – ASEAN) and the Americas (the Central American Common Market – CACM and the Andean Community – AC) in the past two decades, or the creation of new integration 'clubs' such as NAFTA or Mercado Común del Sur (MERCOSUR). All of them attempt to incorporate, adapt or minimize the impact of this corporate-led agenda that was nested in the networked system emerging in the post-Bretton Woods era. Will this mean that the new world economic order is heading towards the triumph of disembedded markets in which states lose their mediation mechanisms in order to balance the social and political costs of the growing commodification of material life? Will 'neoliberal' governance of economic 'global issues' become the legitimate 'good governance' model of the world?

The answer to those questions is still difficult to articulate. The fact that a corporate-led agenda has been nested in a system of networked governance, and that there seems to be a minimal convergence to it, does not mean that a 'neoliberal' decalogue is becoming the model of

'good governance' practices. The evolution of the EU, post-Maastricht, is an example of this. The European model has been successful in combining a corporate agenda established since the creation of the Single Market, with a social agenda, regional policies and supranational institutions that attempt to preserve or re-adapt former national-based welfare institutions. Japan, South-East Asian countries and China, while exploiting well the advantages of globalization, still keep the core policies and practices of a 'developmental' state. Even in North America, where the inception of the disembedded liberal agenda has become a model of economic governance, as will be discussed in the following chapter, this has not (yet) challenged the welfare state in Canada and the oil-state-monopoly in Mexico through which social policies are ensured. However, North America has become a sort of laboratory for this new wave of market revolution, challenging the role and faculties of a welfare or developmental state either in Canada or Mexico, as will be explained in the subsequent chapters of this book. Mexico has in fact become the country that has had to adapt more to this policy change, and the country that has had more difficulties in articulating cross-border development policies after NAFTA.

What becomes then interesting for analytical reasoning is to explore how shared norms, values, agendas or regimes' 'social purposes'[12] are being changed not by the mere imposition of a hegemonic state's agenda vis-à-vis non-hegemonic or weak states. What becomes relevant for our analysis is how a hegemonic state, in this case the US, is able to adapt old principled regimes and create new ones in order to respond to the centrifugal forces unleashed by globalization. Since the emergence of the so-called 'Washington consensus' at the turn of the eighties, geared to the managing of subsequent financial crises provoked, in part, by the globalization of financial markets, to the present, Washington has consistently pushed for a 'disembedded market model' as a benchmark of 'policy change' for dealing with the pressures of globalization. This model became nested during the financial crises affecting Mexico and many LAC and developing countries during the two last decades of the 20th century. It became better articulated at the outset of the Uruguay Round in 1986, and with the opening of the bilateral or minilateral front of trade negotiations with Canada, and later Mexico, gearing to the signing of NAFTA.

## The emergence of the 'Washington consensus'

During the financial crises of the eighties, affecting Mexico and other LAC countries, the so-called 'Washington consensus' was crafted for

managing bail-outs and the restructuring of state-markets relations in the developing world. As we know, the articulation and implementation of this new policy formula meant the triumph of 'neo-classical' economic models over former Keynesian-inspired models that prevailed in LAC countries from the aftermath of the Second World War. Import substitution, industrialization policies pursued through protectionism, and welfare policies leveling labor with corporate interests were all inspired in Keynesian paradigms calling for the state as a buffer between market forces and social protection (Biersteker, 1992; Fernández-Kelly, 2007). Import substitution through state-dirigisme became part of the 'embedded liberal order' prevailing during the Cold War years, through which developing countries could reduce the inequalities conveyed by international markets which played against their own industrialization. Accordingly, developing countries ought to develop a vigorous manufacturing sector in order to level the playing field for competing in international markets.

By contrast, the neoliberal paradigm supposes that economic wealth can be obtained if entrepreneurial freedoms are optimized within an institutional setting where individual liberties, private property rights, efficient and free markets are enforced by the state. States remain regulatory agents, policing and enforcing fair competition and the 'freedom of choice' of individuals (the so-called *homo economicus*) and their polities (Harvey, 2007: 22). As opposed to Keynes-inspired models, state intervention became stigmatized as creating distortions in price signals and the natural equilibrium between aggregated supply and demand. Only in those fields where 'market failure' became apparent – such as basic education, health, safety nets – did state intervention become required in order to supply a 'public good'. However, once markets appeared to become 'more efficient' for supplying those very public goods, the commodification or 'privatization' of those fields was required, in order to increase 'efficiencies' and 'welfare gains' (regardless of the social distributive impact).

Since the Thatcher/Reagan administrations in the United Kingdom and the US, during the seventies and eighties, corporate rights, firm restructuring and market efficiency became empowered against former states' practices in order to ensure the restructuring of production and the relocation of resources in the most efficient way. Going back to 19th century Spencer-inspired ideas on evolutionary economics, neoliberals currently advocate that markets work as a sort of 'fitness center for all kinds of firms, in all kinds of industries, not just the large and lucky, and also for their workers and host communities' (Richardson, 2005: 112).

This global 'fitting room' spurs the 'creative destruction' of capital, through a process of 'sifting and sorting'; 'unhealthy' firms leave the market, and only the fittest survive.[13]

The debt crisis affecting developing countries during the eighties, provoked in fact by a rise in interest rates by the US Federal Reserve, became a 'window of opportunity' for generalizing the neo-classical prescription for adjusting and restructuring state-markets relations in the developing world. The twin Bretton Woods sisters, the IMF and the World Bank (WB), already overtaken by the collapse of the fixed-rate monetary system, rearticulated their programs in order to police and implement the 'Washington consensus' formula as a means for bailing out and overcoming the financial havoc.

The IMF became the lending of 'last resort', able to mediate – with the monetary support of the US – between failed debtors and private banks. However, stand-by and other emergency loans were extended by the bank as a condition for restructuring according to the neoliberal formula. Accordingly, the WB extended new loans for enhancing infrastructure and human capital under the same premises. Thus, under the principle of 'crossed-conditionality', these two institutions phased out state-dirigisme and pushed for fiscal discipline, privatization of public-owned enterprises and the liberalization of trade (*The Economist*, 1991).

The US treasury also played a major role in the crisis management of the time. Since Washington still deploys what Susan Strange (Strange, 1988) called 'structural power' in the financial system – credit capacity and the supremacy of the dollar as a currency of exchange and reserve – its support became crucial for facilitating any bail-out. The Mexican debt crisis showed this, as well as the subsequent crises this country suffered, the most recent one at the turn of 1995, a year after NAFTA came into force. The US treasury crafted in fact a whole strategy of crisis management – around the Baker and Brady plans – through which multilateral institutions, private and public banks, and 'sovereign' debtor countries negotiated the rescheduling of their loan payments, debt reduction in order to reduce interest payments and the entrance of 'fresh money' as a condition for regaining growth and the reintegration of debtor countries to financial markets (cf. Isaak, 1991: 194–224; *The Economist*, 1991). However, if default countries wanted to regain their credibility to corporate firms, institutional investors and private banks, their models for regaining economic growth had to be anchored around the neoliberal consensus.

However, the Washington consensus never had a wide support among the population of the country that launched policy change according to

its general guidelines (Biersteker, 1992: 126–30). Economic adjusting and restructuring during the eighties was undertaken by a coalition of commercial banks, Washington-based institutions such as the Treasury, the WB and the IMF, and local-based technocratic élites within developing countries, whose political and ideological legitimacy became anchored on the new credo of policy convergence on market-oriented solutions. The consensus did not spread out in a linear way as a design of destiny or as the imposition of a hegemon. It was rather articulated in the complex networks dealing with both financial and trade governance, either at the multilateral, regional or bilateral level. It also became progressively incorporated in Washington's foreign trade agenda, once it became clear that costs for keeping and widening the liberal trade order had to be equally born by US trade partners.

### From free trade to fair trade: the crafting of the US multi-track trade agenda

Since the turn of the eighties, and during the past two decades, Washington has followed a three-tier approach on foreign trade issues: multilateral, unilateral and minilateral (Saborio, 1992). At the multilateral level, the US made all its efforts for ending the Tokyo Round and for initiating the Uruguay Round in order to negotiate a more ambitious trade agenda. At the unilateral level, the US Congress activated old jurisdictions and initiated new ones in order to abate, though with a wider and enlarged meaning, unfair trade practices. And finally, at the minilateral or regional level the US first engaged in free trade talks with Canada, its main trade partner, in order to further include Mexico in what later became NAFTA. Both the Canada and US Free Trade Agreement (CUSFTA) and NAFTA had the role of widening the coverage of trade and trade-related disciplines according to the principles articulated around the Washington consensus and the new agenda of multilateral talks.

This three-level approach on US trade diplomacy made trade negotiations and bargaining appear at times contradictory, at times complementary. However, in many respects Washington committed to a cross-cutting agenda, the common aim of which was to 'level the playing field', as it was called, vis-à-vis overall America's trade partners. Pursuing that goal was the rationale under which both multilateral talks under the Uruguay Round were pursued, and bilateral negotiations with both Mexico and Canada undertaken. Though through different means, this was also the rationale under which Capitol Hill mandated and/or activated unilateral relief vis-à-vis unfair trade practices.

By framing key policy initiatives under the major goal of 'leveling the playing field', Washington sent the message to its major partners that non-compliance with old principles (such as non-discrimination or MFN treatment), or with new ones (such as 'barring structural impediments' to trade), would be punished at either the multilateral or unilateral level. In other words, with the notion of leveling the playing field US trade diplomacy aimed at obtaining symmetrical treatment from its trade partners, i.e. a similar treatment given to them by the US. The quest for 'symmetry' of treatment is deeply rooted in the policy debates of the seventies and eighties of the past century, as a means to offset American economic imbalances and relative economic decline due to the proliferation of 'free riders' in the world political economy.

The very best example of this new trend inaugurated at the unilateral level was the Trade Act of 1974 and Section 301, through which Washington enlarged the notion of what it understood by 'unfair trade' practices. This section defined two types of targeted practices: those that violate agreements that the US has with any of its partners, and those that are 'unreasonable', discriminatory and unjustifiable and 'burden or restrict' US commerce (Grier, 1993). In order to restrain the proliferation of these newly-defined unfair trade practices, Congress gave the president the capability of enforcing trade sanctions in order to make conflicting parties abide by them. These sanctions could consist of denying or modifying any trade concessions or increasing any tariff or non-tariff barrier.

The use of economic sanctions for making states respect agreements was not new in US foreign trade diplomacy. What became new in this legislation was the faculty given to the US president for imposing sanctions even in those cases when no violation exists, that is, when foreign practices are being judged as 'unjustified, unreasonable and discriminatory'. Discriminatory practices were already proscribed under the GATT, but the first two practices were not. Washington understood as unjustifiable those policies or practices that are inconsistent with international agreements; that is, practices that are not illegal – according to bilateral or multilateral agreements – but that play against the rules of the game as understood by the US. 'Unreasonable' was defined as any act, policy or practice which, although not violating international legal rights of the US, is otherwise unfair or inequitable (Grier, 1993). Through such a wide and vague definition, almost any economic practice playing against US interests could be targeted by unilateral sanctions (see also Goldstein, 1993: 195).

Section 301 and its later refinement by the Omnibus Trade and Competitiveness Act of 1988 (the so-called Super 301) have never been

perceived as protectionist in the US. By prosecuting practices that either violate legal rights or discriminate against the US, or that are just simply 'inconsistent' or 'inequitable' to US practices, the US Congress sent the message to the world that it was not targeting the entry of imports, but rather the enhancement of exports by inducing partners to play by the rules. Congress was, however, cautious and granted to the president the discretionary faculty for using sanctions. If the Executive judged that national security concerns were at stake, or that the use of sanctions would imply political costs to be borne, sanctions could be waived.

This explains why petitions under this section have been rather few (Goldstein, 1993: 216–7), compared, for example, to other 'classical' unfair trade remedy practices such as AD and CVDs. However, the importance of Section 301, Super 301, and any other similar legislation was that they enlarged the conceptual scope under which 'unfair trade practices' was understood in the US. 'Unfair' meant not only a violation of an agreement or a discrimination against a partner, but also practices that were inconsistent, unjustifiable, unreasonable and inequitable to US commerce. By using the 'threat' of imposing trade sanctions for abating 'unfair' practices, Washington aimed to expand market access by 'leveling the playing field' with the rest of its trade partners.

Unlike the faculties stemming from Section 301, procedures for imposing AD and CVDs are rather quasi-adjudicative and not subordinated to political or strategic consideration by the White House. Final decisions are being taken by the Department of Commerce (DOC) and the International Trade Commission (ITC), with no interference by the US Trade Representative (USTR). AD petitions became a major tool for American producers to seek relief from 'unfair' practices. CVD petitions increased as well, though the rate of acceptance did not follow the same trend as that of AD (Goldstein, 1993: 217–9). The flexibility introduced by Congress for activating those mechanisms made them a major sign of US 'neo-protectionism'. This became materialized as the proliferation of 'managed-trade' deals throughout different industry sectors such as steel and automotive.

What becomes important to highlight here, is that the activation of AD and CVD, combined with other relief mechanisms and the enactment of Super 301 in 1988, increased the uncertainties for accessing to the US market. By increasing the uncertainties and consequently the costliness of accessing its own market, the US increased the incentives for its trade partners to join trade negotiations either at multilateral or bilateral levels. Incentives became higher once trade partners realized that market access was not the only issue of the problem. By legitimizing the use of

unilateral retaliation as a means for enhancing exports, the US also increased the costs for their trade partners of keeping the status quo in their respective trade policies. This explains why the US could simultaneously pursue multilateral and minilateral trade negotiations while maintaining an aggressive unilateral trade agenda.

The rise of unilateralism was not confined only to the US; the then-called European Community overzealously activated its trade remedy laws as well and reached voluntary export restraints with the Japanese. The enactment of the Single Act, announcing the establishment of a single market for 1992, and the creation of the so-called European Space, embracing former European Free Trade Area (EFTA) countries, signaled the coming back of regionalism as discriminatory blocs for fueling growth in specific regions of the world to the detriment of multilateral cooperation.

This was reinforced by the parallel negotiations of the CUSFTA and the subsequent discussions about whether regional blocs were contributing to or hampering the expansion of GATT disciplinary ruling. Last but not least, the waning of the East-West conflict, that came to an end with the fall of the Berlin Wall and the collapse of the Soviet bloc, made apparent the possibility of spilling over conflicts from the trade agenda to the security agenda. Consequently, for those advocating the reinforcement of the multilateral trade system the negotiation of a 'big package' in the Uruguay Round was necessary for strengthening the multilateral system (see Schott, 1990: 8–9).

For the US, the launching of the Uruguay Round had two major goals: to curb unilateral pressures at home and abroad, and to enlarge the coverage of multilateral rules in new areas in order to induce structural reforms compatible with the financial adjustments that were taking place under the command of the IMF and WB. By seeking to level the playing field with its trade partners, Washington aimed at 'universalizing' the corporate and market-oriented strategies articulated under the Washington consensus. This time, the legitimacy for those policies could be enlarged, going beyond the interests of banks, investors and neoliberal-inspired technocracies involved in the financial restructuring of the time. By launching a new round of multilateral trade negotiations targeting the design of new rules and institution building, the US attempted to enlarge the support of its market-oriented formula.

The multilateral negotiations took place at three levels: i) the tuning up of 'old rules', ii) the coverage of new fields, and iii) the governance of the multilateral system. In the realm of 'old rules', the agenda established in previous negotiations, mainly the Tokyo Round, concerning

subsidies, dumping, government procurement, safeguards and the elimination of barriers to trade (both tariff and non-tariff) was continued. Major improvements were achieved in this field, mainly in relation to subsidies, tariff reductions and government procurement. As for the new fields, they became the focal point of long and lasting discussions which caused this round to be completed three years after originally scheduled. The new fields under discussion were market access in agriculture, the liberalization of services under the General Agreement on Trade in Services (GATS); and rule making concerning investments and corporate rights under what was called Trade Related Investment Measures (TRIMS) and Trade Related Intellectual Property Rights (TRIPS). As for the institutional deepening for upgrading the governance of the multilateral system, the negotiations improved the dispute settlement mechanism and transformed GATT into a multilateral institution as it was originally planned in the Havana Charter. The World Trade Organization (WTO) was consequently created.

In parallel to the multilateral front opened by the Uruguay Round, the US initiated bilateral trade negotiations with Canada, its major partner. The opening of the bilateral track in US trade diplomacy was thus nested in the midst of mounting unilateral trade actions propelled by the Americas Congress since the first part of the seventies, and the new profile of a multilateral agenda that the White House had tried to advance since the mid eighties under the GATT. For the US, to strike a whole trade package with its major trade partner, at a time in which its rising unilateralism was being highly criticized by the world, was also a way to curb domestic protectionist pressures and to internalize the neoliberal agenda continentally. As for Canada, going into trade talks with its powerful and most important partner also had both domestic and foreign policy issues. The Canadians entered into bilateral negotiations once the Trudeau years were over and the Conservative Party won the elections in the fall of 1984. The Conservative Party, with Brian Mulroney as Prime Minister, came to power with a new policy agenda, which in many ways announced the end of the state-centered 'nationalist' option that prevailed during the seventies.

Though Washington had tolerated inward-looking industrial policies launched by Canada since the first part of the seventies, it became more reluctant to accept those policies during the eighties. Bilateral talks, unilateral retaliation and multilateral resolutions were used by the US in order to increase the costs of maintaining, yet deepening, the inward-looking policies taken by its partner. Washington denied Canadian firms leases on US federal lands arguing that Canada was not a reciprocating

country. As long as Washington broadened its concept of countervailing subsidies, the overzealous use of US trade-remedy laws became one of the hottest issues in US–Canada trade relations. Though Canadian imports did not become the main target of those measures, the activation and discretionary use of trade reliefs made market access to the US highly uncertain (Morici, 1991: 49–51).

Once in power, Mulroney's Conservative administration made clear the end of an economic policy based on resource wealth exploitation. The new policy goal was to increase Canadian competitiveness in manufacturing and services, and for that, to enhance market access to the US was necessary, as well as the elimination of domestic non-tariff barriers in order to attract foreign investments. Thus for Mulroney, entering into bilateral trade negotiation with the US had the double aim to lock in domestic policy changes that signaled the end of the Trudeau era, and to negotiate a whole package for 'guaranteeing' market access to its major trading partner.

In parallel to the progressive suppression of remaining tariffs between the two countries in a span of ten years, the importance of the CUSFTA was that the core of what Washington was negotiating at the multilateral level could be obtained at the bilateral one, on a better basis. Canada and the US agreed, for example, to liberalize many agricultural sectors, an opening that both Europe and Japan had been very reluctant to accept (see Hart, 1989: 131). However, some of the major non-tariff barriers still pending in agriculture, such as price support mechanisms and subsidies were not addressed in the negotiations. At the sectoral level of manufacturing, ad hoc agreements were reached in the fields of the automotive, wine and spirits and energy industries. The latter became fully deregulated ending the state-led energy policy followed in previous years. In relation to government procurement, a reduction on the threshold established in the GATT was obtained,[14] though this threshold only included purchases of federal agencies.

In relation to unfair trade practices, a mixed balance was obtained. Though Canada wanted to negotiate a common code regulating subsidies and dumping, no common jurisdiction could be obtained in this agreement, neither thereafter under NAFTA. What was obtained, by contrast, was the introduction of an alternative dispute settlement mechanism (ADSM) under which arbitration panels could substitute domestic courts in reviewing administrative decisions related to dumping or subsidies. Though no better definition of subsidy could be obtained under the CUSFTA,[15] what Canadians obtained from this agreement was the right to challenge American administrative agencies under bilateral panels

whose faculties and attributions were precisely defined by the two countries. All this was stipulated under Chapter 19, considered for some Canadians as the jewel of the agreement, because it aimed at curbing the 'overzealous' use of American legislation for masking protectionist interests.

The CUSFTA also included a more flexible ADSM embodied in Chapter 18 addressing any action that could violate, impair or nullify the agreement. In case a party failed to comply with the panel award, the claiming party had the right to impose economic sanctions equivalent to the damage inflicted upon it. By so doing, the CUSFTA legitimized the use of trade sanctions as a means for compensating for the breach or the impairment of what was previously agreed upon. Until then, the use of trade sanctions for compelling partners to comply by the rules remained a unilateral decision, mainly of the US, as long as the decisions taken under the GATT panels remained declaratory. Finally, the CUSFTA made what Michael Hart considered a 'cautious start' on the then 'new issues' of the agenda such as services, business travel, investment, intellectual property rights and financial services (Hart, 1989: 75).

## The Road to NAFTA

Two years after CUSFTA came into force, Mexico and the US initiated negotiations for a rather similar agreement. Once Canada joined the negotiations, under the condition that nothing that was agreed upon in the CUSFTA would be revised, Washington confirmed its minilateral approach not only to its major two trading partners, but to the rest of the western hemisphere. In fact, in parallel with the opening of the NAFTA talks, President George Bush launched in Miami its so-called Initiative of the Americas, aiming at the creation of a whole free trade area with the rest of the continent. The fact that Mexico accepted to negotiate an integration package with Washington earmarked the beginning of a new era of Inter-American cooperation, ending the traditional Mexican mistrust that had prevailed during the Cold War regarding US foreign policy towards Latin America.

Mexico joined NAFTA for similar reasons to those that explained Canada's signature of the CUSFTA. The US had also become Mexico's major exporting market and the principal source of foreign investments. The surge of contingent protectionism since the mid seventies, following the Bretton Woods debacle, increased the tensions on bilateral commercial relations. Similar to what happened with Canadian exports, Mexico was suddenly threatened with being countervailed in the US. Like the

Canadian political circumstances, the decision to negotiate came in Mexico from a new political administration which made deep economic reform its major political banner. In this sense, to enter into trade negotiations with the US had the intention of locking in the domestic economic reforms that the Mexican government had initiated in 1986 but that gained a decisive momentum during the Salinas de Gortari years (1988–1994).

Though the content of NAFTA as well as the organization of the negotiations were highly inspired by the previous negotiations the US had with Canada, the scope of the negotiations became widened.[16] The liberalization of tariff barriers to goods and commodities among the three countries was designed and decided following the CUSFTA model. Sectoral provisions became better specified, as for example in agriculture, textiles, automotive and energy industries. As Canada did with its cultural industries, Mexico refused to open its energy sector. As for the additions, NAFTA explicitly deregulated the service sector, including finance, against which Mexico was originally reluctant to negotiate. Whole new chapters were drafted on property rights ruling and investment measures. A great innovation introduced by the NAFTA was in fact its Chapter 11, through which private corporations could directly challenge government decisions concerning expropriation and/or investment regulations before international tribunals. Another innovation was the negotiation of two side agreements dealing with labor and environmental issues.

Those two agreements were nested on the original NAFTA agreement once Bill Clinton became the president of the US, and had to obtain the support of the American Congress for passing the agreement. Due to the fact that unions, environmental and other grass root movements were highly active during the different stages of the trade negotiations, the addition of these two agreements was the price to pay for the three governments to get NAFTA voted in the US. Through these two side agreements, Mexico accepted the use of sanctions, yet fines, if there was a 'persistent failure' to comply with its domestic environmental legislation. A similar situation was accepted in case there was a 'persistent failure' to comply with labor legislation regulating minimum wages, safety and security standards at work and child labor. Canada refused to accept sanctions from another country and agreed that any claim regarding a failure to comply with its environment and labor standards would be handled by their domestic courts. Notwithstanding, NAFTA became the first trade agreement legitimizing the use of sanctions in order to induce a country to comply with its respective labor and environmental legislation.

Last but not least, Mexico was the country that had to adapt more to the 'leveling of the playing field' policy pursued by Washington. Though Mexico had initiated unilateral trade opening at the turn of the eighties, and subsequently joined GATT in 1986, the Mexican approach was anchored on a progressive and piecemeal process where government policies remained crucial for reducing the economic and social costs of change adjustment. By signing NAFTA, however, Mexico made an abrupt and sudden change in both its domestic and foreign economic policies.[17]

# 2
# The Governance of Economic Openness through Trade Regimes: NAFTA as a Model of US Open Regionalism for the Americas

## Introduction

NAFTA was not only conceived to increase trade and investment flows among the partners; it was also devised as a disciplinary regime aiming to reduce non-tariff and non-trade barriers affecting cross-border trade and investment decisions. In other words, NAFTA has established a rules-based trade and investment regime under which economic openness and the mobility of both trade and capital are to be maintained and activated at the trilateral level. By so doing, this regime has instituted the empowerment of market actors vis-à-vis government bureaucracies, and of institutional actors at the inter-state level (i.e. panels and NAFTA-based institutions) in order to ensure the legal sustainability of the regime. The latter play a major role for building confidence and facilitating conflict resolution amongst private parties and government agencies. The common denominator of these ADSMs is that they attempt to protect the rights and interests of private actors, mainly firms involved in trade or business across the region, against discretionary or unjustified policies enacted by public agencies that could breach or impair the Agreement. This was highly desired by Canada and Mexico due to market access problems they have traditionally had with the US. But this was also particularly relevant for the US vis-à-vis Mexico, mainly concerning the pre-NAFTA investment and trade regimes that prevailed in the latter country, in which investors and markets were highly subordinated to government policies. Thus, in this chapter I

argue that the final goal of NAFTA's norms, principles, rules and legal procedures is to discipline state policies vis-à-vis firms and market actors. I also argue that NAFTA has enabled the transfer of authority to private and/or civil society actors. After more than 13 years of operation, NAFTA's institutional mechanisms have also shown their virtues and their limits, which will be assessed according to the major issue areas covered by the agreement.

## NAFTA as a disciplinary regime for facilitating the governance of cross-country economic openness

### Regional regimes and political asymmetries among parties

It is known that principled regimes or organizations grouping different states around common interests reduce the political cost for building and maintaining a minimum threshold of governance on specific global issues, such as trade, finance, technology, monetary policies, etc. The major goal of the regional club is to make members become institutionally consistent with the structural transformations taking place in their external environment.

Economists have largely argued about the advantages and attractiveness of these policy regimes.[1] They stress mostly the supply of 'public goods' these regimes normally provide, that is, goods that are in general terms non-excludable and non-rivals in their consumption (Kaul et al., 1999: 5). Most of these goods have intangible properties, like peace, security, macroeconomic or financial stability, trade openness, etc. Public goods could be offered at the national, regional and global level. The boundaries between these functional levels are not only defined by geographic considerations, but also by the positive externalities they may entail to the global system even if public goods are supplied locally. Lastly, the economic argument says that public goods have supply problems, because private agents cannot bear the cost or reap the benefits of providing those goods. There is a 'market failure' problem that makes state intervention and cooperation highly demanding.

Institutional economics approaches have also suggested that 'global' public goods could be the by-product of a pressing demand for institutional change. If we assume that markets are, above all, transactions governed by institutions under a polity, those institutions are doomed to change once major actors have realized that the costs of maintaining them are higher than the anticipated benefits of transforming them. For centuries, markets, either local or 'international', were organized under national lines and priorities. During the past three to four decades, as I

have argued in the previous chapter, financial markets began to be organized according to a cross-border rationale, which became later extended into the production and consumption domains. The digitalization of informational processes and the emergence of the virtual space as a territory of exchange moved banks and companies to re-structure their corporate operations according to transnational guidelines. Hence, policies governing markets according to national calculations became inefficient and more costly to maintain in some areas. Market actors started to press for a redefinition of market policies at the minilateral and regional levels, conforming to a so-called 'demand' for regime creation (Lawrence, 1996).

The role performed by regional regimes explains in many ways their impressive proliferation during the past years. The bottom line of these different types of clubs is to create through different means a minimum of policy convergence towards trade, investment and financial openness. Some of them, such as the EU, NAFTA, and MERCOSUR have devised wider goals and more sophisticated mechanisms of enforcement. At the same time, those clubs have become an interface between unilateral and multilateral actions, as long as they provide better benefits and gains than unilateral or multilateral agreements.

Regimes are thus important because of their direct impact on the exercise of relational power, that is, in the way actors shape their policy options and behavior. They create 'patterned behavior' through which actors do not have to recalculate their options each time they take a decision (Keohane, 1984). In this sense, regimes shape policy change both internationally and domestically. They facilitate policy convergence around shared values and rules that make sense to collective action, and they restrain local actors from undertaking policy options that play against those rules agreed upon.

However, principled regimes are not politically neutral; they are rather the product of political bargaining and undertakings that reflect both interests of state-bureaucracies and interests of domestic constituencies. R. Gilpin maintains that regimes could only be created and maintained by hegemons, that is superpowers that devise the regimes and multilateral institutions as a tool for maximizing and legitimizing their hegemony (see Gilpin, 1987). In this sense, regimes are the extension of the hegemon's power, either as a way to legitimize its supremacy in a certain field, or as a cost-sharing device for reducing the burdens of its leadership (see Nye, 1990: 253–61). For other authors, however, regimes and institutions have a dynamic in themselves that allow them to be maintained, yet transformed as long as the different actors recognize that mutual

gains over time still exist (Keohane, 1984). There is, however, a common ground in this discussion that highlights the political dimension of all agreements, in the sense that they reflect, to some extent, the accommodation of interests of the negotiating parties[2] (Chayes and Handler, 1995: 4). This explains why all regimes encompass a set of 'shelter' domains and devices, through which states or specific local actors escape the governance of the regime (see Rugman and Verbeke, 1994). Those shelter domains are the product of a political exchange that makes the regime feasible and sustainable. As we know, in the case of NAFTA, Canada sheltered its cultural industry, the US some high technology sectors and Mexico the oil and energy industries as part of their strategies to make NAFTA politically possible and sustainable.

If the regional club is not politically neutral, but the product of a political coalition clustering interests that express themselves at international and domestic levels, regional clubs are thus nested on political asymmetries and bargaining capabilities. Without US leadership and hegemony the foundations and functioning of the so-called Bretton Woods system would have been impossible; but this very same leadership became crucial for transforming and adapting the trade and financial system once the impact of globalization became manifest. In the previous chapter I already explained how the US played a major role in redefining both multilateral and minilateral rules on the economic front, as witnessed by the launching and conclusion of the Uruguay Round, the creation of the WTO, and the negotiation of NAFTA. I also explained how NAFTA was nested as an interface between multilateral and unilateral US-led trade policies. Thus, the values, principles, issue areas and procedures covered by the agreement mainly reflect US interests promoted and defended at the time. The final outcome rather reflects how Canada and Mexico accommodated their own interests into the US-led trade policy agenda.

Although political asymmetries explain the creation and transformation of principled regimes, their adaptability and sustainability depend on the anticipated gains, both politically and economically, they entail to other members. Both Canadian and Mexican governments agree, although on different bases, that the two of them have benefited from NAFTA, in spite of the US remaining the major player. As long as benefits are obtained, gains anticipated, and some asymmetries balanced, though not eliminated, regimes remain endurable, sustainable and open to further transformations.

However, the effectiveness of governance through principled regimes will depend not only upon the degree of interconnectedness among the

different polities and institutions in a given issue area, but also on their capacity to construct and maintain a community of shared beliefs that gives consistency to the whole connection. In fact, the legitimacy and maintenance of the whole club remain anchored, in the long run, to matters of interconnectedness and shared values. As Manuel Castells (1997: 171) has suggested, the major attributes for making a network perform effectively are its connectedness (its ability to transmit noise-free communication among its members), and its consistency (the sharing of interests between the network goals and the goals of its components). If a regime could be compared to a network of shared authority and power, and of informational and other institutional resources, the strategic role they play in the construction of an economic order lies in their ability to be interconnected and consistent. How is this reflected in the case of NAFTA?

## The NAFTA regime

NAFTA is not only about trade, but first of all about a myriad of principles and disciplines of which the goal is to contain and rule the involvement of states in the economy. NAFTA could be defined as a trade and investment regime of which the major target is to discipline the state vis-à-vis markets and firms, consistent with the neoliberal wave looming in Washington since the turn of the eighties. If we consider principles as beliefs of fact, we could say that free trade, economic openness and market efficiency are the major principles guiding this venture. Those principles are explicitly stated in the foreword of the Agreement and became the rationale for the foundation of a free mobility area in commodities, services and finance. If we consider norms as standards of behavior defined in terms of rights and obligations, and rules as prescriptions or proscriptions for action (see Kratochwil, 1991: 59) the twenty-two chapters forming the Agreement, as well as its seven annexes and two side agreements conform the body of norms, rules, rights, duties, and decision-making procedures so characteristic in international regimes.

Table 2.1 attempts to summarize the substance and elements featuring this disciplinary regime. The first column, reading from left to right, presents the core values embedded in this regime. Two sets of values are worth highlighting. The first, encompassing most of the normative backbone of the agreement, are those betting on the creation of efficient markets as a premise to increase welfare gains from growth in trade and investment. A corollary of this main value is the protection and empowerment of corporate and private property rights from intrusive or

abusive state intervention. The removal of non-tariff barriers, mainly in terms of using CVDs and/or AD as protectionist devices, aims to reduce transaction costs as a means for strengthening more efficient markets. All these values are embedded in the principles of neoclassical economics suggesting that wealth creation must be in the hands of markets rather than states. The second set of values is rather linked to environmental and social concerns. They aim to prevent so-called labor and environmental 'dumping', meaning by this a lowering of standards in terms of labor and environmental legislation of the participating countries – mainly Mexico – as a strategy to increase market shares in the North American market. These values do not come from an economic neoclassical 'narrative' but they are rather the product of a political negotiation between unions and principled organizations and states during the process of negotiation (see Mayer, 1998: 219–72).

The question of the convergence of expectations of those participating in a regime is also important. As a whole body of literature has extensively explained, regimes can only be created if the participants have the need or the will to cooperate and hence adjust their individual policies in a certain issue area under the expectation that collective gains in the long term will overcome unilateral short term gains.[3] That is, regimes define issue areas to be maintained in the long term, which could become eventually transformed, renovated or adapted according to changing circumstances. Furthermore, regimes also become the locus around which other regimes could be 'nested'. In the case of the NAFTA the span of the 'game', so to speak, has been settled for 15 years, at least for the construction of a free trade area. In other fields, like investments and property rights, the duration of the agreement remains open. The NAFTA has already become the locus in which two other agreements were nested, one addressing environmental issues and the other focusing on labor issues. These agreements were negotiated after the negotiations of the main agreement were over, as a condition of the Clinton administration for obtaining the congressional support for the NAFTA. These two agreements were the product of a domestic compromise between the White House and powerful environment and labor associations. However, they do not reflect an inter-state consensus due mainly to the fact that they were not a priority for the Mexican government. That is why they rather reflect a transitional 'soft law'[4] instrument anticipating legislation to be settled once the political consensus is reached throughout time.

The second column in Table 2.1 summarizes those issue areas in which integration must be accomplished. Though the list is not

*Table 2.1* NAFTA's institutions and regime maintenance

| Values | Disciplinary areas: setting the benchmarks | Conflict management and location of authority | Enforcement |
|---|---|---|---|
| • Enhance market access<br>• Increase gains from trade creation of efficient markets<br>• Promotion of market-oriented reforms<br>• Raise productivity and welfare gains | Cross-country trade:<br>• Phase-out of tariffs<br>• Phase-out of non-tariff barriers<br>• Deregulation of services<br>• Property rights protection<br>• Government procurement<br>• Sectorial specifications: automobile, agriculture, energy<br>• Other trade-related issues | PANEL Action Plan; STATE; STATE; TRADE COMMISSION | Compromise; Sanctions |
| • Empowerment and protection of corporate-based rights.<br>• Creation of a favorable environment for attracting investment | Cross-country investments:<br>• National treatment<br>• No mandatory regulations<br>• Standard rules in case of expropriation | PANEL Binding; FIRM; STATE | Go to chapter 20 |
| • Reduction of transaction costs<br>• Transparency of trade agencies | Unfair trade regulations:<br>• Dumping<br>• Subsidies | PANEL adjudicatory; STATE; STATE; FIRM | Sanctions; Suspend Ch 19; Denounce NAFTA |
| • Avoid labor or environmental 'dumping' | Environment:<br>• To avoid a 'persistent failure' to comply with domestic legislation | COUNCIL veto power; PANEL | Compromise |
| | Labor. To avoid a 'persistent failure' to comply with domestic legislation (1) health and safety standards; (2) children; (3) minimum wages | INDIVIDUAL, NGO, UNION; Secretariat; STATE; STATE | Monetary fine |

exhaustive, and is just intended to illustrate the scope and interplay of the functional areas encompassed by the regime, they cover the new fields in which the US wanted to expand GATT–WTO disciplines since the mid eighties. The first issue area embraces those rules and norms regulating the creation of a free trade in commodities and services during a 15-year span. It also embraces those specific sectors in which each country has made particular accommodations to the deregulation process, such as in the field of automobiles, energy and agriculture. This field also includes the ruling of other trade-related issues such as government procurement, the enforcement of property rights, and phitosanitary and standard policies. The second issue area depicted in Table 2.1 is the one covered by Chapter 11, concerning the rights of NAFTA-based firms and their investments within North America. The third one is that particularly covered by Chapter 19, concerning the use of trade remedy laws by state members in the realm of dumping and subsidies. The remaining issue areas are those regulating labor and environmental issues. The particularity of these areas is that they are intended to enforce selected issues on labor and environmental legislation according to each country's national legislation. This classification is neither hierarchical nor exhaustive. It is intended just to illustrate that the NAFTA could be understood, by the way it rules and works, as a cluster of functional areas conforming a trade and investment regime operating at a trilateral level.

It is clear that the 'social purpose' of the regime, that is, that the core of rules and norms around which state actors have made a legal commitment play to the benefit of market actors, mainly firms and transnational companies. The core of the consensus among the three countries is consequently there, that is, to build a more transparent and predictable environment for market actors, in order to increase the efficiency of cross-country trade, services and investment transactions. The fact that the NAFTA has fully disciplined some key issue areas around that major goal, such as the creation of a free trade area (FTA) in a span of 15 years, the abatement of the use of trade remedy laws by governments as protectionist measures, the explicit enforcement of property rights, the regulation of a new code for cross-country investment, the extension of MFN and national treatment to all parties involved in trade, services, and investments, and the disposition of other similar measures, makes us think that this is the locus where the mutual expectations of the three partners are located and hence ready to comply with, even if opportunistic gains in the short term could thrive. This disciplinary ruling was also negotiated under the 'negative list'

approach which made possible a general opening in the fields covered by the agreement by allowing parties to establish only individual exceptions. Through the negative list method, a comprehensive agreement is reached, and countries enumerate only those sectors which remain outside that coverage.[5] This means that if new areas emerge in time, e.g. electronic commerce, or new sort of services and investments, these new areas are automatically covered by the new rules since they were not listed as exceptions. This approach highly contrasts with the one prevailing within the WTO negotiations, wherein investment and services deregulation is being done following a 'positive list' methodology. According to the latter method, countries explicitly post the sectors to be covered by the new rules, and by doing so protect emerging fields that may appear in time.

By contrast, the labor and side agreements, due to the way they were devised and ruled, were conceived to work rather as discussion forums through which non-governmental organizations (NGOs) and other civic groups could put forward their claims on specific issues. The studies, discussions and decisions coming from this issue area could eventually shape a new agenda for better ruling labor and environmental issues in the coming years, when the competing and shared interests of the actors involved make feasible a better-defined undertaking. Labor mobility and social issues were kept out of the agreement, because the US government or all participating members refused (or failed) to address those issues during the negotiations.

Finally, regimes and agreements can be understood according to the level of compliance and enforcement with the norms agreed upon. As Chayes and Handler have correctly suggested, if norms are clear, unambiguous, and reflect well the political interests involved, there is a high propensity to comply (Chayes and Handler, 1995: 3–17). In NAFTA, most of the different issue areas are fully regulated by explicit rules that in the whole conform a 'hard law' regime, since it reflects a high level of rule precision, obligation, and to a lesser extent, of delegation[6] (see Abbott, 2000: 519). The opposite is also valid when rules are ambiguous and poorly reflect the interests at stake. States sometimes agree to broad and vaguely defined principles in order to avoid international surveillance in areas which they consider still remain under their national jurisdiction. There is a time lag between those principles and the will to enforce them; this gap could nonetheless be narrowed in a series of agreements negotiated in different 'rounds', as is the case within multilateral trade negotiations.

However, what gives strength to a regime is not only the clarity of the norms, but most of all, how they become instituted into authoritative

decisions that establish what the 'law' is (Kratochwil, 1991: 63). In the case of the NAFTA this is mainly accomplished by the ADRMs provided by the agreement. That is, the way economic openness is ensured, yet maintained, by the NAFTA, goes beyond the economic normative body of the Agreement. Openness is being provided, overseen and enforced by a complex institutional machinery working at two levels of jurisdiction. In most cases, the goal of these ADRMs is not necessarily the enforcement of rules agreed-upon. They rather work as facilitators in government to government negotiations when dealing with conflicts stemming from most of the issue areas in which economic integration is taking place. This is especially the case with Chapter 20's ADSM of the NAFTA, covering any conflict that threatens or actually challenges any stipulation of the Agreement – except those directly covered by the other ADRMs – as well as those conflicts arising from the interpretation of the Agreement itself. This is also the case within the ADRMs instituted by the side agreements, that is, those dealing with environmental and labor issues. Columns 3 and 4 of Table 2.1 summarize the enforcement aspects of NAFTA.[7]

A second level of rule enforcement was instituted by Chapters 11 and 19 of the Agreement, dealing with investors' rights and the administration of AD and subsidies laws by national trade agencies, respectively. Only in these cases, ADRMs are entitled to award 'quasi-adjudicative' decisions, that is, decisions taken by neutral panels and that are mandatory. Hence, according to the nature of the conflict, and the issue area in which it is grounded, panel decisions are mandatory or not, highlighting a two-level enforcement and compliance of the regime. Table 2.1 also attempts to depict this two-level enforcement of rules and their nuances through the five main issue areas encompassed by the NAFTA.

The NAFTA regime with its clusters of issue areas, institution building process and two-level rule enforcement modified the governance of trade and investment exchanges within North America. NAFTA relocated the loci of authority for trade and investment matters from the national-based level to the trans-state, yet sub-state levels. I use the term 'trans-state' in order to avoid that of transnational. The latter applies to supra-state institutions still non-existent within NAFTA. Authority has been transferred to the sub-state level because firms and other non-state actors participating in the civil society have been empowered by the NAFTA normative body in some key issue areas such as trade remedy laws, investments and to a lesser extent, labor and environment. Authority has been transferred to trans-state institutions – the Trade Commission and NAFTA panels – mainly in those areas covered by

Chapters 11 and 19. Column 3 of Table 2.1 depicts this double way in which the transfer of state-centered authority is being made by the NAFTA regime.

Hence, it is clear that arbitral panels are a new juridical figure, not to say a new institutional actor, mediating between states, and between firms and states. Panels are entitled to assess whether a breach of the agreement or a threat to comply with it has been committed by one party. The fact that panels' determinations are normally not politically motivated, but rather technically based and rules-framed, entitles them to build the general framework under which confidence building and conflict resolution is implemented among partners. Even in those areas in which state to state negotiations remain important to the maintenance of the regime, the role of NAFTA's normative institutions and dispute resolution is no less important, provided they facilitate policy options and the mutual adjustment of states' preferences. Last but not least, arbitrated decisions have given legitimacy to the use of retaliation (e.g. trade sanctions, fines, nullification of specific articles, etc.) as the arm of last resort in order to make parties abide by the rules.

## NAFTA's functional areas grounded on negotiation and compromise

### NAFTA's ADRMs addressing a breach, impairment or nullification to the overall Agreement

Chapter 20 institutes a resolution mechanism covering any conflict – except those directly covered by the other ADRMs – considered to be inconsistent with the Agreement, that threatens to cause impairment or nullification of any right or concession or that arises from the interpretation of the Agreement itself. The creation of a panel under Chapter 20 takes place once consultation among conflicting parties and a conciliatory role of the Trade Commission has proved unsuccessful to help parties to reach a compromise. Conflicts under this chapter must be handled mainly on an inter-state cooperative basis, as stated in article 2003. Panels under this chapter also play a conciliatory role. They first draft a preliminary decision or a so-called 'action plan' in order to get the opinion of the contending parties. In this first report panelists are bound to state whether an action is not compatible with the Agreement (or suppress the expected benefits of it), and if necessary, they draft a recommendation in order to solve the conflict. Once panelists have submitted their preliminary position to the contending parties, they elaborate a final decision. Final decisions rather frame policy options for the

disputants in order to make them negotiate a mutually satisfactory solution.

If there is no solution that is mutually satisfactory to the parties in disagreement, the complaining party may suspend the benefits of 'equivalent effect' to the non-abiding party, in order to compensate for the damage. Retaliation could be accomplished in the same sector the damage is being done, or in case this does not have any effect, in another sector (cross-sector retaliation). That is, drawing from the GATT experience and from most of the trade agreements of this sort, NAFTA institutes unilateral retaliation as a compensatory measure and as a tool of last resort in order to make partners play by the rules. However, it is understood that unilateral retaliation is the second best of all desirable outcomes. The role of states, the Commission and of panel decisions is precisely aimed to facilitate the accommodation of conflicting interests. The potential of achieving unilateral retaliation could eventually be used as a bargaining tool to reach a mutual agreement.

Chapter 20 of the NAFTA is an improved version of Chapter 18 of the CUSFTA.[8] At the time, the ADSM instituted by Chapter 18 of the CUSFTA constituted a step forward compared to the settlement of disputes that prevailed under GATT. In fact, both Chapter 18 and its revisited version under Chapter 20 of the NAFTA, gave to a disputant party the option to settle a dispute either under the coverage of the trilateral trade regime or under article XXII.2 of the GATT. Prior to the creation of the WTO and the setting of the WTO Understanding on Rules and Procedures Governing the Settlement of Disputes (WTO Understanding), Chapter 20 of the NAFTA was still more efficient and attractive than the dispute settlement mechanism that prevailed under the GATT. The major disadvantage of the GATT mechanism compared to that of CUSFTA/NAFTA was the dominance of the positive consensus formula. Under the pre-WTO Understanding, all members should agree by consensus, including the disputing parties, to establish a panel, to formulate recommendations or to work out an eventual solution, and worst of all, to decide about the adoption of panel reports and the use of retaliatory measures in order to compensate a grievance. Though many reports were adopted by the Council of the GATT, many others were shelved because a disputing party eventually used its 'veto power' guaranteed by the positive consensus formula. Furthermore, panel resolutions lacked transparency and the dispute resolution process was slow and uncertain (see Komuro, 1995: 17–37, and Keohane et al., 2000).

The WTO Understanding substituted that of the GATT and consequently became in 1996 the new ADSM competing with that of Chapter 20

of the NAFTA. The gap in terms of rapidness and effectiveness between the two mechanisms has been narrowed considerably mainly due to the conversion of the positive consensus formula of the GATT system to a 'negative' consensus mechanism now dominating the WTO Understanding. That is, the veto power that a disputant previously had under the former mechanism has been lifted by requiring now a consensus of all members for preventing the functioning of the dispute mechanism. In other words, a consensus is needed if members agree that a panel should not be established to deal with a dispute, if they consider that a panel decision must not be adopted, or if retaliation should not proceed. This has made the WTO Understanding more expeditious and less uncertain.

Retaliation is never unilateral if it stems from a WTO-framed conflict, contrary to what prevails within NAFTA. In the case of the WTO, retaliatory measures are always under the approval and surveillance of the Dispute Settlement Body (DSB). Retaliation could be parallel, if it is accomplished in the same sector where nullification or impairment was found, it could be cross-sector if it is done in a different sector or cross-agreement if retaliation is done in a different agreement covered by the WTO (Komuro, 1995: 60). Finally, both the WTO Understanding and Chapter 20 of the NAFTA envisage an arbitral mechanism if a party finds that the level of retaliatory measures exceeds the level of the impairment or nullification.

## The institutional constraints of Chapter 20

As of April 2007, several conflicts have been handled under Chapter 20, though only three have activated the panel mechanism. The three cases are already terminated confirming by unanimity in each of the cases the Canadian and Mexican positions. Out of the three cases, the most controversial one was that involving cross-border trucking traffic between Mexico and the US. This conflict showed how domestic protectionist pressures could compromise US principled obligations with its partners. According to NAFTA, the US should have permitted cross-border trucking services and related investment for Mexicans in border states at the end of 1995, and subsequently throughout the US as of January 1, 2000. Until recently, the US government denied access to any carrier or investor coming from Mexico, while entry barriers have already been barred to Canadians. The denial of US agencies was grounded on an over-interpretation of Articles 1202 and 1203 of the Agreement, by which parties grant National and MFN Treatments to trucking services. Through these articles, a party commits itself to grant a no less favorable

treatment, 'in like circumstances', to services provided by nationals or by other parties. US agencies alleged that the inclusion of the phrase 'in like circumstances', limits the National Treatment and MFN obligations 'to circumstances with regard to trucking operations which are like, and that because adequate procedures are not yet in Mexico to ensure US highway safety, NAFTA permits parties to accord differential, and even less favorable treatment where appropriate to meet legitimate regulatory objectives (see NAFTA Arbitral Panel Established Pursuant to Chapter Twenty, 2001: 3).

Mexico did reject this over-interpretation of Articles 1202 and 1203 of the Agreement, because it would have meant that Mexicans had to adopt the same standards in their regulatory trucking system to those prevailing in the US, something that was never raised nor discussed during the NAFTA negotiations. The Mexicans argued that the US inaction was motivated not by safety concerns but by protectionist pressures coming from organized labor in the US (The Teamsters Union). The panel simply rejected the way US authorities abusively interpreted clear principles such as 'national treatment' and 'MFN' for masking protectionist interests. In spite of this, cross-border trade by surface between Mexico and the US is still being done on a pre-NAFTA basis, although a pilot program has recently been devised in order to start a piecemeal liberalization of cross-border trucking traffic.[9]

This controversial case – as others that will be reviewed in the subsequent sections – shows the institutional limits of the NAFTA machinery, involving both domestic political pressures in the US and institutional loopholes in the agreement. When political pressures of interest groups become powerful, US agencies are ready to impose their own interpretation of rules and norms in order to protect particular interests, as shown in the cross-border trucking case, but also in other cases such as sugar or softwood lumber, reviewed in the following sections. In other words, although the NAFTA disciplinary mechanisms have made more predictable market access and policy outcomes from government agencies and bureaucracies, it has not overcome the political asymmetries existing amongst the three members.

This case has also shown how the NAFTA regime is institutionally handicapped for dealing with second and third generations of non-tariff barriers. By the former is understood all entry barriers triggered from the use (and abuse) of phitosanitary measures, human health protection, AD and CVD national legislations, etc. By the latter is understood all those barriers derived from differences in standards prevailing amongst countries as well as institutional differences on rule making and interpretation (see Abbott, 2000, endnote number 5).

The barriers pending on Mexico–US transport services could be classified as those of third generation, since US agencies are alleging not only differences in standards compromising the safety of their roads and highways, but more recently environmental regulations, claimed by different tribunals in a system where the authority regulating transport services is highly fragmented.[10] Neither Chapter 20, nor any other ADSM is legally equipped for addressing this type of barrier; consequently, due to the absence and lack of will for moving into supranational legislation from all parties (this has been a common trait since the inception of NAFTA to the present), the only way to handle these 'structural' impediments is through ad hoc deals and compromises.[11]

Notwithstanding, the fact that several other conflicts were terminated before going to a panel might suggest that Chapter 20 is working according to the goals it was originally anticipated to fulfill; that is, to induce inter-government negotiations in order to solve conflicts. Further studies should, however, be undertaken in order to clarify that hypothesis. Nonetheless we should remember that the controversial Helms Burton law was one of the cases discussed under Chapter 20, prompting the Trade Commission to mediate among the parties. The extra-territorial faculties of this law were suspended, however, due to the discretionary powers of the White House for deciding the final implementation of the law. Do NAFTA and the WTO – a forum where the Helms-Burton law was severely dismissed – help to contain US trade measures that play against the new trading system? Or did NAFTA and these new trade mechanisms help the American president to contain strong protectionist pressures coming from the US Congress? Though further research on this point is necessary, we should stress that both Canada and Mexico were very cautious in stepping the problem to the panel level.

So far, most conflicts handled by either Chapter 18 of the CUSFTA or 20 of the NAFTA, with the exception of the Mexican–US trucking case, have focused on technicalities or on the interpretation of the Agreement. The settlement mechanism has been expeditious. Once appointed, the panels have normally issued their determinations quite promptly (four to six months, except one that took nine months), faster than WTO panels, and far faster than if disputes were referred to a national court for adjudication.[12] It is worth highlighting that, in contrast with NAFTA, the WTO Understanding provides for a single ADSM for all issue areas covered, and their resolutions are grounded not following the national legislations of members (as is the case with NAFTA in many issue areas), but on the general codes and agreements signed by the parties throughout the different rounds hosted by the GATT–WTO. In other words, the

WTO Understanding features a single standard of review for the litigation of cases, which is international law codified by this institution, while NAFTA encompasses manifold, i.e. national standards, NAFTA standards, WTO standards, and even international law standards. Furthermore, the WTO has a permanent appellate body that reviews panel decisions, as previously noted, and which is non-existent within NAFTA. This concurrent mechanism and the advantages of the WTO Understanding compared to NAFTA's Chapter 20, could explain why parties have preferred the former for dealing with bilateral conflicts that could be also handled by the latter.[13]

### NAFTA's ADRMs addressing the domestic enforcement of labor and environmental issues

The fact that side agreements were nested at the US domestic level, and thereafter negotiated at the inter-state level as a compromise formula for facilitating the passing of the NAFTA by the US Congress, explains their genetic deficiencies. As Reisman and Wiedman have asserted, they were designed not to work (1995: 30). First of all, the possibility for activating a panel review is considerably vague and limited. A topic might be reviewed by a panel if a country witnesses a 'persistent pattern of failure' – never defined by the two agreements – to effectively enforce its environmental law or labor legislation on specific areas. The issues raised must be submitted to ad hoc secretariats and councils in order to assess whether there really is a 'persistent' failure to comply with a domestic law. The respective councils (one for labor and another for environment) are integrated by cabinet-level members of the three parties and must convene to the activation of a panel by two-thirds of the vote. That is, the activation of a panel under these two agreements is not automatic as in the rest of NAFTA's ADRMs, giving the possibility that a pertinent issue could become eventually blocked by the Council. Furthermore, in the case of labor issues a panel review proceeds only if they are related to a persistent failure to comply with legislation covering health and safety standards, children's work or minimum wages.

The role of panels is to find whether in fact there was a violation of labor or environmental laws, taking into account the restrictions already mentioned. Panels are not entitled to review the adequacy of those laws, nor any amendment to them, as is the case within Chapter 19 of the NAFTA. If a panel's finding is positive, states and not private actors should normally negotiate a mutually satisfactory solution, as in the case of Chapter 20. In case that a mutually satisfactory solution is not reached, the novelty of these agreements is that they envisage a

monetary enforcement award (MEA), or a fine, that panels can impose on a non-abiding party. However, a MEA can not exceed 0.007 per cent of the total trade between the parties and it could take more than two years for a panel to decide for this measure. In case that a complaint-against party does not comply with the MEA, an annual fine can be collected theoretically – though it should not exceed the original MEA – through the suspension of benefits by the complaining party. But this final solution could take three years to be implemented (see Reisman and Wiedman, 1995: 32–3).

It is worth noting, however, that these side agreements empowered advocating groups and other civic organizations, even individuals, to instigate an investigation directly to the ad hoc Council. Nonetheless, all remedial negotiations derived from a panel award are handled strictly by states. Though the possibility for a private initiative to become a final panel award is not simple, these side agreements have already proved to work as forums in which different environmental organizations, research institutes, human rights groups, lawyers' associations and other groups of the civil society can put forward their claims over specific environmental or labor issues. Their claims have spurred the making and publication of several ad hoc studies, the organization of ministerial-level consultations and the monitoring of some cases by the administrative body created by the side agreements. Though no submission under these agreements have activated a panel, so far, claims coming from civic associations have succeeded in some cases in putting pressure over state agencies to solve a claim in a satisfactory case. This was the case, for instance, when the US National Labor Relations Board ruled that a plant closing was motivated by anti-union reasons, after a submission was done by private groups at the Mexican National Administrative Office created by the side agreement on labor cooperation.[14]

Although grass-root movements have become empowered by these side agreements, those movements still reflect the interests of civil society groups that have a say in US politics. Some groups existing either in Canada or Mexico, striving for the defense of the welfare state or state-led agricultural policies, are still peripheral to the debate about the governance of externalities provoked by the integration process.

## NAFTA's functional areas grounded on 'quasi' adjudicatory decisions

In contrast with the issue areas in which conflict resolution is being guaranteed by mediation and negotiation, NAFTA embraces two major

fields where dispute resolution is handled by panel on a quasi-adjudicative basis. These fields cover the domain of cross-country private investments coming from a party, and regulated by Chapter 11, and trade remedy laws targeting dumping and subsidies, regulated by Chapter 19. Within these areas, there is little room for states to negotiate their differences, except in those specific situations when negotiation is allowed. Furthermore, within those two areas market actors have the possibility and the choice to substitute local tribunals for a panel review. However, in neither case are panels to be considered as supranational bodies. Chapter 11 final awards, although binding, can only be enforced by states through unilateral retaliation; within Chapter 19, panels can not judge nor abrogate final decisions coming from national administrative agencies. They are only allowed to decide whether those final decisions are consistent with national legislation and, if this is not the case, they remand in part or in full this decision to be reconsidered by the appropriate agency.

**Regulating conflicts in the field of capital mobility**

Chapter 11 does not truly institute a new ADSM; it rather provides that any conflict arising from the issues covered by that Chapter (trade-related investment measures) as well as by articles 1502 and 1503 of the Agreement (concerning state monopolies and government-owned enterprises), must be handled by arbitration procedures regulated either by the World Bank's International Center for the Settlement of Investment Disputes (ICSID) or the United Nations Commission on International Trade Law Arbitration Rules (UNCITRAL). However, the ICSID Convention works for a panel if both the disputing party and the party of the investor are signatories of the Convention. The United States is currently the only signatory of ICSID, which means that no panel under present circumstances can be invoked under those rules. However, Chapter 11 provides that the Additional Facility Rules of ICSID could be eventually invoked, provided the disputing party or the party of the investor, but not both, is a party of the ICSID. Hence, these rules will regulate arbitration activities under any dispute arising between the US and any of the other two members. Due to the fact that neither Mexico nor Canada are signatories of ICSID Convention, the arbitration of disputes stemming from this chapter will be regulated under UNCITRAL arbitration rules.

An important feature of the Chapter 11 arbitral provisions is that market actors could activate a panel dispute against a state, without having to go through their own governments. No other ADSM within

NAFTA makes such an empowerment of private actors. This is not the case under Chapter 20 disputes, under which government to government conflicts are framed and negotiated. The empowerment of private actors was done at the judicial and governance level. Chapter 11 of the Agreement defines rules of thumb for dealing with foreign investors. Apart from granting National Treatment, Minimum Standard of Treatment and MFN status to investors and investments, this chapter prohibits performance requirements, bans nationality constraints for the selection of CEOs and administrative boards of firms, guarantees free monetary transfers, and regulates expropriations or measures tantamount to expropriations. Chapter 11 also enables firms and investors to activate a panel dispute against a state, without having to go through their own governments if any of the above rules are breached.

Final awards of arbitrated panels activated under Chapter 11 are binding, and in case they are neglected by governments, the complaining party has the option to activate a panel mechanism under Chapter 20. Alternatively, the investor may claim its case before the host country's domestic courts. However, once a private actor activates a panel under this chapter, he waives his rights to address the same conflict in a domestic court. The fact that there is a possibility that government agencies could eventually neglect the final implementation of the award could severely restrain the scope of the ADSM under Chapter 11. The mechanism is conceived to put legal pressure on governments in case they breach investors' rights enacted under Chapter 11 of the agreement. But governments could eventually fail to correctly enforce arbitrated awards. In such a circumstance, private investors have the option to activate a panel mechanism under the rules of Chapter 20. However, as previously seen, disputes under this chapter are handled by states, not by market actors against states, and final solutions are not necessarily rules-based, but rather politically compromised.

Chapter 11 did not exist under CUSFTA so in many ways it could be envisioned as a device for deterring Mexico's discretionary policies concerning nationalization and foreign investment policies. In many ways, this chapter has meant a challenge to Mexico's and in some way Latin America's state-centered law paradigm regarding the treatment of foreign investments. Chapter 11 is drawn from the investor/host state dispute settlement mechanism established in US bilateral investment treaties signed with some Latin American countries, which Mexico and Brazil traditionally refused to sign up to (Taylor, 1997; Manning-Cabrol, 1995: 1200). The reason for this is that Mexico traditionally was attached, for historical reasons, to the principles of the Calvo Doctrine.

This doctrine enacted since the end of the nineteenth century the absolute equality among sovereign states and the equal treatment between nationals and foreigners. Consequently, when a foreign investor was involved in a dispute, it could not claim the diplomatic protection of its own government and ought to submit its claims under local tribunals. Though enacted by an Argentinean magistrate, the Calvo Doctrine became very popular in Mexico and in most Latin American countries seeking to protect themselves against potential military invasions coming from Europe or the US, alleging the defense of their nationals on disputes concerning their investments in the host country.

That is why the Mexican Constitution still inserts a Calvo clause under its article 27, requiring foreign investors to be treated as nationals, and if such an investor invokes diplomatic protection its property is ceded to the Mexican state (Manning-Cabrol, 1995: 1188). Hence, the Calvo-rooted Mexican paradigm, as in most of Latin America, compelled foreign investors to be treated as nationals, renouncing the privileges of diplomatic protection. This approach reached its height in the late nineteen-thirties, when the Mexican government nationalized foreign oil companies according to local criteria enacted by national tribunals. Though diplomatic protection was invoked by those companies, Mexico made clear that the conditions of the expropriation were settled by national tribunals.

This approach was completely opposed to the international minimum standard that the US government has traditionally required all states to comply with when dealing with foreign investments. According to the US view, even if a state does not provide its own nationals with minimum international rights, it may not escape international responsibility to guarantee minimum standards to nationals of other countries (Manning-Cabrol, 1995: 1177). Though Latin American countries, including Mexico, have moved progressively from the national-centered paradigm to that of the 'minimum international standard' approach, Chapter 11 of the NAFTA is a turning point in this regard. By this move, Mexico is not only accepting that foreign arbitration could substitute national tribunals in conflicts arising with foreign firms, including the case of expropriation, but what Stephen Zamora has called the increasing internal heterogeneization of state regulation. That is, the emergence of a new form of plurality of legal orders featuring the existence of partial legal fields constituted by discrepant logics coexisting in the same state legal system (Zamora, 1997).

The case of the Calvo clause is a good example of this so-called heterogeneity of legal orders coexisting in the same territorial space.

NAFTA has put an end to the Calvo clause if a conflict involving foreign investments could be claimed under its jurisdiction. What about those investors that could eventually not qualify as North American investors? In principle, the Calvo clause remains valid to them, as far as this clause remains a part of the Mexican Constitution. To make things more complex, we should remember that Mexico has negotiated NAFTA-like investment agreements with the EU, Japan and other trade partners. This means that the 'minimum international standards' legal space accepted under NAFTA is being extended to other partners. What about those countries remaining outside those overlapping agreements? Furthermore, by accepting international arbitration in conflicts arising with foreign investors the Mexican government is contradicting, ironically, one of the principles of the Calvo Doctrine: the equality between national and foreign individuals. Mexican investors remained attached to the logic of the state-centered legal system, while their NAFTA and other foreign partners have the option either to submit their disputes in local tribunals, or to address them under international arbitration. This shows well how, according to the words of Stephen Zamora, the nation-state is losing coherence as a unified agent of social regulation, becoming a network of 'micro states', each one managing a partial dimension of sovereignty or of the loss of it with a specific regulatory logic (Zamora, 1997).

What Chapter 11 and its spin-offs are confirming, is exactly what I argued in the first part of this chapter: the relocation of authority competencies from state-centered actors to non-state actors, or what some authors have called the 'privatization' of authority. (For a general discussion on the subject, see Cutler, 2003.) This relocation is being done both to the upper and downside levels. To the upper level, authority is being transferred from the state level to international arbitration, considering that national tribunals may be substituted by the former. To the lower level, authority is being transferred from the state to the individual, as long as private investors or firms may activate directly a dispute against a state. This transfer of authority to the individual actor could eventually become completed, at least in the field of investments, when national investors realize that the principle of equality is being contradicted by the proliferation of NAFTA-like agreements. This time, however, the principle of equalization will move in the opposite way, at least in Mexico and other Latin American countries, from the state-centered paradigm to the international-centered.

Consequently, Chapter 11 of the NAFTA is proving that trade regimes are not only fragmenting sovereign faculties of states in their own

territories, as Stephen Zamora suggests; by creating new spheres of authority at the trans- or sub-national level, they are also providing for new spaces of convergence in complex issue areas where multiple and differentiated actors have a stake. In that sense, NAFTA is facilitating a networked governance in a field that is moving from the nation-state as the most important actor, to a multi-actor international regime in which firms, civil-society organizations and regional and multilateral institutions are playing a salient role (see Manning-Cabrol, 1995: 1171).

Finally, it is important to stress that Chapter 11 is in fact a compromise between the two types of ADRM encompassed by the Agreement. It prescribes that disputes concerning this chapter should be addressed in rules-based resolution mechanisms, i.e. adjudicative decisions. Nonetheless, it envisions the use of a policy-oriented mechanism in case that the adjudicatory mechanisms fail to address the problem in a satisfactory way. This two-tier formula devised by Chapter 11 reinforces the idea that NAFTA is not instituting supranational bodies compelling states to abide by transnational rules. NAFTA strengthens the role of arbitration panels in order that both governments and market actors frame the scope and nature of a conflict, and put pressure on those parties that fail to comply with the principles and rules instituted at the trilateral level.

## Institutional constraints of Chapter 11

The most controversial issue about this chapter has become its 'perverse' effects. Conceived as a mechanism for making state policies concerning investments and investors more accountable, the current record shows that in some cases these same investors have changed the defensive mechanisms of the chapter into an offensive tool. One of the most controversial cases, the so-called Ethyl Corp. v. Canada, showed that by skillfully interpreting the ambiguities of the agreement, private firms may overrule government policies aimed at the protection of the environment, a goal that ironically NAFTA is also promoting. NAFTA ambiguities stem from a rather broader definition of an investment and the absence of a narrowed-frame definition of expropriation.

There is indeed very little limit to the scope of what Chapter 11 defines as an investment. The latter could be understood as a business, shares in a business, a loan to a business, real estate bought for business purposes and the broad concept of 'interest' arising from the commitment of financial or human resources to economic activity. In the case of S.D. Mayers v. Canada, for instance, the Tribunal ruled the scope of investment as including such assets as market share and access to

markets in the host state, suggesting that almost any kind of business activity can constitute an investment that is subject to protection (International Institute for Sustainable Development (IISD), 2001: 23).

Chapter 11 regulates three types of expropriations: direct expropriation, indirect expropriation and measures tantamount to expropriation. The record of cases suggests that the second two definitions have become the same. The case of Ethyl Corp. v. Canada becomes relevant. When the Canadian government banned the import of a chemical component (methylcyclopentadienyl manganese tricarbonyl: MMT) into the country, as well as its inter-provincial trade, alleging environmental reasons, Ethyl Corp., a subsidiary of an American firm, sued the Canadian government alleging that the ban amounted to an expropriation of its business in Canada, for which it should be fully compensated. Although the Canadian government justified the ban by its concern on the potential toxic properties of magnesium, a component of MMT, the Tribunal ruled for the compensation of the firm and the Canadian government overruled the ban. In the Metalclad v. Mexico case, the Tribunal award made explicit that measures 'tantamount' to expropriation are not constrained only to open '... deliberate and acknowledged takings of property ... but also covert or incidental interference with the use of property which has the effect of depriving the owner, in whole or in significant part, of the use or reasonably-to-be-expected economic benefit of property if not necessarily of obvious benefit to the host State' (quoted in Hufbauer and Schott, 2005: 233).

The arguments that environmental legislation, or that a 'covert or incidental interference with the use of property' could be interpreted as tantamount to expropriation are new, and have raised concerns that any foreign-owned corporation could use similar arguments to attack any type of government regulations that might have a potential impact on its profits. In fact, Chapter 11 has been used by firms as a two-edged sword: for protecting their rights, and for restraining governments from enacting policies addressing public concerns. The fact that disputes under this chapter are settled in rather a secret manner, with no obligation of governments to distribute information, and with important impacts on public policies, have led some environmental organizations to talk of a 'democratic deficit' in the field of the deregulation of investment.

Since most of the wide interpretation done to expropriation measures by some panel awards was grounded on what international law understands by 'Minimum Standard of Treatment', the Free Trade Commission (FTC) issued some 'notes on interpretation' aimed at narrowing the meaning of this principle. These notes, issued in July 2001,

assert that 'a determination that there has been a breach of another provision of the NAFTA, or of a separate international agreement, does not establish that there has been a breach of Article 1105(1)'.[15] NAFTA's FTC also urged for more transparency in the information submitted and handled under Chapter 11 litigation processes.

The US government has also shared this interest for restraining the scope and meaning of the content of similar investment chapters in subsequent FTAs signed with other trade partners. The US-Chile FTA, considered as a second generation trade agreement although most of its content and social purpose is similar to NAFTA's, limits the notion of indirect expropriation to measures that have an 'effect equivalent to expropriation' (quoted in Hufbauer and Schott, 2005: 250). The FTA signed in 2006 between the Dominican Republic and five CA countries (DR-CAFTA) states that nothing included in the investment chapter shall be construed, as long as is consistent with it (Chapter 14), to prevent a party from maintaining, enforcing, or adopting any measure 'sensitive to environmental concerns' (Article 10:11). It also prescribes a more transparent litigation process under the rules of UNCITRAL or ICSID and includes a whole annex clarifying the terms of expropriation and 'indirect' expropriation.[16]

### Administration and surveillance of trade remedy laws under Chapter 19 of the NAFTA

Chapter 19 is the most sophisticated of the ADRMs instituted by NAFTA. It could also be considered as a self-contained agreement, due to the fact that this chapter only applies to the interpretation and implementation of trade remedy laws concerning AD and CVDs of each member party. NAFTA does not institute any common body of rules concerning dumping and subsidies to be observed by the three countries. Contrary to that, each country maintains its own body of rules, laws and procedural practices concerning the activation of AD and CVDs. However, in order to deter the use of those remedy laws for protectionist purposes, a major concern shared both by Canada and Mexico when this chapter was negotiated with the US, Chapter 19 institutes four ADRMs in order to review final decisions of administrative agencies and to ensure the actual enforcement of final awards. Two of these mechanisms are entitled to award quasi-adjudicative decisions, in the sense that awards are binding and leave no room for negotiation. The two other mechanisms work on a similar basis to Chapter 20's in the sense that they frame the conflict in order to facilitate a mutually satisfactory solution for the disputant parties. However, in case that a mutually satisfactory

solution is not reached, this chapter allows a complaining party to apply the most severe of retaliatory measures envisioned in the whole Agreement. Retaliation ranges from the softest to the toughest, that is, from the mere suspension of benefits, up to the nullification of Chapter 19 or the withdrawal from the whole Agreement. Complaining parties have the discretional faculties for choosing from this myriad of retaliatory measures, giving them bargaining tools for inducing the complained-against party to reach a compromise. Consequently, even Chapter 19, presumably the most accurate chapter for dealing with trade conflicts, is a mixture between adjudicative and negotiation-based mechanisms.

The first mechanism is activated under article 1904, when a party requests a panel in order to review a final determination (only concerning the implementation of AD and CVDs) of an administrative agency of another party. Contrary to Chapters 20 and 11, there are no consultations among contending parties prior to the establishment of a panel. Market actors are entitled to request a panel, but have to do it through the representation of their own governments; that is, they have no jurisdiction to call for a panel by themselves as is the case within Chapter 11. However, private actors have the right, during the first 30 days after an administrative agency issued a final determination, to call for a panel before the trade authorities of their own country. Normally, official authorities cannot refuse this claim.

The scope of action of panels called under article 1904 is to work as an alternative device to domestic tribunals reviewing final decisions of administrative authorities. However, arbitration panels do not have the same faculties as domestic tribunals have when reviewing those final decisions. The faculties of panels are severely restrained by the normative frame mandated by Chapter 19. They are not entitled to judge or change the domestic legislation of the non-complying country, but only to review whether AD or CVD final determinations were enacted in compliance with domestic legislation and procedures. In other words, their goal is to countercheck whether trade remedy laws were applied appropriately, that is, according to domestic legislation.

In no event are panels entitled to activate a new investigation concerning the application of AD or CVDs. They work as a corrective mechanism to deter any judicial or procedural anomaly coming from a public authority. Hence, final awards of these panels confirm final decisions or remand part or the totality of those decisions in order that the government authority adopts a final decision consistent with the arbitrated award. Panels decisions are binding, as in Chapter 11, though within Chapter 19 panels establish a deadline to administrative agencies

to comply with the final award, in case of a remand. After that deadline, the same panel reviews whether the administrative authority has implemented a decision according to the final award. If this is the case, the dispute is settled, but if not, the decision is once again remanded. In principle, decisions on remand can be remanded many times, but panels have the explicit faculty of 'finalizing' all cases, that is, of issuing a final decision saying that the concerned administrative authority has modified its final decision according to the last remand decided by the panel.[17] No other chapter contains this important provision, giving authority to a panel for urging a party to abide by an award.

The second arbitration mechanism instituted under Chapter 19 is the so-called Extraordinary Challenge Committee (ECC). In contrast with other chapters, Chapter 19 allows a party to challenge a final arbitration award. However, the possibility of a challenge is severely restricted to causes of impropriety or 'gross panel error' that could threaten the integrity of the process (art. 1904.13). Under CUSFTA, the ECC was activated three times, in very controversial cases reviewing US measures against Canadian pork, live swine, and softwood lumber. (For a review of these cases, see Davey, 1996: 225–51.) In all cases the ECC confirmed the panel's final decisions. In two of these cases the US authority challenged the faculties of panels for finalizing cases. In the two cases the ECC unanimously upheld that finalizing a case was part of the faculties of the panels reviewing AD or CVD decisions (see also Mercury, 1995: 544–5). Under NAFTA, the ECC has been activated three times, again by the US against controversial cases involving both Mexico (Portland cement) and Canada (Pure Magnesium and Softwood Lumber). In all three cases, decisions coming from bi-national panels were confirmed. (For a review of final awards of all cases see NAFTA's Secretariat home page: http://www.nafta-sec-alena.org/.)

In order to avoid a never-ending remand process between panelists and administrative authorities, the third arbitration mechanism instituted by Chapter 19 aims to safeguard the faculties and decisions of panels activated under article 1904. Article 1905 states that a three-member special committee may be established to review allegations of one party that the application of another party's domestic law has prevented the operation of the panel system. According to some authors, this mechanism has been devised against the '*amparo*' regime prevailing in Mexico, under which a private party can challenge the decision of an authority (Vega et al., 2005: 50–51). In case that the final award of the committee states that a party is actually impairing the correct operation of the panel mechanism, the contending parties will attempt to reach a

mutually satisfactory solution. If this is not the case, the complaining party has two options: either to suspend article 1904 vis-à-vis the non-complying party (that is, the essence of the review mechanism under Chapter 19), or to suspend benefits according to the circumstances. Here once again we find a hybrid model for managing trade conflicts. If a country is blocking the implementation of a final award, a special panel should decide whether this is consistent or not with the Agreement. If positive, panels are not allowed to administrate the remedies; this is handled through the 'good offices' and political negotiations of the governments involved. However, NAFTA gives them the bargaining tool for not only suspending comparable benefits, but for dismissing the entire Chapter 19. Up to now, since the ruling of CUSFTA and its continuation through NAFTA, no panel has been activated under these circumstances. However, it is worth stressing that Chapter 19 gives the opportunity to a disputing party to negotiate, with a complaining party, the non-compliance of a panel resolution if the former finds that is politically costly (perhaps in terms of a domestic constituency) to abide by the rules.

Finally, and due to the fact that each party maintains its respective domestic trade remedy laws, and consequently, the right to modify them, Chapter 19 establishes a fourth panel mechanism in case that any modification impairs a prior panel decision or is not consistent with article 1902. If the final award determines that the legal reform is not consistent with the agreement, contending parties start consultations in order to reach a mutually satisfactory solution. If no compromise is reached, the complaining parties have two options: either to adopt similar legal or administrative measures, or to denounce the integrity of the NAFTA vis-à-vis the non-complying party. Though in principle any party can denounce the Agreement whenever it wants, this is the only case in which the NAFTA clearly indicates that denouncing the Agreement could become a legitimated retaliation measure in case that a party does not play by the rules. So far, this possibility has remained hypothetical.

### Institutional constraints of Chapter 19

The ECC, safeguard and the panel mechanisms instituted under articles 1904.13, 1905.2 and 1903 reinforce each other and are devised for making panels work effectively under article 1904.4. So far, the historical record of both CUSFTA and NAFTA proves that this has been the case, though the efficiency and fairness of panel decisions show mixed outcomes. During the span life of CUSFTA (five years), 47 cases were

considered by panels, of which 35 were finalized by them, 12 were terminated before a final decision was issued, either at the request of a participant or by mutual consent, and two remain active because a panel order stayed the proceeding pending a final resolution by the US Court of International Trade.[18] In all cases, when a final award terminated the case, national authorities complied with the award either at the first, second or even third remand. Out of 35 finalized cases, 20 were remanded in part or in their totality, most of them against US authorities. The fact that panels should normally work with explicit timeframes and that their decision-making hardly could become blocked, guarantees that once a case has been activated a final decision would come in a reasonable time period (theoretically 315 days). In case that the decision is a remand, the time for finalizing a case could be longer, depending on the time it takes an administrative authority to make a decision on remand, and the number of times that decision is remanded by panels. But as shown in the CUSFTA experience, most panel disputes under Chapter 19 were terminated, in one way or another. In other words, the fact that 12 conflicts were resolved before a final award of a panel could be also considered as a 'systemic' effect of Chapter 19 for settling disputes. Either the complainant realized that it was not worth waiting for a final resolution, or the disputants preferred to negotiate a mutually satisfactory solution. In both cases we could assert that Chapter 19 helped conflicting parties to reach a solution.

In terms of time frames, the efficiency of panels procedural under CUSFTA was less than anticipated. According to John Mercury (1995: 542), the average duration of a panel review was 511 days, far above that theoretically anticipated but still less, according to him, than if the conflict had had to be handled by the US Court of International Trade, as was the case before CUSFTA.[19] However, most of the time delay is to be explained by the great amount of cases that were remanded. Consequently, some highly controversial cases that were remanded more than once, such as those dealing with softwood lumber, carbon steel and tufted carpets, took between 697 to 797 days to be finalized. The average time elapsed, for instance, in all cases remanded to the US authority was 612 days, against 498 elapsed in the Canadian cases.[20]

Last but not least, although the quality and professionalism of panel decisions under the CUSFTA were good, there are still some doubts pending on their fairness. From a sample of 30 finalized cases, 11 were not reached by unanimity; panelists either dissented from the majority or gave concurring opinions or views. Some experts have diagnosed that the way Chapter 19 was designed and operated provokes an asymmetry

of favorable outcomes to the benefit of Canada. This is due, among other things, to the fact that panels normally are bound to apply and respect the standard of review of each country, the Canadian standard being more deferential to trade authorities in some cases than that of the US. Furthermore, in a thorough analysis made by John Mercury on panel decisions under CUSFTA, he also concludes that the manner in which panels formulated and applied each country's standard of review was also decisive to explain the asymmetry of outcomes. Panelists were severely strict when interpreting the US standard of review, and considerably soft when applying Canada's (Mercury, 1995: 552 – 3).

Due to the fact that NAFTA's Chapter 19 is in many ways a copy of the same chapter under CUSFTA, its performance since 1994 has been rather similar.[21] This chapter has indeed corrected some protectionist biases on administrative agencies of the three partners; however, it has failed to deter strongly rooted protectionist interests in the region, mainly those coming from the US. The saga of the softwood lumber dispute between Canada and the US epitomizes the nature of conflicts involving trade disputes among the partners. US lumber producers have claimed since 1981 that Canadian imports of lumber are subsidized and causing damage to their production. On the grounds of the conflict there are differences in the regimes of land ownership between the two countries and in the political organization of Canadian provinces vis-à-vis US federal states. Although US trade agencies decided in 1983 that timber allocation and stumpage rights were not countervailable, in 1986, once the powerful Coalition for Fair Lumber Imports (CFLI) was created, a renewed file submitted to the US Department of Commerce (DOC) found that both the allocation of timber and stumpage fees were provided on a discretionary and specific basis, and were hence countervailable.

Canada has since alleged that stumpage fees are a matter of public and development policies, and that US agencies cannot decide how provincial governments must manage their natural resources. Anticipating the final decision of the Department of Commerce, the Canadian government decided to sign a Memorandum of Understanding (MOU) under which a tax of 15 per cent was imposed on Canadian softwood lumber exports, and that was terminated in late 1991. The DOC subsequently initiated its third countervailing investigation, which, as expected, was affirmative. This time Canada decided to challenge the US decision under Chapter 19 of the CUSFTA (see Ek, 2001; Gagné, 1999). Panels reviewed and remanded both the DOC's decision on subsidy and the ITC's decision on material injury. In the case of subsidy, panelists did

not find that Canadian stumpage fees were provided on a specific basis, nor did they find that the ban on exports of logs from British Columbia had specific benefits for considering it a countervailable subsidy. However, US agencies confirmed their positions, leading to a second remand from the panelists. The second remand confirmed the panel's original position, but this time panelists were split along national lines.[22] The US finally activated the ECC and the judges confirmed the panel's decision although not by unanimity.

As for the test of injury the panel awarded that there was no evidence, according to US laws, that Canadian lumber imports were damaging the US industry. This decision had to be remanded two more times before the US agencies finally accepted it, without any split in the members of the panel. These two awards provided evidence that the definitions of 'subsidy' and 'injury' in US law and practice had become so flexible as to accommodate almost any petition for a trade relief (Gagné, 1999: 85).

However, the role of the CUSFTA panels could not avoid the politicization of what had already become the most sensitive trade dispute between the two countries. The US government invoked Section 301 of the 1974 Trade Act in order to force a deal with the Canadians. Once the dispute was handled under the CUSFTA mechanism, proceedings were initiated in order to challenge the constitutionality of the panel's decision under US courts. Once panels finalized the case, the US government delayed the reimbursement of duties collected, and the CFLI threatened to open the case as soon as possible. All these political pressures ended up with the signing, in 1996, of a new ad hoc agreement through which lumber exchange between the two countries became subject to a tariff-rate quota.[23] The agreement contemplated its own dispute settlement mechanism which permitted contending parties to circumvent the dispute mechanisms of the CUFSTA and NAFTA.

The five-year peace agreement expired on March 31, 2001, and in early 2002 the DOC announced again an affirmative determination of dumping and subsidies against softwood lumber coming from Canada. In April 2002, the Canadian government requested a panel review under NAFTA challenging the US final subsidy and antidumping determinations. In January 2003, the WTO established another panel at Canada's request to resolve on the methodology used by the DOC in determining the margin of dumping. All panels have remanded in part US final decisions and methodology. A NAFTA panel found, for instance, that US ITC determination was unsupported by 'substantial evidence and inconsistent with US law' (cf. www.international.gc.ca). Since the US resisted bending completely to what panels have awarded, either by using appellate

mechanisms or by simply inducing panelists to remand previous remands (see Anderson, 2004; Inside US Trade, 2004), an ad hoc agreement was finally reached in April 2006. Through this ad hoc agreement, Canadian exports are subject to a tax collected by the federal government if prices fall below an agreed upon floor price.[24]

Many other trade-related disputes have emerged among NAFTA partners without being resolved under the formal dispute settlement mechanisms. Take for example the tomato and avocado disputes between Mexico and the US, or the Helms Burton Law that involved both Canada and Mexico against the US. In the first case price and quota undertakings – to some extent similar to those agreed under the softwood lumber case – were negotiated. In the second one, consultations were activated under Chapter 20, and the White House eventually declined to enforce the extra-territorial consequences of the law.

As anticipated, Chapter 19 of the NAFTA inherited the genetic problem of the CUSFTA that affected the interpretation and procedures of the so-called standard of reviews. This time the Mexican standard, practices and legislation had to be added to the process. The Mexican cases concerning Imports of Flat Coated Steel Products (MEX-94-1904-01) and Imports of Cut-to-Length Plate Products (MEX-94-1904-02) from the US have been some of the most controversial. Though the two cases presented similar features – review of antidumping determination by the Mexican administrative agency – and the complaining companies argued their points on similar bases, the final award in each case was quite different. In the first case, terminated long after the second one, panelists remanded in part the Mexican decision, but affirmed unanimously that the Mexican authority imposing dumping duties was legally constituted. By contrast, in the second case, the panel decided by majority that the Mexican decision was against its Constitution, because the federal agency lacked the authority to impose the duties. Yet the terms of the award were not in the sense that Mexico's Trade Ministry had to remand in totality its decision, but rather to abrogate it, as the Fiscal Federation Tribunal – the domestic tribunal substituted by the panel – would have done if they had reached the same decision. The two dissenting votes opposing the majority highlighted that panelists were exceeding their faculties as strictly framed by Chapter 19.[25]

The steel case concerning Mexico's antidumping determinations reinforces John Mercury's hypothesis in the sense that the differences in the standard of review, and the different manner in which they are interpreted, could create a bias on panelists' decisions in the wrong way, that is, to the detriment of a fair position that loses its legitimacy by a

skillful manipulation of the law by a complaining party. The contrary could be argued, in the sense that panelists still are learning from this process, and that the more predictable their procedures become, the more reliable panels under the Chapter 19 will be. The problem here is that panels do not create any precedent and jurisprudence. This is in fact a real limitation of the whole mechanism.

Although NAFTA panels under Chapter 19 have worked pretty well, from year 2000 it has become more and more difficult to conform them and make them work. The main reason for this is that panelists are not well paid, and in many cases they have had to renounce because of alleged conflicts of interests. This has provoked serious delays for the establishing of panels as well as for making their final awards.[26]

## Improving or 'deepening' NAFTA's institutional mechanisms

Apart from specific issues concerning natural resources in Canada, and US trade relations and trade in services (the case of transport between Mexico and the US), NAFTA's institutional machinery has proved to function well for the goals that it was created for: to discipline state involvement in specific issue areas (market access, government procurement, capital mobility, protection of corporate property rights, among other things) in order to empower market actors, although sometimes to the cost of important public policies, as witnessed by the record of Chapter 11. By so doing, NAFTA is setting specific benchmarks – or 'good governance' practices – ensuring anticipated or desirable outcomes from state-market relations. Within this institutional setting, Canada and Mexico have been the countries that have had to adapt more to this leveling of the playing field pursued by Washington since the decade of the seventies. For Canadians, CUSFTA–NAFTA meant the end of state-led industrial policies followed during the Trudeau years. For them, a 'pooling' of sovereignty in trade and investment issues have been the cost to pay in order to make more predictable the access to the US market.

Mexico without doubt became the laboratory in which this legalistic, disciplinary machinery was internalized, with the aim of transforming previous state dirigisme. It is true that Mexico's institutional transformation of the state started before NAFTA, but it is not less true that the new disciplinary body locked in previous reforms, and that deepened and accelerated the demise of state interventionism. The way Mexico joined NAFTA illustrates well how this new disciplinary machinery

operates: institutional change was not the outcome of an imposition, or of Mexico's submission to a hegemonic agenda. It was construed as a means to release market mechanisms from inefficient and corrupted state control in order to increase welfare gains. It was not the demise of the state but its radical transformation into a regulatory agent according to good governance practices.

The premise and the promise of this radical transformation became appealing to multiple Mexican constituencies whose interests and expectations were anticipated to be better satisfied with this new role of the state. Firms, market actors, technocracies, urban professionals and middle classes coalesced, tacitly or implicitly, to create what some called the 'demand' for an international regime. NAFTA's legal disciplinary body emerges and circulates thanks to this releasing message: it doesn't build a repressive machinery, it rather empowers rights and entrepreneurial capabilities by reshaping the scope and nature of state actions. This very same formula has been used by Washington with the rest of LAC countries for expanding NAFTA-like agreements although with less success, as will be reviewed in the last chapter of this book.

In other words, NAFTA's disciplinary machinery becomes powerful for producing anticipated or desirable policy outcomes not only because of its own institutional design, but also due to the support of specific or diffused stakeholders that anticipate positive expectations by sticking to the disciplinary mechanism. This was proved during the Mexican peso crisis at the turn of 1995, that is, one year after NAFTA came into force. Mexico's political and economic elite preferred to use more of the same medicine (state downsizing and liberalization) as a means to overcome the financial crisis.

Nonetheless, after more than 14 years of operation, NAFTA's institutional mechanisms have proved their own limits. In recent years, academics and specialists have warned about the institutional loopholes and restraints of the agreement. Here I summarize the major ideas nourishing this debate according to the nature of the problem they address.

## Institutional reforms gearing to the reduction of transaction costs

Most of the ideas and suggestions pleading for NAFTA's institutional reform aim at further lowering transaction costs in what I call in the next chapter the emerging North American economic space. Suggestions range from the most specific to the widest. The need to suppress, as much as possible, the use of rules of origin is an example of the former. For by so doing, NAFTA members could eliminate them in those

tariff schedules where the three NAFTA members' MFN tariff falls within plus or minus one percentage point of the average of the three countries (Hufbauer and Schott, 2005: 475). NAFTA members could also decide for a wider option: to move to a Customs Union. As a Customs Union, NAFTA parties should stick to a Common External Tariff (CET), something that could be problematic, taking into account that all three members are now engaged in multiple FTAs with third members. Some authors suggest that this could be done on a sectoral basis, by building CETs in those areas where MFN tariffs are already very low in all three countries. The need to move to a Customs Union has been echoed mainly by Canadians and American specialists, hoping to eliminate the costliness of rules of origin and to consolidate the borderless economic space that the security imperatives threaten to fragment after the terrorist attacks of 2001 (see Hart, 2004; Dobson, 2002).

Another set of suggestions and ideas aim at improving the working activities of the arbitration panels. Most of the problems witnessed by the operation of those panels, mainly for Chapter 19, stem from the fact that panelists are not permanent, are not well paid and have to renounce because of alleged conflict of interests. The creation of a permanent, well-paid roster of panelists, serving on all NAFTA cases, for a period of six years has been suggested. By so doing, panelists will become familiar with the various standards of review encompassed by the agreement (Hufbauer and Schott, 2005: 249; Vega et al., 2005: 302–6).

However, the major institutional constraint shown by NAFTA is that its institutional design is not prepared for abating second and third generation of non-tariff barriers. The respective sagas of the softwood lumber and transport cases are there to prove it. As long as the continental economic space becomes more integrated, this type of structural non-trade barrier shall become more apparent. Unless NAFTA parties agree to harmonize their respective trade remedy laws by creating a sort of permanent trade tribunal, the only way to overcome these impediments is the negotiation of sectoral deals, as witnessed by the long record of softwood lumber. Managed trade policies and sectoral negotiations are taking place in parallel to the institutions created by NAFTA in the realm of transport, cement, automobile, steel and energy in order to overcome institutional differences and other types of barriers. These sectoral negotiations have become the pillars for increasing the so-called 'competitiveness of the region' in a new strategy called the Security and Prosperity Partnership (SPP), to be reviewed in Chapters 5 and 6 of this book.

## The need for 'institutional deepening'

A set of specialized opinions is geared towards the creation of NAFTA institutions in their own right. Robert Pastor has suggested, for example, the creation of a North American Commission (NAC), staffed by a mix of civil servants and independent professionals. Conscious that NAFTA pursues a different pattern of integration to that followed by Europe, especially in the sense that Americans are not keen on the creation of strong bureaucracies, let alone supranational institutions, Pastor calls, however, for a robust NAC entitled with the mandate to move North America beyond just the sum of two bilateral relationships.[27] The need to have independent headquarters has also been raised.

If economic integration is to be deepened, the need for creating a common legislation on trade remedies has become pressing. This is a position reflecting mainly Canadian, and to some extent Mexican, interests, since many of the cases lost or won within Chapter 19 disputes are linked to the differences still existing among national legislations. Michael Hart has openly suggested moving into a single trade remedy regime (at least between Canada and the US) on a piecemeal basis, i.e. by exempting from trade remedies those sectors which for a span of time have not had cases (Hart, 2004: 44). Hufbauer and Schott (2005: 251–2) have even suggested the eventual cancellation of Chapter 19, if the three parties progressively find it more convenient to bring cases before the WTO, where trade remedies are judged according to multilateral codes and agreements. The creation of a common Investment Tribunal or moving towards the creation of a monetary union are other proposals that have been put on the table.

## Go for a 'strategic package'

In all three countries a set of academics and officials are conscious that the only way to move North America from where it stands now, that is, a simple FTA betting to a disciplinary governance of market openness, regardless of the economic, social, and political imbalances prevailing in the region, is to strike a sort of 'strategic package', a Great Bargain, or Big Idea in order to build a trilateral community addressing common and sub-regional problems (see Pastor, 2001; Dobson, 2002; Hart, 2004; CCCE, 2004). The key factor in any great proposal is to get the interest and support of the strategic partner, the US. As long as political and economic asymmetries prevail in the North American space, the sponsorship of Washington remains crucial.

There is not yet a consensus around which renewed expectations on North American integration should converge; so far, each country has

pushed for its own agenda. Mexico became in fact the first country to make the first step forward, when the Fox administration articulated what he called a 'NAFTA-plus' approach. Mexico's 'Big Idea' of the time was based on labor mobility and development policies geared to the reduction of inequalities (see Chapter 4). After the September attacks of 2001, the US great project for prompting the political collaboration of its NAFTA partners was the launching of the smart borders approach, which eventually saw the emergence of a new security regime anchored on what has been called the Security and Prosperity Partnership (SPP) (see Chapter 5). As for Canadians, fearing a sort of 'mexicanization' of their own front line, they have moved to a policy of 'economic security' through which they attempt to maintain fast, free, secure and cheap access to the US market while enhancing Canada–US security cooperation without compromising Canadian military and diplomatic autonomy (see Chapters 5 and 6).

# Part II

# The Post-NAFTA North American Economic and Social Space

# 3

# After NAFTA: Trade Regionalization and the Emergence of a North American Economic Space

## Introduction

NAFTA not only introduced a disciplinary benchmark among state participants, but it also conveyed a 'policy shock' in the region; that is, once firms and market actors realized the complete phasing out of barriers to both trade and investment and the new market-oriented disciplines of the game, they had to adapt their production and market strategies accordingly. This chapter will explore some of the impacts entangled by this policy change conveyed by the disciplinary regime, mainly in terms of a further regionalization of trade and, to a lesser extent, investments, and in terms of the locational advantages of trans-border regions within North America.

In this Chapter I argue that the Post-NAFTA emerging economic space clearly features the consolidation of a continental hub, where the intensity of trade exchanges and specialization is most concentrated. This continental hub, conformed by the provinces of Ontario and Quebec, in Central Canada, and the US region going from the Great Lakes up to New England, concentrates more than 50 per cent of overall Canada–US exchanges and hosts many of the most global and dynamic metropolises in North America. This hub is clearly connected with two major spokes in the southwest American border, mainly conformed by the states of Texas and California, which function as interface with most two-way trade coming from central and northern Mexico.

Canada's and Mexico's trade and production (and probably labor) specialization have become functionally continentalized under the aegis of MNCs operating in the region, as depicted by the role played by both

intra-industry and intra-firm cross-border trade. Within this functional space, Canada plays a major role both as a high-tech competitive partner and a major reservoir of competitive and/or strategic primary resources (forest, water, oil and gas, agricultural products), while Mexico is consolidated as a space of manufacturing relocation and as a major reservoir of 'competitive' cheap labor force, as witnessed by the composition of *maquiladora* exports and the growing immigration of Mexican workers, either legally or not, to the US.

This chapter also argues that in parallel to this continental specialization and networked configuration, a kind of 'periphery' is looming in the North American landscape. This periphery features lagging industries, mainly agricultural activities, and populations that have become vulnerable to disembedded market changes unleashed by NAFTA. This periphery is located in Mexico's southern states, and will probably become enlarged towards Guatemala, El Salvador, Honduras, and Nicaragua, as a consequence of US-DR-CAFTA.

## The regionalization trend: commercial and investment flows within North America

It can be said that trilateral integration in North America started in the mid sixties, when Canada and the US signed the Auto Pact deal, and Mexico and the US started, in the same year (1965), the *maquiladora* program. This was the equivalent to a 'policy shock' for both Canada and Mexico (Eden and Monteils, 2000), since firms and markets had the stimuli for orienting their production from the domestic to the US market. In the case of Canada, the Auto Pact meant the de facto integration of the automotive industry between the countries commanded by the three major US assemblers: Ford, General Motors and Chrysler. This meant the reorganization of production by US MNCs in which the Canadian market was not only part of its strategy of expansion, but a platform for relocating mid- to high-tech chains of their production, for exploiting market contiguity and economies of scale (see Studer, 2001). In the case of Mexico, the *maquila* program aimed at exploiting the low-skilled labor surplus in Mexican territory, and closeness to dynamic US markets in the southern border, in order to assemble manufactured products in Mexico for re-export to the US, only paying taxes for the value added in Mexico.

That first move towards integration led to the emergence of border economies, sealing in some way the destiny of the two countries. Dynamic markets and economies of scale led to the regionalization of production in the northern borderlands of the US, and locational and

costs advantages led to regionalization of production in the borders of the south. This new pattern of regional production modified the nature of bilateral exchanges between the US and Canada, and the US and Mexico. In the first case, trade concentration and intra-industry specialization became an irreversible trend. During the first part of the twentieth century, the United Kingdom still remained the principal trade partner of the Canadians. During the second part of that century, the US market took the primacy. The second wave of regionalization, starting in the mid eighties when Canada and the US entered into free trade negotiations, accentuated this pattern of concentration and specialization.

As for Mexico–US trade relations, the American market has become a sort of destiny for the Mexicans. In spite of attempts at diversifying trade relations during the seventies and eighties, Mexican commerce has become more concentrated with the US and *maquila*-based exchanges for almost half of Mexico's overall exports. Mexico has consistently remained a space of cheap labor supply and production in the continental economy. However, the country has proved to develop a pattern of intra-industry specialization during the past 15 years, suggesting that Mexico has already become a platform for relocating mid- to high-tech chains of dynamic industries such as automobile, electronics and machinery.

Figures 3.1 and 3.2 show annual average growth rates (AAGR) in US–Canada commerce ranging from the pre-CUSFTA to the post-NAFTA period.[1] As Figure 3.1 shows, US imports from Canada (that is, Canadian exports) have maintained a similar dynamism before and after the CUSFTA–NAFTA agreements. This is probably explained by the de facto integration that these two countries already had before entering into bilateral and regional deals. In the case of US exports to Canada, Figure 3.2 shows a rather similar trend, although rates of growth slightly decreased (in 1 per cent) in the post-FTA period. However, several studies analyzing bilateral trade at the disaggregated level confirm that two-way trade has increased more in those sectors where tariffs were cut the highest. Economists have estimated an 11 per cent increase on US imports for each drop of one percentage in the average tariff rate. Some authors have estimated a 3.2 per cent cumulative increase in Canadian imports coming from the US for one percentage of Canadian tariff reduction for the period 1989–96 and a 12.4 per cent increase of Canadian imports for the whole period. As for Canadian exports to the US, the same authors estimate a 24 per cent increase explained by US tariff reductions for the same period. The larger impact on Canadian exports compared to imports is explained by the bigger size of the American market compared to that of Canada (Helliwell et al., 1999: 24).

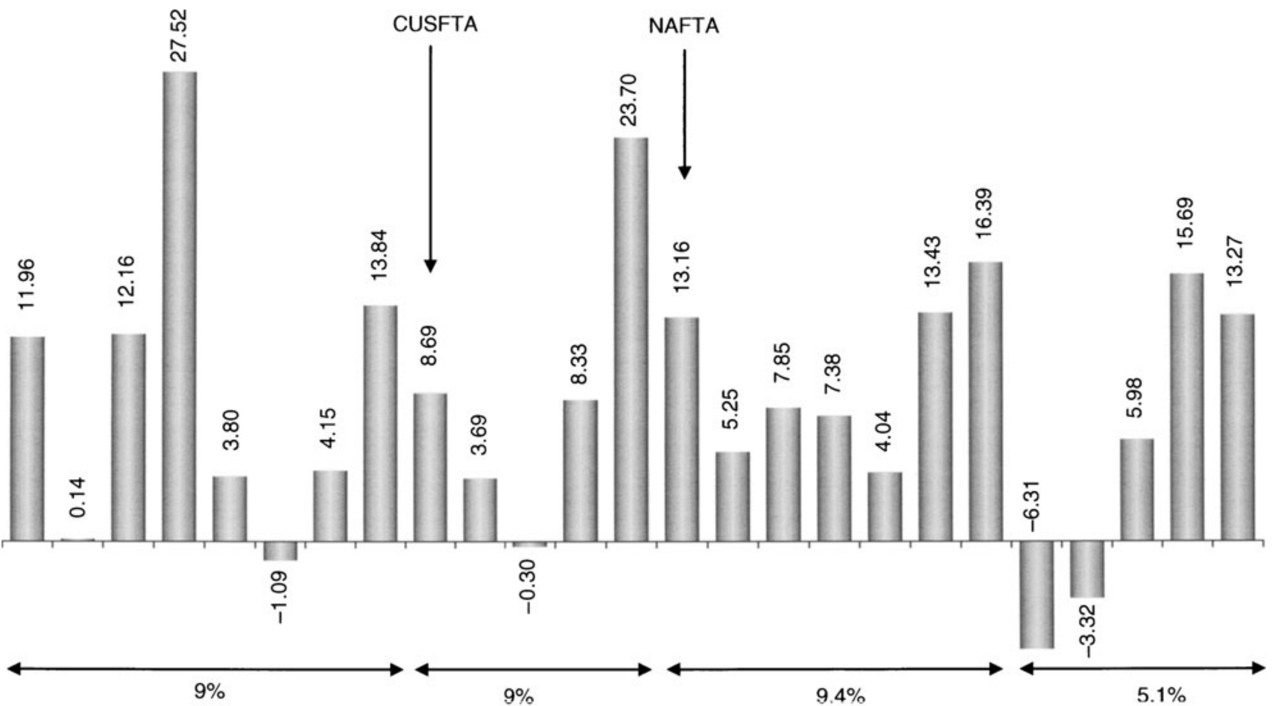


*Figure 3.1* Annual rate of growth of US imports from Canada, 1981–2005

*Source*: US Department of Commerce

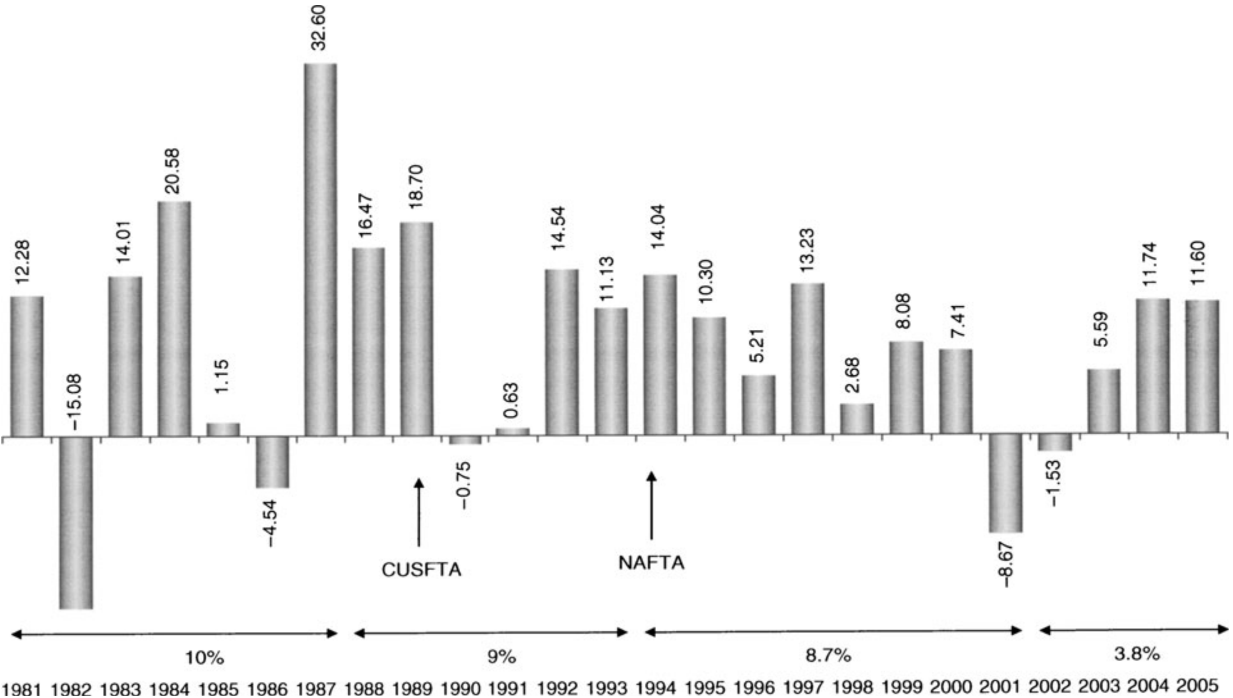


*Figure 3.2* Annual rate of growth of US exports to Canada, 1981–2005

*Source*: US Department of Commerce

Canada has remained a major resource-based exporting economy, since shares in the composition of manufactured exports have not changed substantially. In 1980, 9.7 and 20 per cent of overall exports to the US came respectively from the machinery and automotive branches, while in 2005 those shares reached 10 and 24 per cent. Figure 3.3 shows the current composition of both US imports from and exports to Canada. Primary and primary-based products[2] represent roughly 40 per cent of overall Canadian products entering the US (agriculture, food, cement, mineral fuels, wood, and footwear), while the rest is manufacturing, encompassing all gradients of technological sophistication (from low- to high-tech branches). However, branches that normally contain mid- to high-tech chains, such as transport equipment, machinery, chemicals and plastics, account for 44 per cent of overall US imports. The fact that Canada has become a major energy powerhouse in North America since the last decade, due to the successful development of bitumen and synthetic oil, explains why the resource sector remains heavily important in Canada–US trade.[3]

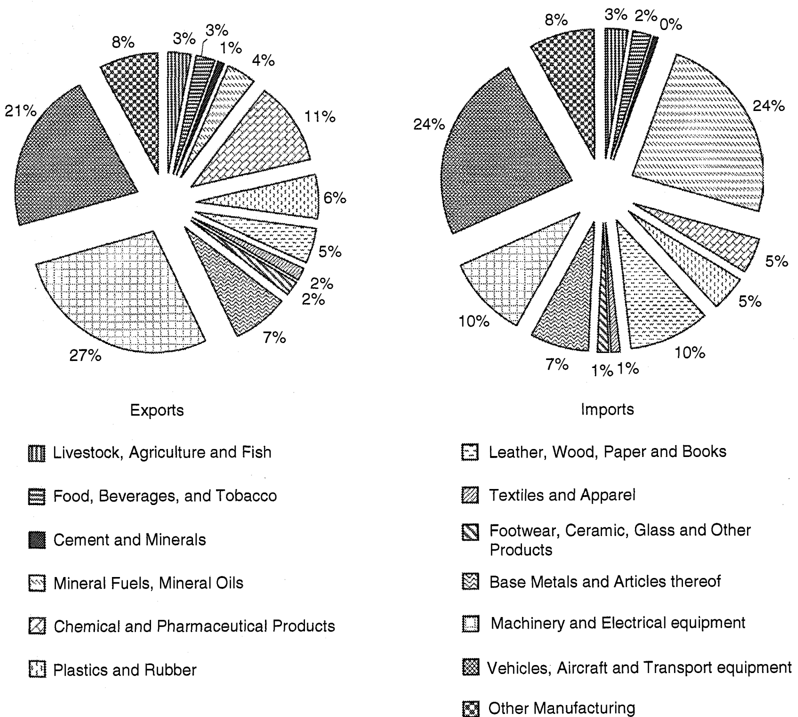


*Figure 3.3* Composition of US exports to and imports from Canada, 2005

As for the composition of US exports to Canada, primary and resource-based products take a minor share (roughly 18 per cent) while mid- to high-tech manufactures account for 65 per cent of overall exports. Needless to say, a pattern of production and trade specialization has been established between the two economies and certainly reinforced in the post-CUSFTA era. Figure 3.4 shows the different performance of main traded-branches. Regarding US imports, resource-based and low-tech products have led the post-CUSFTA growth, with mineral fuels and textiles and apparel[4] taking the lead. In high-tech branches plastics and chemicals have performed far above the overall AAGR of US imports (8.3 per cent). Key sectors such as transport equipment and machinery have performed at lower rates. Interesting to observe is that these very two branches grew at higher rates than overall imports in the pre-CUSFTA period, suggesting perhaps that intra-industry trade between the two countries is more responsive to the business cycle of particular industries than to the elimination of remaining tariffs.[5]

As for US exports in the post-CUSFTA period, high-tech products take the lead, plastics and chemicals witnessing among the highest Annual

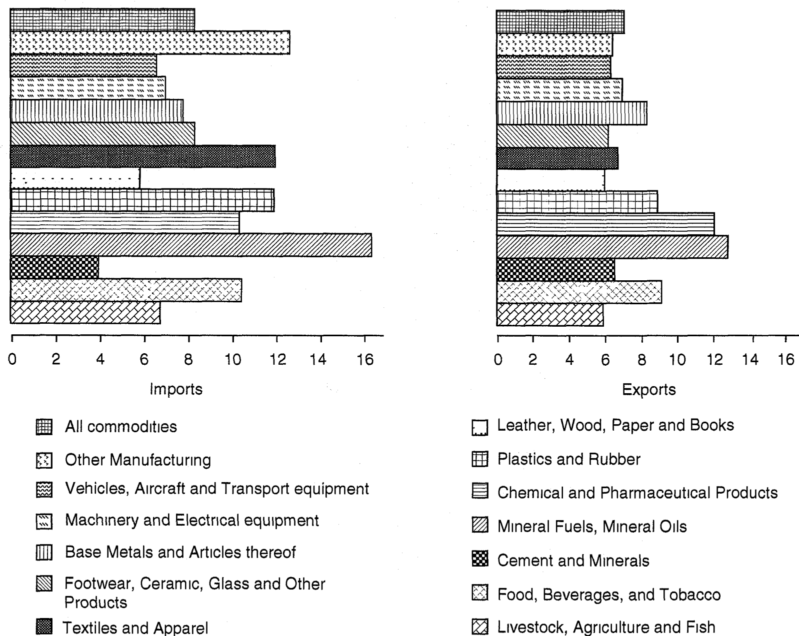


*Figure 3.4* Average rate of growth of US exports to and imports from Canada, 1991–2005

Average Growth Rate (AAGR). Processed food has also performed well, while cement and minerals are the lagging sectors in both US imports and exports. Specialized studies have suggested that post-NAFTA trade between the US and Canada is mainly explained by changes in quantities imported and exported, rather than changes in prices or increases in trade attributable to a growing number of traded varieties.[6] In other words, intra-industry exchange and product differentiation is a major feature of US–Canada commerce in the mid- to high-tech manufacturing sector, while the latter country keeps its leading role as a resource-based manufacturing supplier for the US.

As for US–Mexico trade evolution and composition, Figures 3.5 and 3.6 show AAGR for the pre- and post-NAFTA period. At first glance, it seems that NAFTA has impacted more on Mexico's trade than Canada's, at least if we compare the evolution of US imports from the former country (Figure 3.5). This could be explained by two reasons: in contrast to Canada, Mexico was a closed economy until the mid eighties and US average tariffs for Mexico were higher than those prevailing for Canada. Four periods are clearly shown in Figure 3.5, the 'pre-GATT', 'post-GATT', 'post-NAFTA' and the 'post-recession' period at the turn of the century. AAGR are higher in each succeeding period (except the last one), suggesting that the more open the economy the more responsive to trade creation it became. Mexican exports were revitalized once the country joined the GATT. A similar conclusion can be drawn for the post-NAFTA years.

Nonetheless, some caveats must be taken into account. The pre-GATT years are difficult to take as a reliable reference, because three major financial crises – the debt default of 1982 and the oil bust of 1986 and the further peso devaluation of 1987 – affected all macroeconomic performance during that period. As shown in Figure 3.6, depicting US exports to Mexico, they decreased at an average rate of 1 per cent during that period. So the post-GATT years rather show the recovery of an economy after witnessing two major external shocks in the first part of the eighties. GATT helping, this could explain why US imports grew two-fold during those years and Mexican imports witnessed an increase of 20 per cent annually, a rate that the post-NAFTA years have not matched. The GATT years are also signaled in Mexico by the consolidation of major changes on economic policies, trade liberalization, privatization and fiscal control being their major features. The NAFTA years feature an increase in US imports, compared to the GATT years, but a slower growth in exports, suggesting once again, that trade liberalization in itself is not the only factor impacting trade performance. In fact, a sharp devaluation at the end of 1994 and beginning of 1995 impacted both imports and exports. A probable under-valuation of the peso helped to

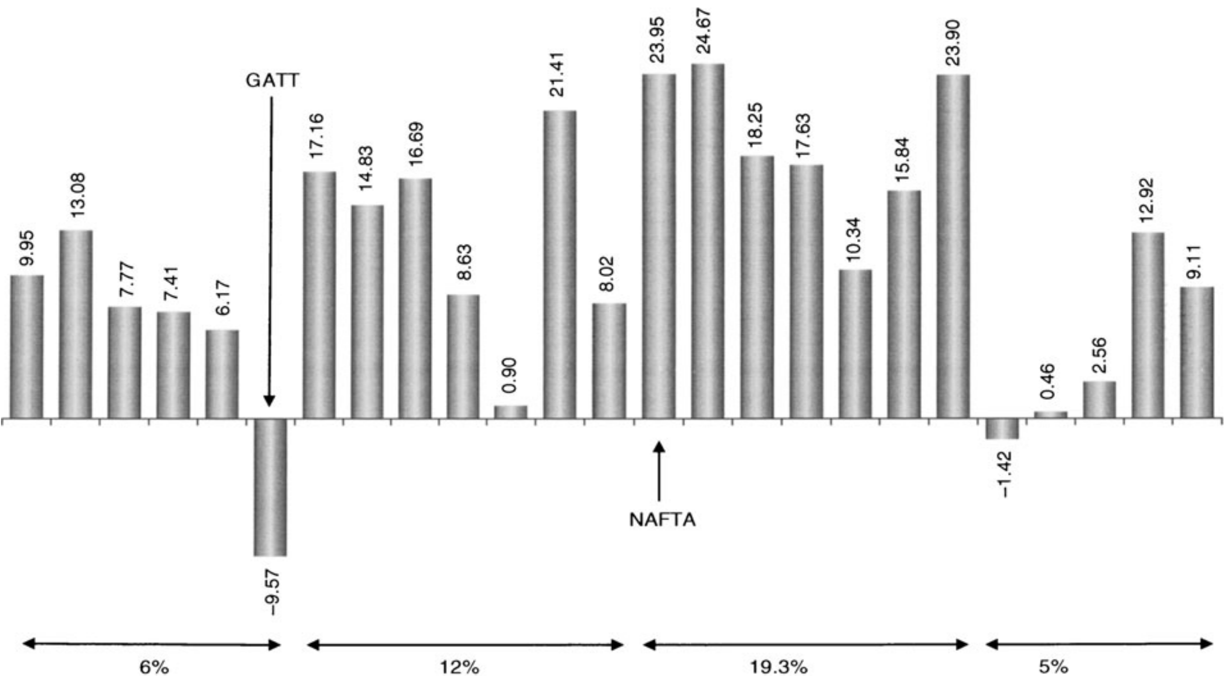


*Figure 3.5* Annual rate of growth of US imports from Mexico, 1981–2005

*Source*: US Department of Commerce

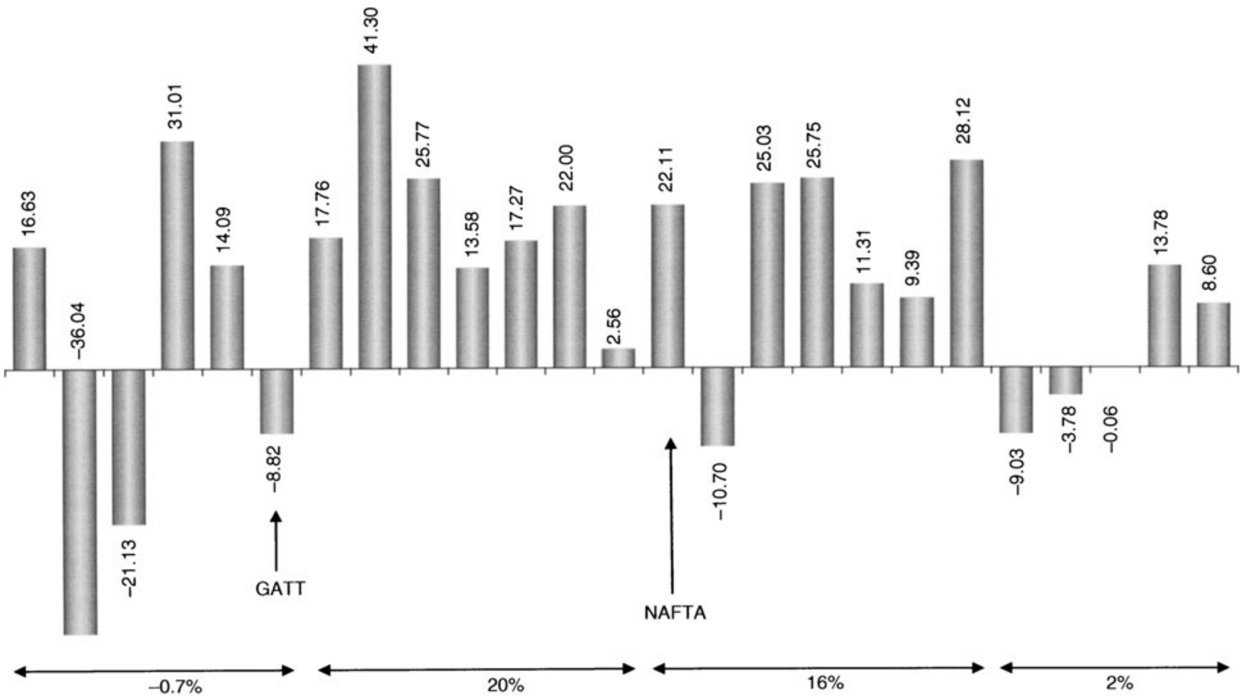


*Figure 3.6* Annual rate of growth of US exports to Mexico, 1981–2005

*Source*: US Department of Commerce

boost Mexican labor-intensive exports, although recent studies have suggested that a 50 per cent increase in overall US imports coming from Mexico is attributable to NAFTA (Lederman et al., 2005: 2). This means that the impact of NAFTA in trade creation for Mexico has been higher than that provoked by CUSFTA in the Canadian economy. Other studies have suggested that Mexico's trade performance has rather become linked to the US business cycle since it joined the GATT, minimizing the impact of the NAFTA deal in trade performance (Montenegro and Soloaga, 2006). In fact, since 2001, as witnessed in the two figures, trade between the two countries slowed down, showing the impact of US recession on its southern neighbor, similar to what happened with US–Canada commerce. This might suggest that the 'NAFTA-effect' (in terms of trade creation) is already over, and that North American trade will respond rather to the overall evolution of the US economy.

While in 1980 63 per cent of US imports from Mexico were mainly mineral fuels (52 per cent of total imports) and other primary related products, in year 2005 the import mix changed dramatically: 23 per cent were only primary and primary-based products while the rest included manufacturing (see Figure 3.7). If we compare the import mix with that of exports, we could say that during the past 20 years Mexico moved from a typical North–South exchange with the US (primary goods against manufacturing), to a rather intra-industry pattern of exchange in the mid- to high-tech ranges of manufacturing, similar to what prevails in US–Canada exchanges. This is mainly the case within the transport and machinery industries of the two countries, where parts and inputs are traded between the two economies.

Recent studies suggest that Mexico's export competitiveness has increased, during the past 15 years, precisely in the non-resource-based sectors. As shown in Figure 3.8, depicting US imports from Mexico, among medium-tech sales the plastics branch has witnessed the most impressive growth from 1994 to 2005. With an AAGR of 17.3 per cent, exports coming from this sector have performed above the AAGR in overall exports, which was 13.2 per cent for the same period. The automotive sector has also performed well (14 per cent AAGR), being the most dynamic mid- to high-tech sector during the years 1994–2000. The electrical and non-electrical machinery branch witnessed an AAGR of 13.1 per cent. Traditional sectors such as mineral oils, primary metals and textiles have, however, witnessed some of the highest AAGR for the whole period (17.9 per cent, 15.3 per cent and 15 per cent respectively). Exports of chemicals have also increased, but at lower rates than overall manufacturing exports. As for US exports to Mexico, mineral fuels

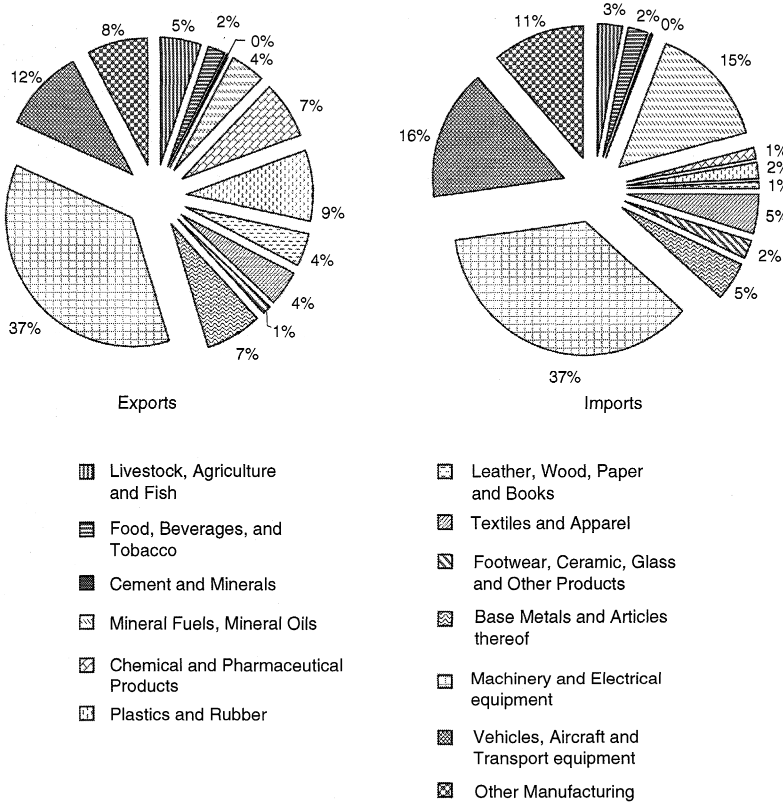


*Figure 3.7* Composition of US exports to and imports from Mexico, 2005
*Source*: US Department of Commerce

witnessed the highest AAGR for the overall period, no doubt witnessing the sudden increase of Mexican imports of natural gas and gasoline due to the problems affecting the energy sector of this country.[7] Notwithstanding, chemicals, plastics, and primary metals grew at 16, 15 and 13 per cent respectively, suggesting that a pattern of production and trade specialization between Mexican and US firms is already in place. It is worth noting, however, that US exports of agriculture and livestock have grown above AAGR, reflecting the crisis of Mexico's traditional agricultural sector.

Mexico's market shares within the North American market have increased. Table 3.1 shows that non-resource-based manufacturing increased its share in the North American market from 2.9 to 10.6 since the post-GATT years. Competitiveness increased throughout the overall

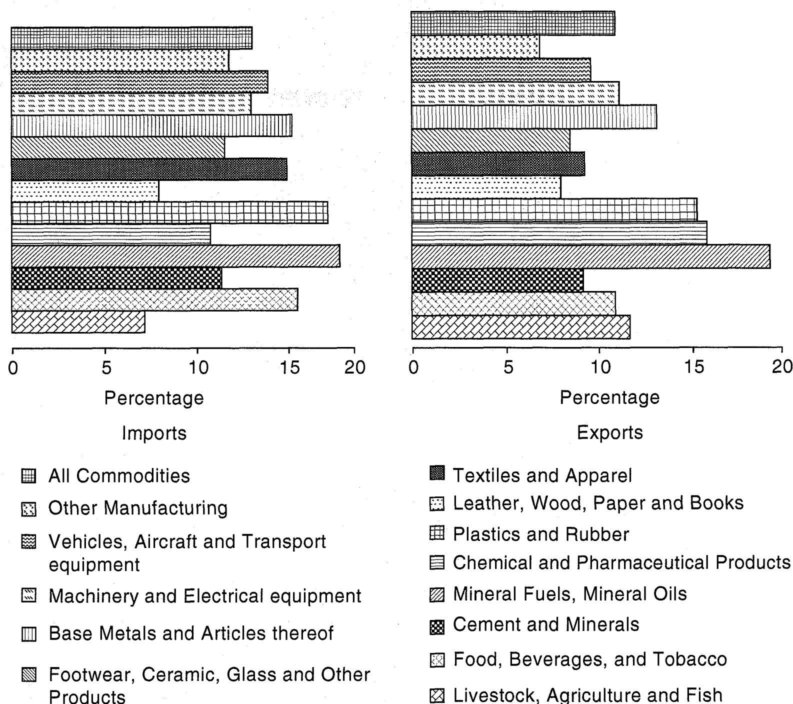


*Figure 3.8* Average rate of growth of US exports to and imports from Mexico, 1994–2005

*Source*: US Department of Commerce

technological gradient of manufacturing. By contrast, primary product exports – mainly oil – decreased their market share (UNCTAD, 2002: 175).

Low-skilled, labor-intensive exports have also witnessed a great success during the past years. The *maquiladora* industry is without a doubt one such success. The goal and raison d'être of this program was to employ cheap labor in assembling activities, in order to discourage illegal migration to the US. *Maquiladora* exports currently represent 45.5 per cent of all Mexican gross exports. Excluding oil exports and taking into account only exports in manufacturing, *maquila* amounts to 55.6 per cent of the value. Furthermore, AAGR have been 1 per cent higher in *maquila* than in non-*maquila* exports during the post-NAFTA years (14 per cent against 13 per cent, respectively), illustrating that the dynamism of Mexican exports has remained anchored in cheap assembly production.[8] Needless to say, this sector is one that has benefited most from exchange-rate fluctuations, mainly after major peso devaluations

*Table 3.1* Mexico's competitiveness in the North American market, 1985–2000

| Product | 1985 | 1990 | 1995 | 2000 |
|---|---|---|---|---|
| **1. Market share** | **4.5** | **5.1** | **7.2** | **9.5** |
| 1. Primary products[a] | 13.0 | 9.5 | 9.9 | 10.4 |
| 2. Manufactures based on natural resources[b] | 3.1 | 2.8 | 3.4 | 3.7 |
| 3. Manufactures not based on natural resources[c] | 2.9 | 4.7 | 7.5 | 10.6 |
| Low technology[d] | 2.1 | 3.4 | 5.9 | 8.8 |
| Medium technology[e] | 2.7 | 5.1 | 8.7 | 11.5 |
| High technology[f] | 4.7 | 5.3 | 7.0 | 10.6 |
| 4. Others[g] | 3.5 | 5.6 | 6.7 | 8.0 |

[a] Contains 45 basic products that are simple to process; includes concentrates
[b] Contains 65 items: 35 agricultural/forestry groups and 30 others (mainly metals, excluding steel, plus petroleum products, cement, glass, etc.)
[c] Contains 120 groups representing the sum of low, medium and high technology
[d] Contains 44 items: 20 groups from the textile and garment category, plus 24 others (paper products, glass and steel, jewellery)
[e] Contains 58 items: 5 groups from the automotive industry, 22 from the processing industry and 31 from the engineering industry
[f] Contains 18 items: 11 groups from the electronics category, plus another 7 (pharmaceutical products, turbines, aircraft, instruments)
[g] Contains 9 unclassified groups (mainly from section 9)

*Source*: UNCTAD, based on the United Nations Comtrade database and the TRADECAN computer software of ECLAC
Cited in: World Investment Report 2002. Transnational Corporations and Export competitiveness. Geneva, 2002, page 175

in 1987 and the end of 1994. However, imports have maintained the same pattern of growth.[9] This increase in imports reflects the very nature of this type of industry, that is, that it mainly focuses on using Mexico's cheap labor. Since Mexico has maintained a surplus in its *maquiladora* trade, the major benefits of the *maquiladora* industry have consequently been the creation of jobs and currency income.

Although *maquiladora* is a cheap-labor, assembly-based industry, it is not merely concentrated in low-tech branches. At the end of the nineties, 22 per cent of these assembling plants were located in the machine tools and electronic sectors, and 7 per cent were located in the auto-parts branch. These sectors accounted for 39 per cent and 19 per cent respectively of overall *maquiladora* value-added. As of mid 2002, 82 per cent of overall gross exports came from those branches (INEGI, 1998: 23–35, and Banco de México). Lower-tech *maquiladora* branches such as food processing, clothing, footwear and furniture concentrated 45 per cent of all plants but accounted for 23 per cent of value added and 10 per cent of gross *maquila* exports. Accordingly, assembly plants have also played a major role in Mexico's restructuring of the manufacturing sector,

reinforcing the functionality of the Mexican economy in the North American space: a site of relocation of value chains according to cheap labor and locational advantages.

Closely related to the success of *maquiladora* exports, is the great export performance in Mexican clothing and textile branches. From 1994 to 2005 these grew at an AAGR of 15 per cent, that is, one point higher than that witnessed by the transport sector. Much of this growth is a result of the growing penetration of *maquiladora* activities within these branches, as already stated. It shows however, the competitiveness of these traditional industries, which performed well while the peso was overvalued to the dollar and were very responsive to Mexico's devaluation of late 1994.[10] Another low-tech sector that performed well during this period was that of processed food.

Last but not least, Canada and Mexico 'rediscovered' themselves as trade partners once NAFTA came into force. Imports from Mexico have grown at an AAGR of 14 per cent, while imports from Canada at 12 per cent (see Figures 3.9 and 3.10). However, Canadian imports from Mexico represent 3.5 per cent of overall imports and exports just 0.7 per cent, whereas for Mexico, Canadian imports represent 3.1 per cent

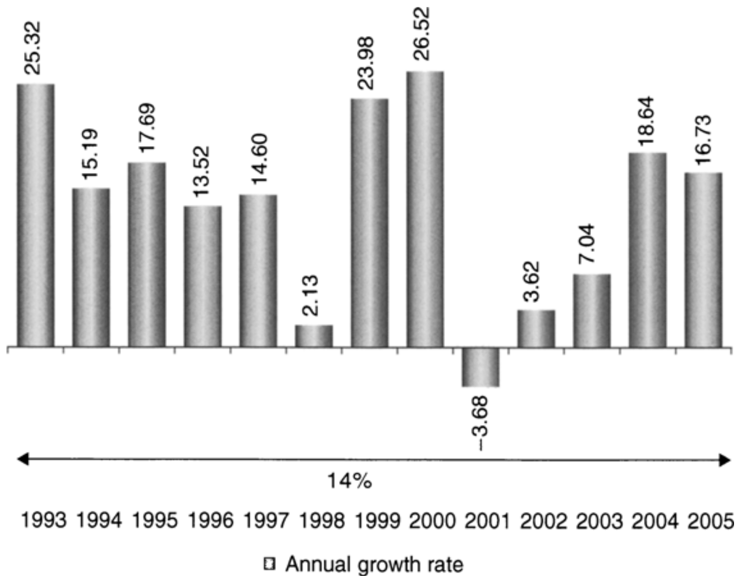


*Figure 3.9* Canada's total imports from Mexico, 1993–2005
*Source*: US Department of Commerce

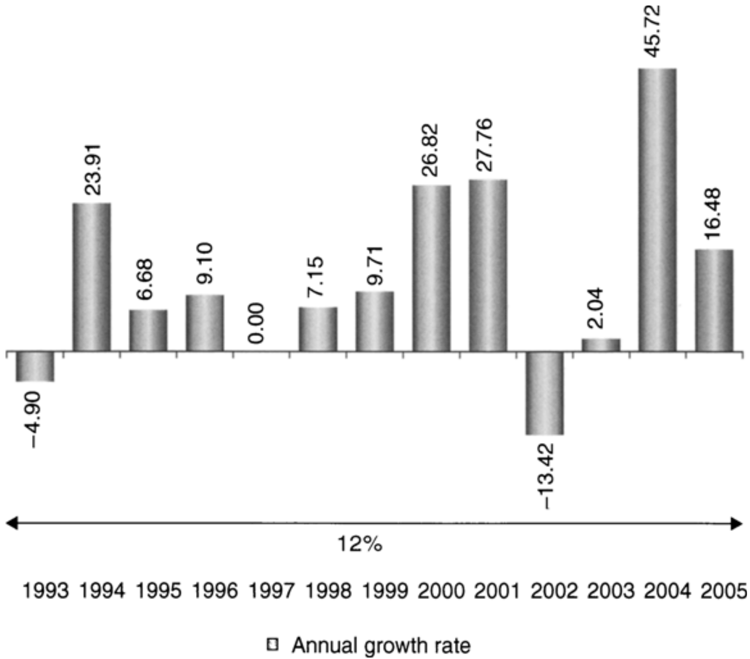


*Figure 3.10* Canada's total exports to Mexico, 1993–2005
*Source*: Statistics Canada

of overall imports and 2.2 per cent of exports. As for trade specialization, Canadian exports to Mexico seem to be dominated by agricultural and automotive products. In the latter sector, it seems that intra-industry specialization already exists between the two countries (see Figure 3.11).

Trade regionalization has become, at the end of the day, a major trait in economic exchanges within North America. This is not only the case of Canada and Mexico, whose major trade partner is by far the US. The US economy has also become inter-dependent with its two border partners. While at the beginning of the eighties 63.6 per cent of overall Canadian trade was intraregional, in 2005 this figure was 77 per cent. For Mexico, this figure was 68.1 and 70.1 per cent, respectively. As for the US, the concentration moved from 22 to 30.7 per cent[11] (see Figure 3.12). However, Figure 3.12 clearly shows that at the turn of the century the trends towards intraregional concentration came to a halt and apparently started to revert, as if a de-regionalization cycle was about to begin. Although the trend is very recent in order to get solid conclusions, it is clear that new entrants in the North American arena

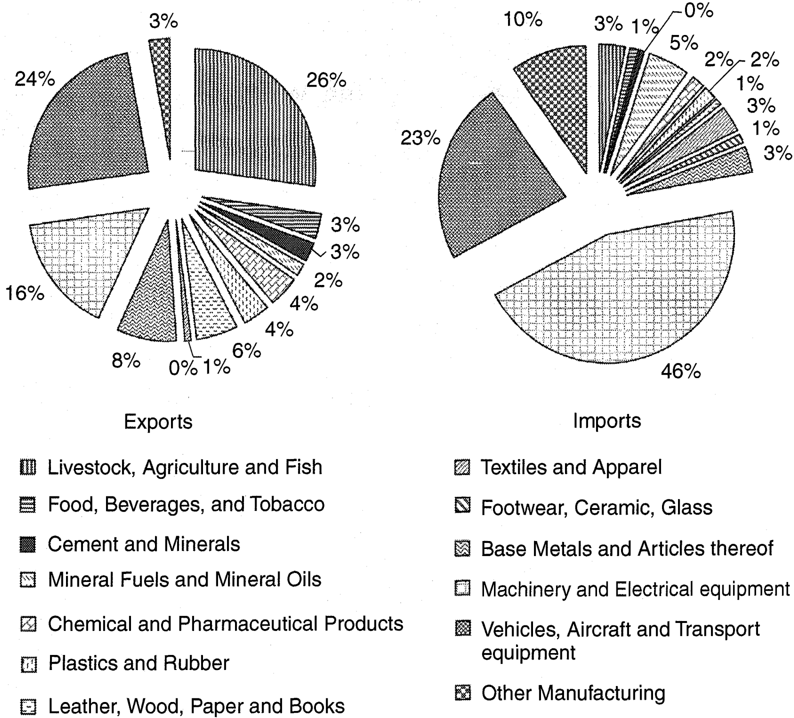


*Figure 3.11* Canada's exports to and imports from Mexico by sector, 2005
*Source*: Statistics Canada

due to the proliferation of FTAs, and the entrance of new members to the WTO, are already eroding the original advantages of NAFTA. The growing share of Chinese exports in the US market, for example, explains in part the shrinking of North American intraregional trade. China increased its market share in the US from 7.8 per cent of overall imports in 1998, to 14.6 per cent in 2005, that is, it almost doubled its share in the span of seven years, displacing Mexico as the second trading partner of the US in 2003. Although the least dependent in this regional trade network is the US, Chinese exports have also helped to reduce US share in the Mexican market. US exports to Mexico peaked in 1997, when they represented 74.7 per cent of overall Mexican imports, while in 2005 this share was just 55.5 per cent. By contrast, Chinese imports have grown from 1.1 per cent to almost 8 per cent during those same years.

So far, Canada remains the main partner of the US, though China could challenge that position if trends continue this way. Needless to say, the US still remains a global player in terms of commercial

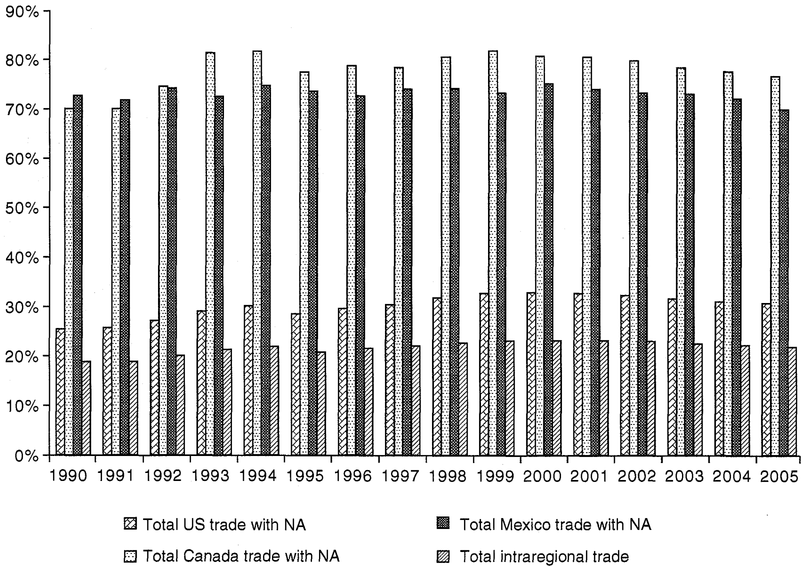


*Figure 3.12* Intraregional trade of NAFTA members, 1990–2005
*Source*: US Department of Commerce, Statistics Canada and Banco de México

exchanges. In fact, the US is the only country whose commercial flows remain evenly distributed throughout the globe. This makes the American economy the hub in the region while Canada and Mexico are its spokes.

## The changing nature of international investment flows

Although the EU remains by far the largest source of foreign direct investment (FDI) flows (both inflows and outflows), North America is ranked second as a major source and destination of investment. Figure 3.13 shows the shares of both inflows and outflows of FDI in the world. It is well known that the main source of these flows is the Triad region. As for the destination of these outflows, the picture is quite similar, although developing countries have a slightly larger share. This shows the high interdependence of the Triad region in terms of FDI and distribution of productive chains. Most of European and Asian investment goes to North America and the other way around.

Within the North American bloc, the US is by far the major source and destination of overall FDI flows. In contrast with commercial flows, where a regionalization of commodity exchanges was a major trend

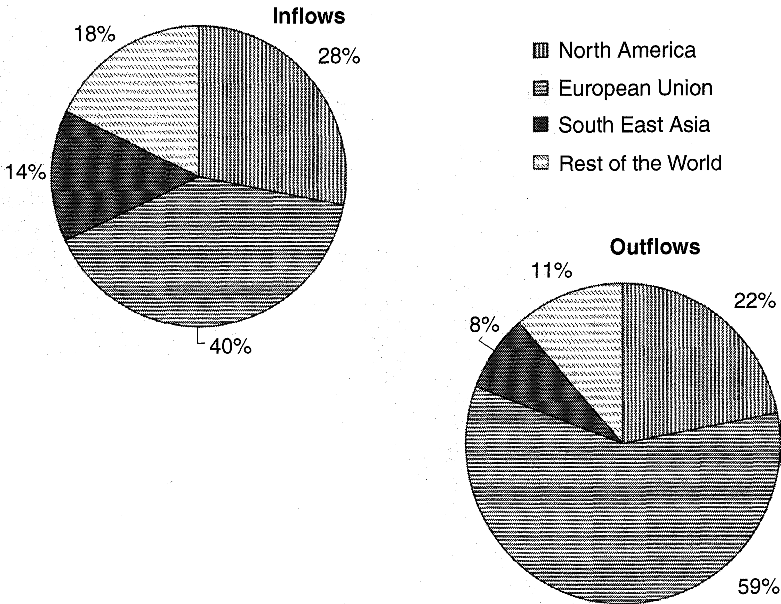


*Figure 3.13* FDI inflows and outflows by main regions, 1993–2000
*Source*: UNCTAD, World Investment Report. Various issues

until very recently, US investment in North America shows a different picture. During the nineties, Europe, and more concretely the EU has confirmed its primacy status as a major source and destiny of investment to and from the US: whereas in 1992 59 per cent of overall FDI in the US, on a historical cost basis, came from Europe (52 per cent from the EU), in the year 2001 the share was 72 per cent (61.2 per cent from the EU). The consolidation of Europe as a major investment partner played against investments coming from South Asia, whose share in overall FDI in the US declined from 26 per cent to 15 per cent (see Table 3.2). By contrast, Canada and LAC countries have maintained, in general terms, their respective shares as a source of FDI in the US: above 8 per cent for Canada and below 5 per cent in the case of LAC countries. Nonetheless, Mexico, a rather needed-country for capital inflows, increased slightly its share as a source of FDI to the US from 0.3 per cent in 1992, to 0.6 per cent in the year 2001.

As previously said, the US is also the major source of FDI outflows in the region, but again, most of its outflows go to Europe, a trend that has slightly been reinforced during the nineties. Europe jumped from 49.4 per cent to 52.5 per cent as a destiny of US FDI outflows, while

*Table 3.2* US FDI position, 1992–2001

**US direct investment position abroad on a historical-cost basis, 1992–2001 (Canada and Mexico)**

| | 1992 | 1993 | 1994 | 1995 | 1996 | 1997 | 1998 | 1999 | 2000 | 2001 |
|---|---|---|---|---|---|---|---|---|---|---|
| All countries | 498,991 | 548,664 | 612,893 | 699,015 | 795,195 | 865,531 | 1,000,703 | 1,173,122 | 1,293,431 | 1,381,674 |
| Canada | 68,832 | 70,395 | 74,221 | 83,498 | 89,592 | 96,031 | 98,200 | 111,747 | 128,814 | 139,031 |
| Mexico | 13,729 | 15,413 | 16,968 | 16,873 | 19,351 | 21,056 | 26,557 | 32,888 | 37,332 | 52,168 |

**Foreign direct investment position in the United States on a historical-cost basis at year end, 1992–2001 (Canada and Mexico)**

| | 1992 | 1993 | 1994 | 1995 | 1996 | 1997 | 1998 | 1999 | 2000 | 2001 |
|---|---|---|---|---|---|---|---|---|---|---|
| All countries | 425,636 | 445,268 | 480,667 | 535,553 | 594,088 | 681,651 | 778,418 | 955,726 | 1,214,254 | 1,321,063 |
| Canada | 37,845 | 39,408 | 41,219 | 45,618 | 54,799 | 54,022 | 72,696 | 90,559 | 114,599 | 108,600 |
| Mexico | 1,230 | 1,039 | 2,069 | 1,850 | 1,999 | 1,723 | 2,055 | 1,999 | 7,832 | 7,418 |

**US direct investment position abroad on a historical-cost basis**

| | 1992 | 1993 | 1994 | 1995 | 1996 | 1997 | 1998 | 1999 | 2000 | 2001 |
|---|---|---|---|---|---|---|---|---|---|---|
| All countries | 100.00% | 100.00% | 100.00% | 100.00% | 100.00% | 100.00% | 100.00% | 100.00% | 100.00% | 100.00% |
| Canada | 13.79% | 12.83% | 12.11% | 11.95% | 11.27% | 11.10% | 9.81% | 9.53% | 9.96% | 10.06% |
| Mexico | 2.75% | 2.81% | 2.77% | 2.41% | 2.43% | 2.43% | 2.65% | 2.80% | 2.89% | 3.78% |

**Foreign direct investment position in the US on a historical-cost basis at year end**

| | 1992 | 1993 | 1994 | 1995 | 1996 | 1997 | 1998 | 1999 | 2000 | 2001 |
|---|---|---|---|---|---|---|---|---|---|---|
| All countries | 100.00% | 100.00% | 100.00% | 100.00% | 100.00% | 100.00% | 100.00% | 100.00% | 100.00% | 100.00% |
| Canada | 8.89% | 8.85% | 8.58% | 8.52% | 9.22% | 7.93% | 9.34% | 9.48% | 9.44% | 8.22% |
| Mexico | 0.29% | 0.23% | 0.43% | 0.35% | 0.34% | 0.25% | 0.26% | 0.21% | 0.65% | 0.56% |

*Source*: US Department of Commerce. Economics and Statistics Administration. Bureau of Economic Analysis. Survey of Current Business. Various numbers. US Department of Commerce: Bureau of Economic Analysis. International Investment Data: www.bea.doc.gov/bea/di/fdi61-95.htm. Consulted in February 2004

Latin America also increased its share by 1 per cent. Mexico is one of the countries that have benefited from that increase, jumping from 2.75 to 3.8 per cent of overall US FDI abroad. By contrast, Canada has reduced its share as a destiny of US FDI, from 13.8 per cent to 10 per cent. Europe, Latin America and to a lesser extent the Asian-Pacific countries have increased their shares to the detriment of the Canadians.[12] This shift reflects the trilateralization of investments throughout the Triad space, rather than a regionalization of US investments within North America. As in the commercial flows the US remains a global player in terms of a source or host of FDI, although part of it remains regionalized in North America. By contrast, Canada and Mexico remain spoke spaces inasmuch as most of their FDI outflows and inflows still go to or come from the US.

It is also worth noting that US FDI in Canada, during the past decade, witnessed some sectoral moves. While in 1992 48 per cent of that investment was located in manufacturing, in the year 2001 the share dropped to 38.6 per cent. US FDI has apparently moved to more attractive sectors, such as petroleum, finance and other services branches. As for Mexico, US FDI has shifted to other sectors more rapidly. While in 1993 still 70 per cent of all US FDI in that country was located in manufacturing (food processing, chemicals and transport), in the year 2000 that share dropped to 50 per cent. More attractive sectors, such as banking, finance and other services have attracted US investors (Survey of Current Business, July 1999 and June 2002). This also reflects the wave of privatization that started in the country since the Salinas years, and was consolidated during the succeeding administrations, when banking was privatized and opened to foreign investors.

While the US remains a global player in terms of investments, Canada and Mexico remain key regional players. Table 3.3 shows Canada's position in terms of FDI, both its foreign and inward stock. Just before the signing of the CUSFTA, the US remained the most important source of Canada's inward stock and a destination of Canadian outflows. In 1988, 67 per cent of total FDI in Canada came from the US and 64 per cent of Canadian FDI abroad went to that country. In the year 2001 those shares were 67 and 51 per cent respectively. The primacy of the US remained although with a Canadian investment deviation towards Europe, showing the importance Canada is getting as a player within the Triad cluster. As for Canadian investments in the US, they mainly concentrated in the energy (20.4 per cent) and financial sectors (23 per cent), for the period 1988–2001, while US investments in Canada concentrated mainly in the energy and metallic minerals (24 per cent), machinery

*Table 3.3* Canada's FDI position, 1987–2001

| **Canadian Direct Investment Abroad (Can. $, millions)** | | | | | | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **Annual** | **1987** | **1988** | **1989** | **1990** | **1991** | **1992** | **1993** | **1994** | **1995** | **1996** | **1997** | **1998** | **1999** | **2000** | **2001** |
| All industries | 74137 | 79763 | 89851 | 98402 | 109068 | 111692 | 122427 | 146315 | 161237 | 181238 | 218607 | 262909 | 283228 | 340366 | 389426 |
| Mexico | 206 | 201 | 237 | 245 | 199 | 451 | 530 | 1073 | 948 | 1933 | 2163 | 2864 | 3325 | 3686 | 4020 |
| United States | 48876 | 51025 | 56578 | 60049 | 63379 | 64502 | 67677 | 77987 | 84562 | 93939 | 110707 | 133267 | 143612 | 164526 | 198404 |
| South and Central America | 1466 | 1786 | 1989 | 2096 | 2242 | 2642 | 3816 | 4959 | 6907 | 8019 | 10440 | 12423 | 13736 | 17670 | 18104 |
| Europe | 12455 | 14981 | 18626 | 22089 | 25112 | 22874 | 26219 | 33418 | 37158 | 39632 | 47985 | 57230 | 57125 | 81399 | 87934 |
| Africa | 272 | 219 | 233 | 268 | 258 | 301 | 400 | 469 | 635 | 1217 | 1301 | 1385 | 1388 | 2393 | 2819 |
| Asia/Oceania | 5567 | 6619 | 6689 | 7636 | 9253 | 10760 | 12932 | 15785 | 16772 | 17407 | 19383 | 22278 | 23179 | 25151 | 28811 |
| Others | 5295 | 4932 | 5499 | 6019 | 8625 | 10162 | 10853 | 12624 | 14255 | 19091 | 26628 | 33462 | 40863 | 45541 | 49334 |
| | | | | | | | | | | | | | | | |
| **Foreign Direct Investment in Canada (Can. $, millions)** | | | | | | | | | | | | | | | |
| **Annual** | **1987** | **1988** | **1989** | **1990** | **1991** | **1992** | **1993** | **1994** | **1995** | **1996** | **1997** | **1998** | **1999** | **2000** | **2001** |
| Total | 105937 | 114175 | 122664 | 130933 | 135234 | 137918 | 141493 | 154594 | 168167 | 182126 | 194277 | 219389 | 248618 | 302300 | 320931 |
| Mexico | 14 | 31 | 12 | −13 | −21 | 60 | 154 | 177 | 161 | – | – | 117 | 101 | 138 | – |
| United States | 74022 | 76049 | 80427 | 84089 | 86396 | 88161 | 90600 | 102629 | 112948 | 121943 | 128978 | 146893 | 172802 | 191017 | 214960 |
| South and Central America | 153 | 203 | 247 | 294 | 292 | 240 | 115 | 48 | 376 | 347 | 372 | 324 | 303 | 565 | 719 |
| Europe | 24183 | 29152 | 32421 | 36400 | 36823 | 37256 | 36930 | 37572 | 40121 | 43722 | 47207 | 54392 | 57967 | 93361 | 86983 |
| Africa | 7 | 7 | 7 | 6 | 15 | −7 | 2 | 15 | 27 | 36 | 77 | 80 | 61 | 145 | 100 |
| Asia/Oceania | 6296 | 7020 | 7940 | 8483 | 10046 | 10468 | 11566 | 12171 | 12387 | 13715 | 15319 | 14758 | 14228 | 13949 | 15287 |
| Others | 1262 | 1713 | 1610 | 1674 | 1683 | 1740 | 2126 | 1982 | 2147 | 2363 | 2324 | 2825 | 3156 | 3125 | 2882 |

**Canadian Direct Investment Abroad (share)**

| Annual | 1987 | 1988 | 1989 | 1990 | 1991 | 1992 | 1993 | 1994 | 1995 | 1996 | 1997 | 1998 | 1999 | 2000 | 2001 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| All industries | 100.00% | 100.00% | 100.00% | 100 00% | 100.00% | 100 00% | 100.00% | 100.00% | 100.00% | 100 00% | 100.00% | 100.00% | 100.00% | 100.00% | 100.00% |
| Mexico | 0.28% | 0.25% | 0 26% | 0.25% | 0 18% | 0.40% | 0 43% | 0.73% | 0.59% | 1.07% | 0.99% | 1 09% | 1.17% | 1.08% | 1.03% |
| United States | 65.93% | 63.97% | 62 97% | 61.02% | 58.11% | 57.75% | 55.28% | 53 30% | 52.45% | 51.83% | 50.64% | 50.69% | 50.71% | 48.34% | 50.95% |
| South and Central America | 1 98% | 2.24% | 2 21% | 2.13% | 2.06% | 2.37% | 3.12% | 3.39% | 4.28% | 4.42% | 4.78% | 4 73% | 4.85% | 5.19% | 4 65% |
| Europe | 16 80% | 18.78% | 20 73% | 22.45% | 23.02% | 20.48% | 21.42% | 22 84% | 23.05% | 21.87% | 21.95% | 21.77% | 20.17% | 23.92% | 22.58% |
| Africa | 0.37% | 0.27% | 0.26% | 0 27% | 0.24% | 0.27% | 0.33% | 0.32% | 0.39% | 0 67% | 0.60% | 0.53% | 0.49% | 0.70% | 0.72% |
| Asia/Oceania | 7 51% | 8.30% | 7 44% | 7.76% | 8.48% | 9.63% | 10 56% | 10.79% | 10.40% | 9.60% | 8.87% | 8.47% | 8.18% | 7.39% | 7 40% |
| Others | 7.14% | 6 18% | 6.12% | 6.12% | 7 91% | 9.10% | 8.86% | 8.63% | 8.84% | 10.53% | 12.18% | 12 73% | 14.43% | 13.38% | 12.67% |

**Foreign Direct Investment in Canada (share)**

| Annual | 1987 | 1988 | 1989 | 1990 | 1991 | 1992 | 1993 | 1994 | 1995 | 1996 | 1997 | 1998 | 1999 | 2000 | 2001 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Total | 100.00% | 100.00% | 100 00% | 100 00% | 100.00% | 100.00% | 100.00% | 100.00% | 100.00% | 100.00% | 100 00% | 100.00% | 100.00% | 100.00% | 100.00% |
| Mexico | 0.01% | 0.03% | 0.01% | −0.01% | −0 02% | 0.04% | 0 11% | 0.11% | 0.10% | NA | NA | 0.05% | 0.04% | 0.05% | NA |
| United States | 69.87% | 66.61% | 65.57% | 64.22% | 63 89% | 63.92% | 64.03% | 66.39% | 67 16% | 66.96% | 66.39% | 66.96% | 69.51% | 63 19% | 66.98% |
| South and Central America | 0.14% | 0.18% | 0.20% | 0.22% | 0.22% | 0.17% | 0 08% | 0.03% | 0.22% | 0.19% | 0.19% | 0.15% | 0.12% | 0.19% | 0 22% |
| Europe | 22.83% | 25.53% | 26.43% | 27 80% | 27.23% | 27 01% | 26.10% | 24.30% | 23.86% | 24.01% | 24.30% | 24.79% | 23.32% | 30.88% | 27.10% |
| Africa | 0 01% | 0.01% | 0.01% | 0.00% | 0 01% | −0.01% | 0.00% | 0.01% | 0.02% | 0.02% | 0 04% | 0 04% | 0.02% | 0.05% | 0.03% |
| Asia/Oceania | 5.94% | 6.15% | 6.47% | 6.48% | 7.43% | 7.59% | 8 17% | 7.87% | 7.37% | 7 53% | 7.89% | 6.73% | 5.72% | 4.61% | 4.76% |
| Others | 1 19% | 1.50% | 1.31% | 1.28% | 1.24% | 1.26% | 1.50% | 1.28% | 1.28% | 1.30% | 1.20% | 1.29% | 1.27% | 1.03% | 0 90% |

*Source* Statistics Canada, consulted on 2002-02-26

and transportation (14.6 per cent) and financial sectors (15.3 per cent), during that same period.[13] The energy and financial sectors seem to be the most important industries where mergers and restructuring have taken place during the post-CUSFTA period. Although Canada is not yet a strong player in Latin America, its FDI share more than doubled during the period we are reviewing. Similar to what happened in the trade arena, Canadian investment in Mexico also increased rapidly, although the North American partner of the south still remains a market to be conquered. Just 1 per cent of Canada's FDI is located in Mexico.

In contrast to Canada, Mexico is the capital-poor country in North America. It still remains a major host for investors but a minor source of investments. In terms of FDI inflows to Mexico, the picture is quite similar to Canada's, that is, with a majority presence of US capital. Figure 3.14 shows FDI coming into Mexico during the period 1994–2005. In that period 67 per cent came from the US, 19 per cent from the EU, 3 per cent from Canada and 2 per cent from Japan. During this period, most of FDI concentrated in the financial sector (23 per cent of total FDI inflows), a branch that was opened and practically transnationalized after NAFTA came into ruling.

Thus, trade and investment have made both Canada and Mexico real economic platforms for many US and to some extent Canadian firms,

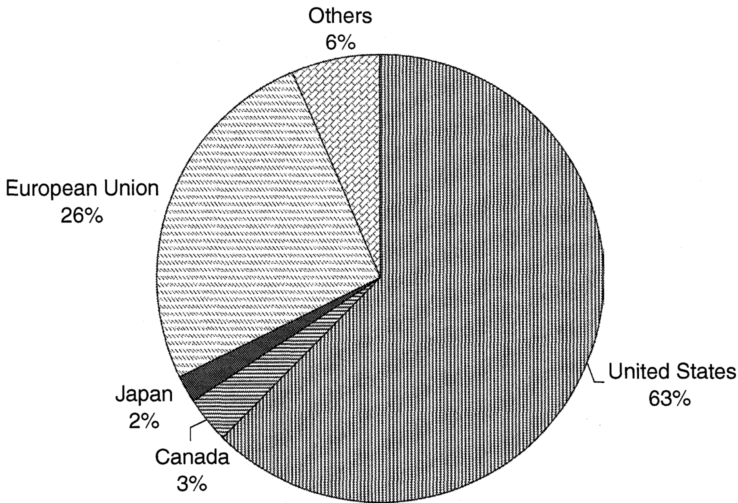


*Figure 3.14* FDI inflows to Mexico, 1994–2005 (accumulated)
*Source*: Secretaría de Economía, Mexico

through which product specialization and economies of scale and scope have developed. The pattern of specialization is clear, since Canada remains a competitive cross-border economy in manufacturing and services and a strategic reserve in resource-based products, while Mexico maintains its relocation attractiveness due to the contiguity to the American market and its (still) huge reserve of cheap labor. The US economy is, however, the real hub in the region, through which spokes located both in Canada and Mexico become connected and shape productive organization and flows exchange throughout it. In the coming section this idea will be better developed.

Before going into more detail, I should highlight that the hub-spoke regional economy becomes clearer if we take into account the important role played by US MNCs in linking trade north and south of the hub. US MNCs have traditionally played a major role in US foreign trade. Table 3.4 summarizes that role. In the early eighties, 77 per cent of overall US exports and 50 per cent of imports were associated with American MNCs; that is, trade that was either intra-firm (US parents to foreign affiliates), inter-firm (shipped by US parents to other foreign parent groups) and arms-length (shipped to non-affiliated persons). Through these mechanisms MNCs have traditionally 'internalized' arms-length markets, as I already explained in the first chapter. Although associated US MNCs' trade has decreased during the past 20 years, the role played by American MNCs in world trade remains crucial. In the year 2000, 56 per cent of US exports and 35 per cent of imports were still associated with US MNCs' operations. This associated trade is the root of the network economy featuring globalization trends. Furthermore, this firm-centered organization of investment, production and trade is the backbone of North America's economic regionalization.

Table 3.5 shows the importance of US MNCs in trade exchanges with Canada and Mexico. In 1982, that is, prior to the signature of the CUSFTA, 60 per cent of US exports to and 46 per cent of imports from Canada were done through US affiliated firms (most of it being intra-firm transactions). Those shares more than doubled US-affiliated trade on a worldwide basis. Although the share of US-affiliated trade against total US trade with Canada has diminished in the past 20 years, the shares remain high (above 30 per cent on both exports and imports) compared to the ratio of US-affiliated trade against total trade. Trade liberalization spurred by the CUSFTA–NAFTA deals could eventually explain the decline of US firms' participation in bilateral trade, by concentrating activities on US parent companies, and relying more on arms-length transactions in order to exploit the removal of barriers. But the

*Table 3.4* US trade in goods associated with non-bank US MNCs (millions of dollars)

| | 1982 | 1989 | 1994 | 1999 | 2000 |
|---|---|---|---|---|---|
| **MNC-associated US exports, total** | **163383** | **236,371** | **344,504** | **435,192** | **438798** |
| Intra-MNC trade | 46559 | 89,539 | 136,128 | 162,503 | 175639 |
| Shipped by US parents to their MOFA's | 44320 | 86,050.00 | 132,694 | 158,575 | 167646 |
| Shipped by US parents to their other foreign affiliates | 2239 | 3,489 | 3,434 | 3,928 | 7993 |
| MNC trade with others | **116825** | **146,832** | **208,376** | **272,689** | **264097** |
| Shipped by US parents to other foreigners | 106666 | 133,813 | 185,050 | 238,693 | 235792 |
| *of which:* | | | | | |
| Shipped to foreign parent groups of US parents | n.a. | 10,413 | 18,207 | 26,140 | 30675 |
| Shipped to foreign affiliates by other US persons | 10159 | 13,019 | 23,326 | 33,996 | 28305 |
| To MOFA's | 8432 | 11,437 | 20,774 | 31,973 | 28305 |
| To other foreign affiliates | 1727 | 1,582 | 2,552 | 2,023 | n.a. |
| **MNC-associated US imports, total** | **120768** | **201,182** | **256,820** | **388,480** | **425920** |
| Intra-MNC trade | 41598 | 77,307 | 113,415 | 164,449 | 179971 |
| Shipped by MOFA's to US parents | 38533 | 71,283 | 107,203 | 158,958 | 172643 |
| Shipped by other foreign affiliates to US parents | 3065 | 6,024 | 6,212 | 5,491 | 7328 |

| | | | | | |
|---|---|---|---|---|---|
| MNC trade with others | **79170** | **123,875** | **143,405** | **224,032** | **245949** |
| Shipped by other foreigners to US parents | 69363 | 103,788 | 122,638 | 193,969 | 210620 |
| *of which:* | | | | | |
| Shipped by foreign groups of US parents | n.a. | 32,398 | 43,243 | 78,002 | 77030 |
| Shipped by foreign affiliates to other US persons | 9807 | 20,087 | 20,767 | 30,063 | 35329 |
| By MOFA's | 7567 | 13,015 | 15,161 | 23,288 | 28731 |
| By other foreign affiliates | 2240 | 7,072 | 5,606 | 6,775 | 6598 |
| **Addenda:** | | | | | |
| Total US exports of goods | 212275 | 362,999 | 512,626 | 695,797 | 781918 |
| MNC associated US exports as a percentage of total | 77 | 65 | 67 | 63 | 56 |
| Intra-MNC exports as a percentage of total | 22 | 25 | 27 | 23 | 21 |
| Total US imports of goods | 243942 | 473,385 | 663,256 | 1,024,618 | 1218022 |
| MNC associated US imports as a percentage of total | 50 | 42 | 39 | 38 | 35 |
| Intra-MNC imports as a percentage of total | 17 | 16 | 17 | 16 | 15 |

*Source:*
1982: Mataloni, Raymond Jr, and Fahim-Nader, Mahnaz, 'Operations of U.S. Multinational Companies: Preliminary Results, from the 1994 Benchmark Survey', Survey of Current Business (SCB), December 1996, p. 21
1989–1994: Mataloni, R. and Yorgason, Daniel, 'Operations of US Multinational Companies. Preliminary Results, from the 1999 Benchmark Survey'. SCB, p. 39, Vol. 82, No. 3, March 2002
1999–2000: Mataloni, R. Jr, 'US Multinational Companies: Operations in 2000', SCB, December 2002, p. 115

*Table 3.5* US trade in goods to Canada and Mexico associated with US MNCs, 1982–2000

| Associated trade | US exports shipped to affiliates (millions of dollars) | US imports shipped by affiliates (millions of dollars) | Total US Exports (millions of dollars) | Total US Imports (millions of dollars) | Exports (share) | Imports (share) |
|---|---|---|---|---|---|---|
| **1982** | | | | | | |
| All countries | 56,718 | 51,406 | 211,198.00 | 247,642.00 | 26.86% | 20.76% |
| Canada | 19,505 | 21,392 | 32,382.20 | 46,476.90 | 60.23% | 46.03% |
| Mexico | 2,818 | 1,940 | 11,103.80 | 15,565.90 | 25.38% | 12.46% |
| **1993** | | | | | | |
| All countries | 124,120 | 107,977 | 456,832.00 | 536,458.00 | 27.17% | 20.13% |
| Canada | 43,068 | 48,596 | 100,190.40 | 121,844.50 | 42.99% | 39.88% |
| Mexico | 12,636 | 11,874 | 41,635.50 | 39,929.60 | 30.35% | 29.74% |
| **2000** | | | | | | |
| All countries | 195,951 | 201,374 | 773,304.00 | 1,222,772.00 | 25.34% | 16.47% |
| Canada | 59,508 | 77,827 | 178,941.00 | 230,838.30 | 33.26% | 33.71% |
| Mexico | 31,017 | 37,408 | 111,349.00 | 135,926.40 | 27.86% | 27.52% |

*Source*: Survey of Current Business (SCB), Vol. 82, No. 3, p. 42, December 1985, and SCB, Vol. 82, No. 3, p. 127, December 2002

fact that more than 30 per cent of trade transaction between Canada and the US is still being done through US affiliates (and most of it being intra-firm trade), in spite of cross-border integration, shows the role played by US MNCs in the organization of commodity and investment markets with the northern neighbor. In many ways, their home has become regional-oriented rather than national-centered, fully compatible with the network of organizational nodes explained in the first chapter.

US–Mexican trade relations show a similar pattern to that of Canada. In 1982 US-affiliates' exports represented 25 per cent of total US exports to that country, while imports were 12.5 per cent. In the year 2000, those figures were 27.8 and 27.5 per cent, respectively. In other words, in spite of NAFTA, that in principle opened new market opportunities for the two economies, hierarchy and network-based-firms transactions consolidated. This becomes more relevant if we remind ourselves that in the year 2000, 30.6 per cent of overall Mexican exports were dominated by 35 leading foreign affiliates, being American, European or Japanese. In that same year nearly two-thirds of the country's manufactured exports came from foreign firms (UNCTAD, 2002: 175–6). At any rate, MNCs and their organizational system have proved to be crucial in order to build the regional network of exchange in North America and to boost the competitiveness of key sectors.

## Geography matters: the emergence of a continental hub with spokes at the cross-border level

Is trade regionalization equally integrating the three economies of North America? Is the strong presence of both US investments and firms in Canada and Mexico integrating their territories evenly to the US locomotive? In fact, if suppressing barriers to trade and investment at the cross-border level conveyed a real policy shock, firms, market actors and regions are far from reacting and accommodating equally to policy change. Economic integration through the CUSFTA–NAFTA disciplinary model is in fact consolidating a regional subsystem of spatial organization and exchange centered upon a major hub and at least two spokes.

Figures 3.15 and 3.16 show clearly the location of the 'North American hub'. It is that region comprising Central Canada provinces – Ontario and Quebec – where most of Canada's foreign trade to the US is being done, and whose trade and economic activities have become closely intertwined with US rich regions going from the Great Lakes to the Middle Atlantic and New England regions. In 2002, 56 per cent of

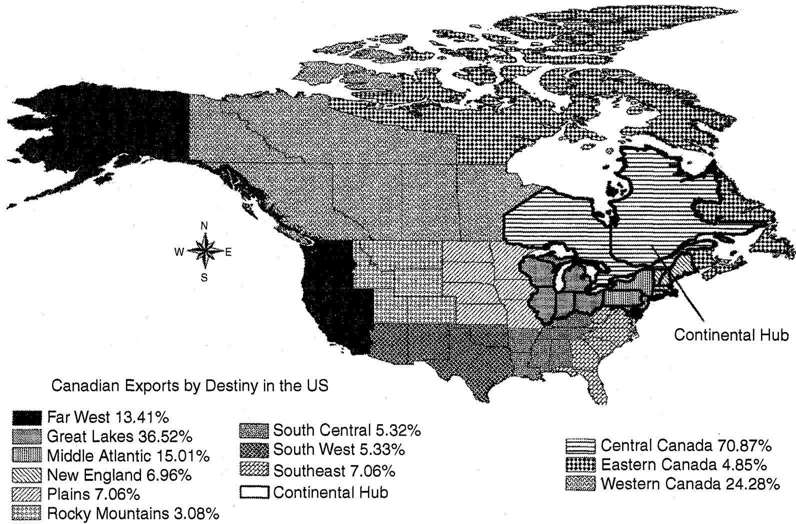


*Figure 3.15* Canadian exports to the US by region

*Source*: Map elaborated by Arc View 3.1 ESRI, with data from Statistics Canada

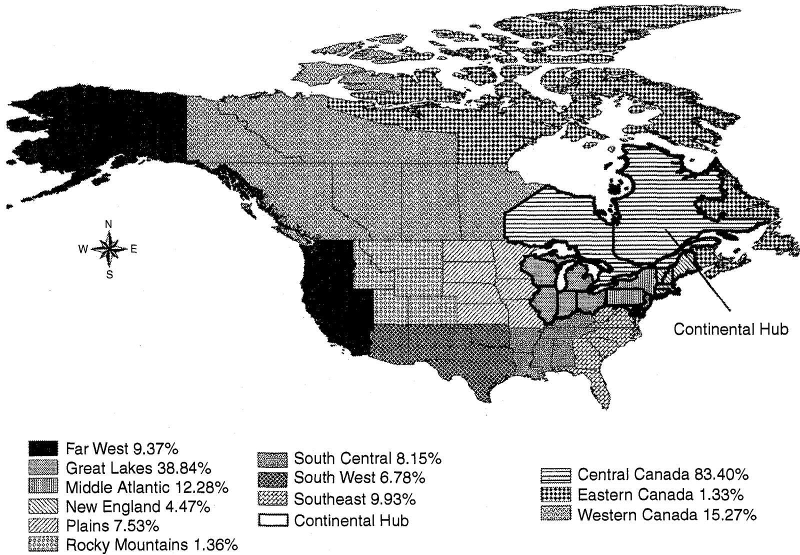


*Figure 3.16* Canadian imports by destination from the US

*Source*: Map elaborated by Arc View 3.1 ESRI, with data from Statistics Canada

overall exports going to Canada originated from this sub-region which at the same time was the destiny of 58 per cent of overall Canadian exports was to the US. At the same time, Central Canada was the origin of 71 per cent of overall exports to the US and the destination of 83.4 per cent of total imports coming from the latter country. Thus, it is within this cross-border region where more than 50 per cent of US trade with Canada is being done, and above 70 per cent of Canadian trade to the US is located (all figures from Statistics Canada). A real hub, if we also take into consideration the concentration of population, wealth, and the location of major metropolises.[14]

This 'continental' hub, as Canadians would like to call it,[15] contains, however, its own sub-regions. The Great Lakes and Ontario feature intra-industry integration unleashed by the automobile industry since 1965. This is the core of the three major auto-makers: Ford, Chrysler and General Motors, whose cross-border vertical and horizontal integration began when the Auto Pact came into force. Of all major cities located in this hub, Detroit and Toronto emerge as the most continental-oriented, the former exporting 70 per cent of its overall exports to Canada and the latter ready to become the capital of a 'region state', that is, a space where most of its economic dynamism will be north–south oriented (Slater, 1999: 378; Courchene and Telmer, 1998). The Great Lakes and Ontario zones heavily interact with what was originally called the 'Industrial Belt', that is, the region where the industrial take-off of the US started, going from the Atlantic coast, between Boston and Baltimore, to the Saint-Louis and Minneapolis-Saint Paul corridor. This old industrial zone, also called 'The Foundry' by Joel Garreau in a seminal regional approach to North America, was successful in making an economic transition to the new industries and services fueled by the new wave of technological change cross-cutting this country (Garreau, 1982; Claval, 1994). North of the old 'Foundry', the Quebec province is well positioned both historically and politically. Being traditionally the commercial interface of Central Canada with Europe, it is currently the Canadian province with more autonomy and with a distinctive cultural presence in the continental hub. Although for different reasons, Quebec's French Canadians are geared to strengthen north–south economic links with the old Foundry and the Great Lakes in order to reinforce their autonomy vis-à-vis Ontario and 'Anglo-Saxon' Canada.

What also makes this continental hub distinctive is that two national capitals are part of it, as well as major 'global' cities such as Chicago and New York, reflecting the high economic and cultural dynamism of the whole region (see Paelinck and Polèse, 1999). Thus, it is not surprising that once the tariff barrier was waived between north–south exchanges,

most of trade creation and deviation has been performed between Central Canada and the Great Lakes–Atlantic-New England regions. According to some gravity models, trade liberalization promoted by the CUSFTA–NAFTA disciplinary model increased exports from Central Canada by 42.8 per cent, and imports by 18.3 per cent. The impact in Western Canada was rather modest, 0.9 per cent on exports and −0.5 per cent (decrease) in imports, while for Eastern Canada the impact was rather negative (−8.8 and −13.1 per cent, respectively). This means that there was trade diversion from Eastern Canada to the benefit of the Ontario and Quebec provinces. Interesting to stress is that NAFTA stimulated trade creation from Western Canada to Mexico.[16] As for the US, all regions benefited from trade creation except the Rocky Mountain, a zone with low urban population. Apart from the Great Lakes, Atlantic and New England regions, trade creation induced by trade integration benefited also the Southeast, South Central and to a lesser extent the Southwest (all figures from Wall, 2003: 20). This clearly shows how 'continental Canada' is well integrated with the US, the anchor of which stems from the Great Lakes and expands north of the Atlantic and south of the Gulf of Mexico.

We cannot neglect the importance of Western Canada both as an origin of US exports (24.3 per cent) and as a destination (15.3 per cent). Although a great part of it is cross-border exchanges with US bordering states, some authors have suggested (e.g. Paelinck and Polèse, 1999) that the corridor going from Los Angeles to Vancouver constitutes a sort of second 'continental' region in North America. However, the dynamism of this second pole is rather linked to trade and other economic links with the Asia Pacific region. Nonetheless, Western Canada epitomizes the strength and strategic positioning of Canada as a resource-based supplier in North America, in terms of agricultural processed products, lumber, water and energy resources. This strategic position could eventually counterbalance the traditional dominance of Central Canada in both the economics and politics of the country.

This is in fact the case for Alberta. Since fuel oils have become a strategic exchange across North America, bitumen-rich Alberta is becoming a key province for supplying both conventional and unconventional energy resources to Mid-West and North Atlantic America. In 2004, overall Canadian crude production reached 2.5 million barrels (Mb) per day, of which 90 per cent came from Western Canada. Most of Canada's conventional and non-conventional crude oil reserves and natural gas stocks are located in the Western Canadian Sedimentary Basin (WCSB),[17] a vast region encompassing most of Alberta, and parts of

British Columbia and Saskatchewan. Currently, oil sands provide 1 Mb per day, and according to Alberta's Minister of Energy, this amount could reach 3 Mb per day over the next decade and possibly grow to 5 Mb per day by 2030 (McFall, 2006). Since most of the oil and gas trade coming from Western Canada to the US is being carried through pipeline, a deeper integration between these provinces and the 'continental hub', and even the South West, is anticipated.[18]

It is precisely south of the Gulf of Mexico, the so-called South West, where the most important interface between 'continental America'[19] and the Mexican economy is located. As indicated in Figure 3.17, US exports to Mexico are shipped from selected regions. As of 2001, 56.5 per cent of overall US exports came from Texas and California. Although these two states are the dominant ones in overall US trade with Mexico, Texas is by far located in the strategic position vis-à-vis Mexico's trade flows. Texas is not only the greatest source of exports for Mexico (44 per cent of overall US trade in 2001, compared with 12.5 per cent coming from California), but it is also the gateway to other key regions in the US which also remain strategic in US–Mexico exchanges. As shown in Figures 3.15 and 3.16, states located in the South East and South Central regions function as an interface between

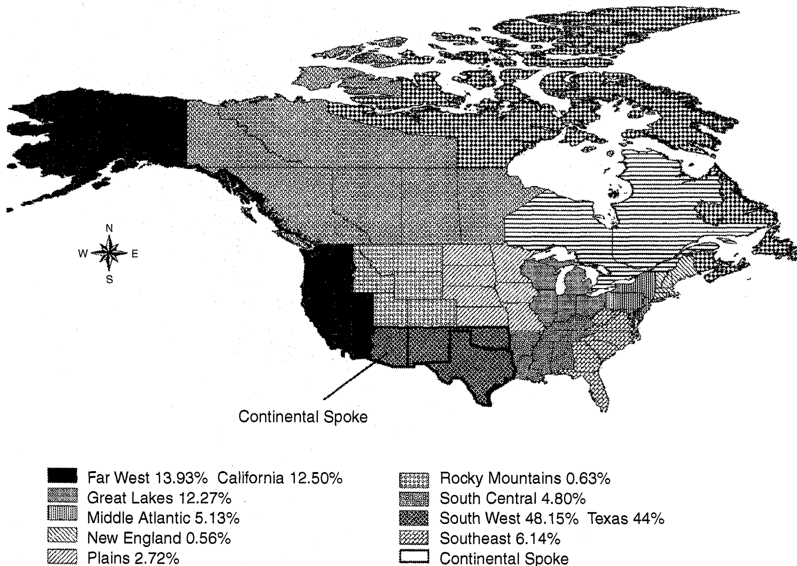


*Figure 3.17* US exports to Mexico by region

*Source*: Map elaborated by Arc View 3.1 ESIRI, with data from Statistics Canada

the South West – in which Texas is located – and the Great Lakes, Middle Atlantic and New England regions. This could explain why 18 per cent of overall US exports to Mexico, in 2001, came from those three northern US regions. Indeed, exports coming from the Great Lakes witnessed the highest rates of growth compared to other regions, reflecting the boom of US–Mexico exchanges in the automobile sector during the early post-NAFTA years (all figures from US Census Bureau, 2003). As previously said, Michigan is the fief of the three major automobile assemblers with a major stake in Mexico (and in Canada). Indeed, 45 per cent of all US exports to Mexico coming from the transportation branch originates in the state of Michigan.[20]

Thus, the continental hub is strategically connected with two major spokes: the South West where Texas is located, Houston being its 'global city' (while San Antonio is a 'continental' counterpart), and the Far West, in which California is located, Los Angeles–San Francisco being the 'global cities' of this region, and San Diego the continental one. Both San Antonio and San Diego ship 50 per cent or more of their exports to Mexico, whereas Houston, Los Angeles and San Francisco, although being important in US–Mexico trade, have a rather global profile in their transactions (Slater, 1999).

Though we don't have data tracing the origin by state of Mexican exports to the US, I followed another approach in order to trace a 'NAFTA-oriented hub' located in Mexico. Traditionally, Mexico's territory has been roughly divided in three socioeconomic regions: the North, highly industrialized and prosperous, the Central Plateau, the most populated part of the country and where most of the industrial activity is concentrated, and the South, where agriculture still remains the main economic activity. Official classifications have divided the country according to geographic parameters. Mexico's Instituto Nacional de Estadística, Geografía e Informática (INEGI), the equivalent to sources of information such as the US Bureau of the Census or Statistics Canada, has depicted six national sub-regions: 1) Northern Border, 2) Central North, 3) Central Mexico, 4) Pacific, 5) Gulf and Caribbean, and 6) South.[21] Inspired by this classification, and considering those industries featuring a good performance in the past ten years, as well as using other socioeconomic data, *à la* Garreau (1982) or Claval (1994), we could say that in Mexico, the core of NAFTA-stimulated activities is located in the central and northern-border regions, the industries of which are strategically connected with Texas and California and other southern US states, as well as with the automobile and machinery cluster of the 'Continental NAFTA core'. It is within this

geo-economic territoriality where most of Mexico–US exchange of commodities, services, resources, labor specialization takes place. This is where the NAFTA market, supported by its trans-border institutional machinery stimulating and reinforcing the mobility of goods, investments, services and skills, is integrating the US and Mexico.

Although economic asymmetries and social imbalances are pervasive across Mexico's different regions, this does not invalidate the empirical fact that most successful export-orientated industries are located in Mexico's NAFTA core. Yet most industrial workers and skilled labor (engineers and technicians) are concentrated there, as reported by some studies (OECD, 1998). Furthermore, the economic governance of this area is commanded by production strategies followed by major market players, such as big or global firms, a business-orientated favorable environment anchored at the inter-state level by the NAFTA rules-based regime, and the empowerment of local institutions and cross-border alliances dealing with environmental and socioeconomic problems triggered by the impact of economic change. In the last part of this section I will rapidly describe the importance of these two key Mexican regions.

### The Mexican Northern interface

This region runs from Baja California to Tamaulipas and encompasses all states included by INEGI in its so-called Northern Border region. It is a dynamic region that in the year 2000 concentrated 24 per cent of Mexico's Gross Domestic Product (GDP), and 28 per cent of overall value added in manufacturing. This region produced in 1999 35 per cent of overall Mexican GDP in the transport industry, 51 per cent of machinery-related branches and 63 per cent of electric equipment.[22] Since 1994, this region has witnessed higher rates of growth than the rest of the regions, as shown in Figure 3.18. GDP per capita is not only higher in this region but also increased in real terms, after 1993, compared to the rest of regions (see Figure 3.19).

This region has benefited the most in the post-NAFTA era. Proximity to US markets, economies of agglomeration and scale, as well as human capital seem to explain this performance (cf. Esquivel and Messmacher, 2002). This northern region also works as a bridge between central Mexico and the US. All road transportation going from the south to either California or Texas must go through the territory of the north.

The Mexican North also functions as the second pole of FDI located in Mexican territory, the first one located in Mexico City and surrounding cities. As many as 23.2 per cent of all firms with FDI are located here, with Nuevo León and Baja California being the prominent states of the

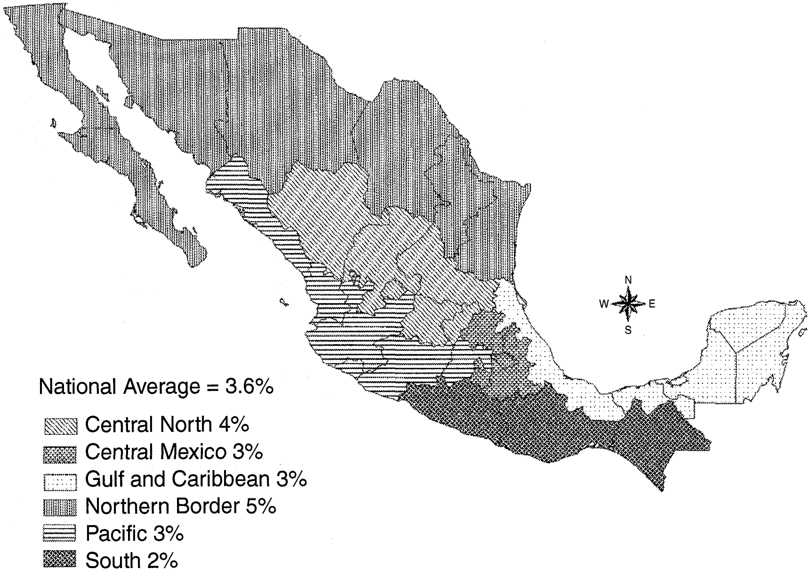


*Figure 3.18* Mexico: rate of growth by region, 1994–2000
*Source*: Map elaborated by Arc View 3.1 ESRI

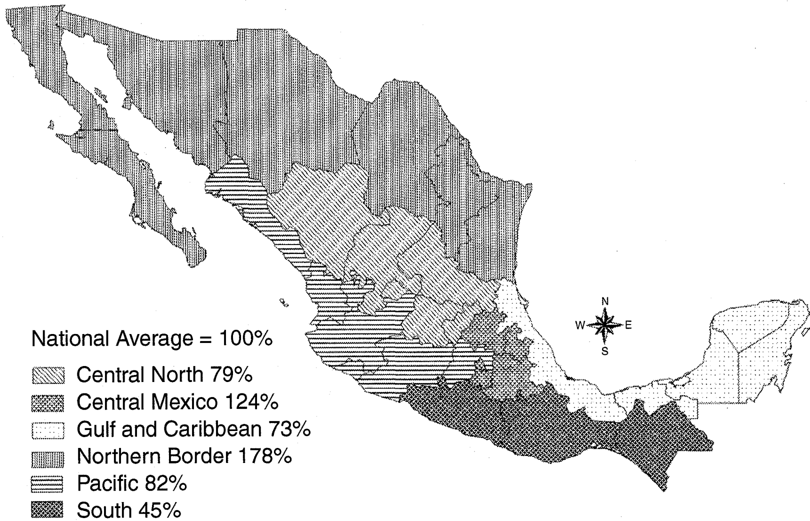


*Figure 3.19* Mexico: GDP per capita, 2000
*Source*: Map elaborated by Arc View 3.1 ESRI

region, and reflecting in some way the role played by both Tijuana and Monterrey as major industrial poles, interfacing with continental and global cities in either California or Texas. This region concentrated 25.6 per cent of overall accumulated FDI from 1994 up to the end of 2001.[23]

The northern core also clusters the major amount of state wealth from all over the country. As shown in Figure 3.18, all states comprising the northern interface region feature a per capita income above the nationwide average, the state of Nuevo León being the richest, with a per capita income 75 per cent above the national level. The northern region, in terms of wealth, is also the most homogeneous region in the whole country.

Being in the North, the 'foundry' of the country[24] and the region that concentrates most machinery (electrical and non-electrical) output (57 per cent of overall value added in this branch), Nuevo León is by far the most important state of this territory, and Monterrey its major city. Nuevo León turns out 14.5 per cent of overall Mexican value in the machinery branch, 7.2 per cent of basic chemical output, 6 per cent of national output in the automobile sector, and 20 per cent of overall GDP in the metals branch (data for 1999). Only the state of Mexico, located at the heart of the central core and surrounding Mexico City, maintains greater importance in all Mexican industries. Monterrey is the place in which a major group of successful Mexican businessmen have their headquarters. This is the so-called 'Monterrey Group' integrated by powerful firms such as ALFA (Steel), CEMEX (cement), CYDSA (Chemicals), IMSA (Galvanized Plate), VISA (beer), and VITRO (glass). Though highly protected by the government during the inward-looking economic model of past decades, these industries have successfully overcome the impact of the new open-oriented NAFTA regime. Most of them have 'strategic alliances' with foreign partners in order to modernize their processes and penetrate export markets (Pozas, 1993).

This Mexican northern interface also encompasses a major sub-region that we could easily call 'Mexamerica'. This is a trans-boundary territory with a state-level political demarcation and self-contained in Mexico's northern states. It is a 210 kilometer-wide strip running along the Mexican border (3,380 km long), from the Tijuana-San Diego corridor in the west to the twin harbors of Matamoros and Brownsville to the east. Between these two poles, three major twin cities exist: the Nogaleses, the Paso del Norte cluster, encompassing both Ciudad Juárez and El Paso, and the Laredos. With more than 11 million people living in this territory (6.1 in the US side and 5.1 in the Mexican side), and with annual population growth rates higher than their respective annual national

averages (3.1 per cent for the US side and 4 per cent for the Mexican side) (Business Week, 1997: 32), Mexamerica is a binational-oriented interface, which has an economic dynamism in itself, mainly thanks to border businesses. Business on the border has two faces: *maquiladora* and other cheap labor-related industries in the Mexican side, and retail trade and services in the US side.[25]

Nonetheless, the vulnerability of this sub-region is precisely in the high concentration of low-skilled labor industries. As I highlighted in the first section of this chapter, cheaper imports coming from China, the Caribbean and Central America are now reducing the market shares of Mexamerica's exports to the US. Real wages have increased in Mexico while in those countries and regions they have remained lower, or 'competitive' (cf. Waltkins, 2002: 11–26). NAFTA's privileges to Mexico are declining, as NAFTA-like treatment is being extended by the US to China, the Caribbean, Central America and other countries either through multilateral negotiation in the WTO, or through bilateral trade agreements. Furthermore, costs of energy have become uncompetitive in Mexico since reforms needed in the power sector have been delayed. *Maquiladora* activities are also moving from north to central and southern Mexico, where labor costs could eventually become lower than in the border region. At the end of the eighties, 90 per cent of all *maquiladora* firms were still located in the north, mainly in those municipalities located in Mexamerica. As of 2001, 76 per cent remained located in northern states, while states like Jalisco, Puebla and Yucatán have become major hosts of these low-skilled industries in recent years.

Although well positioned to exploit the advantages of continentalization, Mexamerica and the northern region have suffered from the growing uncertainties and insecurity provoked by the emergence of a barricaded border with the US, i.e. to deter illegal migration, and the drug 'wars' unleashed by major narcotic dealers in recent years. How these two issues are barring and/or modifying continental trends will be reviewed in Chapter 5.

### The Central high-tech core

This region is located mainly in what INEGI calls Central Mexico, and part of the Pacific and Gulf of Mexico regions. It runs from Jalisco, the Mexican state located on the Pacific Coast, to Veracruz, the state located on the shore of the Gulf of Mexico. Between those two states lie the states of Michoacán, Guanajuato, Querétaro, San Luis Potosí, Hidalgo, Tlaxcala, the state of Mexico, Puebla, and in the very center, Mexico City, considered the only 'global' city of the country. This region

encompasses the whole technological gradient of industries that have been activated by trade liberalization and NAFTA in the recent past. Not all of the states in this region participate on equal terms in the economic dynamism of the whole region. First of all, most of the wealth and activities are concentrated in Mexico City, which is the most populous site of the whole country (with 20 million inhabitants if we include the metropolitan area). Mexico City stands, with the highest per capita income of the country, 158 per cent above the national average, and is considered the financial and services capital of the whole country. It is hence not far-fetched to say that most of the productive activities within this region are linked directly or indirectly to the consumer and social needs of this city. It amassed 23 per cent of overall GDP, 42.5 per cent of all firms with FDI in the country and 60.2 per cent of the accumulated FDI from 1994 to 2001. In contrast with the northern states, wealth is unevenly distributed. For instance, the state of Mexico, which concentrates the most mid- to high-tech production in the whole country and which in many ways provides for the welfare of Mexico City, features a per capita income 20 per cent below the national level! Yet states like Puebla, Guanajuato, San Luis and Hidalgo, encompassing major cities as Puebla City, León, San Luis City, and Pachuca, are below the per capita income of the state of Mexico.

The imbalances of this region can be partly explained by the fact that, despite being the core of manufacturing in the whole country, it still encompasses a significant amount of people living in highly fragmented rural areas. With the exception of Mexico City and its metropolitan area (located in the state of Mexico), people of the central plateau still live in rural settlements (villages of less than 15,000 inhabitants). More precisely, manufacturing activities are mainly concentrated in the major cities of the high-tech core, that is, those going from Guadalajara in the west, crossing through León, Celaya, Irapuato, Guanajuato, Querétaro, Pachuca, Toluca, Puebla City, Tlaxcala City, and then going to the southeast through Jalapa, Córdoba-Orizaba up to the port of Veracruz. This said, we can delineate three major industry belts and two major manufacturing rings (transport and textile) that overlap in a different way across this region.

### *The metals belt*

The states of Jalisco, Durango, Querétaro, Michoacán, San Luis, Mexico, Mexico City, Puebla and Veracruz produce 53 per cent of all Mexican output of primary and fabricated metals. Most of the production is, however, concentrated in the state of Mexico (20 per cent of the GDP in

this branch), from which a metal corridor runs through San Luis up to Nuevo León. The capital of the northern high-tech region, Monterrey, itself turns out 20 per cent of all national production. This shows how northern states are linked to the central core.

*The machinery and electronics belt*

This belt also runs from Jalisco, and encompasses all the states of the former belt, except Durango and Michoacán, and including Guanajuato, Querétaro, San Luis Potosí and Tlaxcala. These states concentrate 34 per cent of overall production in machinery and electronic equipment, the state of Mexico being the place in which this concentration is 14 per cent. A similar corridor to the metals one runs from this state through San Luis up to Nuevo León, which concentrates 15 per cent of overall production. This machinery belt has already become a kind of 'spoke' of the machinery 'hub' located in northern states.

*The chemical belt*

The third major belt that crosses this region is constituted by the chemical industry, a major branch of Mexico's manufacturing in which major growth is anticipated because of the ongoing privatization of PEMEX's petrochemical plants. Jalisco, Guanajuato, the state of Mexico, Tlaxcala, Puebla and Querétaro are part of this major belt. These states contain 67 per cent of overall production in this branch. Mexico City concentrates 30 per cent of national production. The chemical belt is itself continued along the Gulf of Mexico coast, and becomes connected via Veracruz to the petrochemical belt and the oil ring.

*The automobile ring*

As much as 91 per cent of overall Mexican production in the automobile sector is concentrated in 10 states. Four of them are located in the northern region (Coahuila, Chihuahua, Nuevo León and Sonora), creating 31 per cent of national automobile production. The remaining six are located in the central region (Aguascalientes, Guanajuato, Querétaro, Mexico, Morelos and Puebla), featuring a kind of ring around Mexico City. The state of Mexico is once again the king of this sector, concentrating 18 per cent of all production itself. The fact that most of the automobile production is located in these two regions (northern and central) demonstrates the close interdependence and importance of them both. The concentration of FDI in this sector, during the period 1994–2001, also reflects the two major poles: the automobile ring of the central plateau absorbed 64 per cent of overall investments, and the northern states 22.4 per cent.

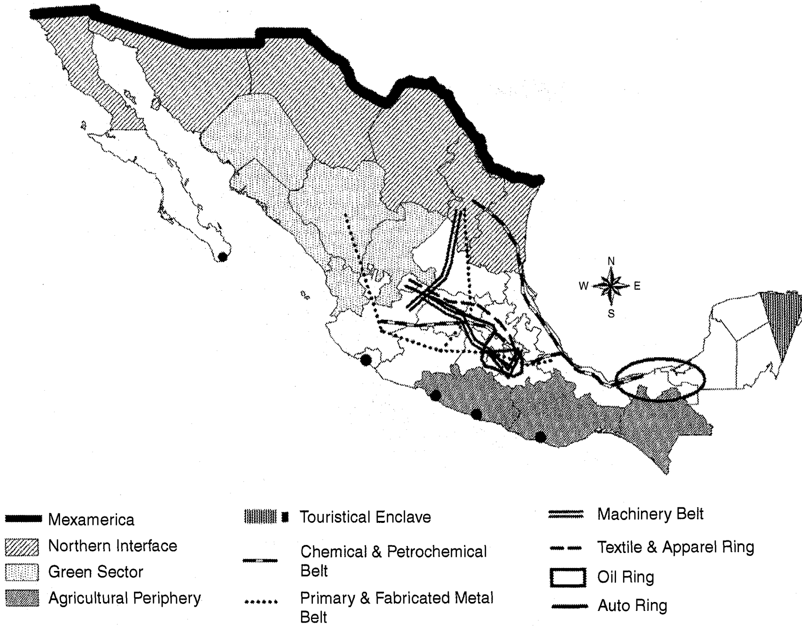


*Figure 3.20* Mexico's interconnection with the continental hubs
*Source*: Map elaborated by Arc View 3.1 ESRI

*The textile and apparel ring*

The transport ring is overlapped by a low-tech ring encompassing the same states that participate in the former, except Morelos. To those five states we should add Tlaxcala, Hidalgo and Mexico City. These eight states are the locus of 59 per cent of overall production in this sector. The state of Mexico and Mexico City concentrate 31.5 per cent of all national production.

## Is there a periphery in North America?

As Dani Rodrik reminded us: 'Trade becomes contentious when it unleashes forces that undermine the norms implicit in domestic practices' (Rodrik, 1997: 40). Market expansion subverts processes that are value-orientated and that could be perceived incompatible with the very nature of the market mechanisms. This is what is at stake in Mexico's rural south and most of the rural-based region going from Guatemala to Nicaragua. This region's complexities stem from the mix of overlapping market-orientated production systems with those

communal- or family-based economic units prevailing mainly in agricultural production. Furthermore, no serious restructuring in this sector has been achieved since Mexico liberalized its agriculture. The historical divide between irrigated land and rain-fed production persists, as well as that between commercial production, mostly located in the north of the country, and local crops, most of the time for self-consumption purposes, located in the south. The problem is that most of the rural population (around 18 per cent of the total) still depends on rain-fed, small plots, grain-based (mainly maize and beans) traditional production.

Thus, economic governance under the network or global firm, framed by NAFTA-based rules ensuring corporate property rights and the free mobility of investments, goods and services, seems not to be the right device for regaining long term growth in this region. The need to launch state-led policies for bridging 'development gaps' in this region becomes clearer if we bear in mind that income disparities between northern and southern Mexico have increased since the inception of NAFTA (see Figures 3.18 and 3.19), and that purely market-led forces won't be enough to redress those historical imbalances that are rather being exacerbated by them.

The question of asymmetries in capital endowment is not only important for understanding the way integration is reconfiguring Mexico's economic space; the manner in which different regions perceive and react politically to the expansion of market and export-orientated policies is also significant. It is possible that the market-orientated formula could be part of the medicine for raising the productivity and competitiveness of the Mexican south. Nonetheless, it has certainly provoked what sociologists call a 'perverse effect', that is the opposite that what was anticipated. The Zapatista uprising and the popularity gained in urban Mexico by its major leader, 'Marcos', because of his sharp criticism of neoliberal reforms and his commitment to the autonomy of indigenous communities, have shown that economic policies in Mexico, especially agricultural policies, cannot be solely the result of market mechanisms.

During recent years, NAFTA has become the target of articulated criticism from some left-wing national-based political parties and, specifically, peasants and guerrilla uprisings located in the southern region, who have denounced neoliberalism as a major betrayal to national, popular yet indigenous values. Their political behavior is more linked to local histories and cleavages, and certainly to the growing erosion of their material conditions of life (Díaz-Polanco, 1997; Le Bot, 1997; Montemayor, 1997).

The best articulated movement against NAFTA reforms in the rural sector appeared in the fall of 2002, when 12 independent grassroots organizations formed a bloc called *El Campo no Aguanta Más* (CNAM),[26] whose main goal was to stop the liberalization of basic staples scheduled for 2003 under NAFTA.[27] They also demanded the renegotiation of the agricultural chapter of this agreement in order to reverse its liberalization, to be finalized in 2008, when tariff-rate quotas on maize and beans will become fully phased out. The movement made other important requests including an increase of the agricultural budget for the years to come; a restructuring and widening of agricultural funding; the prohibition of importing genetically modified staples; and the leveling of the playing field with developed partners in terms of standards and sanitary and phitosanitary (SPS) measures (El Campo no Aguanta Más, 2002).

Since the rise of this movement, the position of the Mexican government was to refuse any renegotiation of NAFTA. However, Mexican officials recognized that Mexican farmers needed further support comprised within a so-called 'agricultural armor plating'. After the radicalization of peasants during the first two months of 2003, President Vicente Fox signed, in April of that year, the so-called 'National Agreement for the Countryside' (ANC: *Acuerdo Nacional para el Campo*), through which the government became committed along with major peasant organizations to a comprehensive review of agricultural policies. The ANC stopped the radicalization of peasant mobilizations and opened a new stage of political and institutional negotiations in order to craft a new policy approach to Mexican agriculture, including trade positions vis-à-vis NAFTA partners and WTO negotiations.[28] However, the need to launch a state-led agricultural policy for the Mexican south is still pending. The importance of such a major state-led restructuring becomes obvious if we review the major traits of this region, considered a sort of 'periphery' within the North American space.[29]

## The agri-subsistence region

From Oaxaca to Chiapas, and beyond the southern Mexican border with Guatemala, a poor agricultural-based economy dominates this territory. This is what I call the agri-subsistence region. The three Mexican states that this territory embraces have the following features:

a) Manufacturing production within their respective state boundaries is far below the national average (21.5 per cent), ranging from 13.5 per cent at the top (Oaxaca) to 4.3 per cent at the bottom (Chiapas).

b) The agricultural sector is above the national level (5.5 per cent of overall GDP), ranging from 10.7 per cent at the bottom (Guerrero) to 15.3 per cent at the top (Chiapas). Nonetheless, in contrast with other regions in which agriculture features in similar ranges or higher (Michoacán or Sonora), land production in this region is mainly maintained for self-subsistence purposes. That is, with the exception of a few products which feature in major national and/or export markets, like coffee, most agricultural production in this region is confined to small local markets or to family self-consumption.

c) As shown in Figure 3.20, this territory encompasses three out of six of the poorest states in Mexico, that is, with GDP per capita representing less than 60 per cent of the national average, Chiapas being the poorest state, with a GDP per capita representing just 42 per cent of the national average. As already mentioned, manufacturing is not that important in this region, when compared with other poor areas, such as Tlaxcala and Zacatecas, where the manufacturing sector is important and major industries like clothing and textiles are located. Hence, the tourist enclaves located in this region highly contrast with the general situation of their economies (see Figure 3.20).

d) Most of the population located in this territory live in rural areas, that is, in villages with less than 15,000 inhabitants, Oaxaca being the most rural state at the national level: 80.4 per cent of its population lives in rural towns.

e) This territory is also the locus of ethnic cleavages. In 1995, 43.4 per cent of the illiterate indigenous-speaking adult people (above 15 years old) lived in this area and were mainly concentrated in these three states.

f) Since 1994, the very year NAFTA came into force, this territory became the locus of a guerrilla uprising denouncing not only the social imbalances prevailing here, but the threats and negative impacts that NAFTA-like economic reforms have had on indigenous communities, mainly on the land tenure system, and their social organization. The fact that the *Ejército Zapatista de Liberación Nacional* is still confined in the Lacandona forest, despite its interest in becoming a civil political movement, and that other guerrilla movements have spread out in Guerrero and Oaxaca, suggest that social tensions and unrest are far from manageable.

g) After the signature of DR-CAFTA by the US, the Central American isthmus has become part, in many ways, of the North American space. Since that agreement is similar to NAFTA, that is, targeting state policies and market reforms regardless of the social costs of the restructuring, it is most probable that the southern periphery of North America will be

expanded to somewhere close to Nicaragua. This has prompted the need for structural reforms embedded in the history and social practices of the 'Mesoamerican' rural space. Some attempts have been crafted in the most recent years, such as a Mexico–US Partnership for Prosperity targeting the most deprived populations in Mexico or the so-called Plan Puebla Panamá (PPP), a sub-regional initiative targeting developing policies in nine southern states in Mexico and seven Central American countries. The scope and limits of those initiatives will be reviewed in Chapters 4 and 6.

# 4

# The Rise and Demise of Mexico's 'NAFTA-plus Approach': the Scope and Limits of a North American Agenda Coming from the South

## Introduction

This chapter will review how Mexico attempted to put forward its own agenda under a new post-NAFTA North America. The Mexican case becomes salient for many reasons because it shows the possibilities and the limits that weaker partners have in order to push forward their own interests within trade and political alliances. Since Mexico was reaffirmed as a cheap labor space looking for new opportunities through North–South integration (by enhancing trade specialization, attracting investment, or by exporting labor), from year 2000 migration became the major post-NAFTA issue to be negotiated by Mexico with the US. In spite of the formal integration of commodity and investment markets, and the informal integration of labor markets between the two countries, the migration agenda became subordinated, if not abandoned, once homeland security became the major concern of the US at the end of 2001. This chapter shall explore the rise and fall of Mexico's major post-NAFTA initiative called 'NAFTA-plus'.

Mexico's failure to put forward its own agenda could be partly explained by the very flaws of the Mexican strategy, but it also highlights the political asymmetry under which North American integration is taking place. Any integrative 'deepening' in the region must accommodate, not to mention reflect, major priorities of the US. The chapter

also analyzes how Mexico attempted to articulate a sort of 'development' agenda, gearing towards reducing the asymmetries reinforced by NAFTA within the country, and how the present and future of oil wealth became entrenched in the debate.

## Mexico's 'NAFTA-plus' according to the Fox administration

### The rationale and avatars of the 'whole enchilada' approach

From the beginning of the year 2000 to the fall of 2001, a kind of honeymoon between Mexico and the US loomed in the political relations of the two nations. The main reason was the increasing optimism of Washington elites towards democratic change in Mexico, the NAFTA partner that was then still run by an authoritarian political clique that had inherited power through non-competitive elections since the late thirties. Indeed, Mexico's presidential elections in the year 2000 became a watershed. Vicente Fox suddenly became the strongest and most credible rival to the Partido Revolucionario Institucional (PRI) candidate, Mr. Francisco Labastida, a man with a rather bureaucratic profile associated with political bosses of the now named 'old regime'. By contrast, Vicente Fox, supported by the Partido Acción Nacional (PAN), a conservative catholic-based party, appeared to be a charismatic and credible leader whose major goal while campaigning was to eject PRI's political clique from power and to inaugurate political openness and competition in the country. His campaign was so successful at attracting the support of some center-left small parties and groups, creating a major coalition beyond PAN's traditional constituencies, that it eventually led Mr. Fox to the presidency, in December 2000.

But another trait of Vicente Fox's campaign was to enlarge his political constituency beyond national borders. He intensively campaigned in New York and California, seeking the support of Mexican and Mexican-American communities whose electoral participation in the US is becoming more and more decisive in key bilateral issues, such as illegal migration and the social conditions of Mexicans in the US. In many ways Fox launched a double-edged diplomacy, the purpose of which was to send a message both to Washington and at home. While campaigning in the US he announced that the legalization of some three million Mexicans already working without documents in that country, and the liberalization of labor markets between the two countries would be major goals of his presidential term. Furthermore, he invoked the creation of a stronger North American community in which free labor

movement, institution building and development-oriented policies would be at the core of this major effort. The message was clear: Mexico took the lead to go beyond NAFTA and to deepen continental integration in which labor mobility and a development approach became the main goals. By so doing, the upcoming Mexican political administration was to enlarge a domestic constituency for supporting a further integration within North America.

Once in power, the Fox government better framed what then became known as the 'NAFTA-plus' project. In fact, Fox's alliances with center-left groups made it possible for Mr. Jorge G. Castañeda, a major critic of PRI's regime through his influential books and articles, to become the brain and the executor of what became known at the time as Mexico's 'new' foreign policy. This new foreign policy consisted in the opening of various fronts for Mexico's international participation. The very first one was to obtain a non-permanent seat at the United Nations Security Council, through which Mexico could participate on global issues, such as peace-keeping operations, or more contentious ones such as the right of intervention for humanitarian reasons.

The second front was to participate in the strengthening of institutional commitments with principled international regimes. Mr. Castañeda openly acknowledged that the country was enmeshed in an international arena in which Westphalian-based notions of sovereignty were being eroded. For him, the post-Cold War order could not be ruled on the principles of non-intervention and self-determination – principles to which Mexico's traditional foreign policy were attached – but on universal rules and principles to be valid and enforced worldwide (Castañeda, 2001a, 2001b and 2002; for a more detailed analysis of this foreign policy change, see Morales, 2006b).

The third front opened by Mr. Castañeda was the 'NAFTA-plus' strategy already sketched by Vicente Fox during his presidential campaign. A two-tier approach was devised around the strategy of linking the regularization of cross-border migratory flows with the need to reduce poverty and regional disparities within the country. Migration became the core of the Mexican initiative, as explained earlier. Though full mobility of labor became the Mexican goal in the long term, the legalization of around 3.5 million illegal Mexican workers[1] and the protection of their basic social and human rights became the short term target of the Mexican strategy. The regularization of this population became in fact a *sine qua non* for negotiating any other point on the migration agenda. In parallel to this, Mexico also focused on the negotiation of a guest worker program promoting temporal and regulated

Mexican migration for around 400,000 workers on a yearly basis.[2] Regularization of Mexican illegal workers already living in the US and the promotion of a bilateral guest worker program became in fact the two major pillars of what Castañeda coined as the 'whole enchilada'; that is, a whole package for regularizing human flows coming from Mexico to the other side of the Rio Bravo. Part of the package also claimed a lift in the caps on Mexican migratory visas already provided by the US government on a yearly basis, a border program focusing on the abatement of human smuggling and violence, and a program targeting the transfer of resources from the US to those communities where migrants came from in order to strengthen their development opportunities (Castañeda, 2006).[3]

At the beginning of his administration, President Fox and his team had the legitimacy and authority for advancing this 'NAFTA-plus' great idea to deepen the scope of the North American economic space, but the circumstances under which this new diplomatic approach was nested suddenly changed. The American economy went into recession at the turn of the new century, a recession which spread, although temporarily, all over the world. The terrorist attacks of September 11, 2001, to the twin towers in New York and the Pentagon premises in Virginia, abruptly changed all the parameters, notions and strategies of American national and international security. And last but not least, the lack of a partisan majority in congress for backing Fox's proposal, and the progressive disarray of his own cabinet,[4] made it much more difficult for Fox to pursue his ambitious 'NAFTA-plus' goals.

The rationale under which Mr. Castañeda built up his 'whole enchilada' approach was, in fact, sound. To claim the legalization of Mexican workers and their families living north of the Rio Bravo, and to pledge for a bilateral guest worker program geared to the acknowledgement of a de facto cross-border labor market operating between the two countries. Within this informal labor market, Mexico has traditionally played the 'push' factor, or the supply of a surplus cheap labor force, and the US economy the 'pull' factor, featuring a huge wage differential and job opportunities for Mexicans to work, although illegally, in the US.[5] In the past, the governments of the two countries had struck bilateral deals in order to regulate the temporal access and seasonal working of Mexican labor. This was especially the case during the Second World War and its aftermath when the US economy greatly needed Mexican labor. In 1964, however, the temporary working program with Mexico came to an end and the Mexican government launched the *maquiladora* program, whose main goal was to create job opportunities to deter Mexicans from migrating further north.

In spite of the relative success of the in-bound industry program, even during the post-NAFTA years (see previous chapter), Mexicans kept moving further north either legally or illegally. This was until the end of the eighties and beginning of the nineties, when illegal migrants who had arrived in the US before the mid eighties became fully legalized with a right to take citizenship, after the ruling of the Simpson Rodino Act of 1986.[6]

In spite of this full regularization of Mexican and other illegal workers, Mexican illegal migration did not stop, and in fact, it accelerated once NAFTA came into force. As of March 2006, the overall unauthorized population of the US was estimated to range between 11.5 and 12 million people, most of it being from Mexican origin, i.e. 6.2 million. 16 per cent of this population arrived in the US in the late eighties, while an additional 18 per cent entered during the period 1990–94. Rates of growth were progressively growing across periods; while numbers of unauthorized workers grew on average at 180,000 yearly during the eighties, they jumped to 400,000 yearly during the following period. Rates of growth jumped to 570,000 yearly during the years 1995 to 1999, and to 850,000 yearly from 2000 to 2005. In other words, 66 per cent of the overall illegal population estimated in the US arrived after 1994 (Passel, 2006: 2).

Difficult though it is to blame NAFTA as an additional 'push' factor on the Mexican side, the fact that it fell short of original over-inflated expectations in Mexico probably played as an incentive for Mexicans to migrate. At any rate, NAFTA did not stop Mexican migration from growing in spite of the arguments stating the opposite opinion during the NAFTA negotiations (see Alba, 2000: 35). However, Mexican scholars claim the financial crisis at the beginning of 1995 as a more credible explanation of the acceleration of the Mexican diaspora. Seasonal migrants coming from traditional depressed rural regions in the country, and that NAFTA did not help to modernize, is an additional reason explaining the diaspora jump. Furthermore, the existence of historical family and informal networks has traditionally nourished a continuous growth of unauthorized human flows (see Escobar, 2000; Santibáñez and Cruz, 2000).

It is important to highlight, though, that the new cohort of Mexican illegal migrants does not come from the edges of Mexican society. Most of them were not unemployed in Mexico when they took the decision to migrate, although certainly many of them were underemployed. More interesting, their level of education is in general terms above the average currently prevailing in the country, they come from the core of

Mexico's labor force (i.e. agriculture, construction, manufacturing and retail), and more and more from new states other than those located in Mexico's Central West, such as Guerrero, Oaxaca, Puebla and Veracruz (Kochhar, 2005: 3–9 and 29). In other words, the rationale to migrate for new cohorts of Mexican workers is not to escape from extreme poverty, but from poor and uncertain economic expectations and incentives prevailing in their local environment.

As the migration debate became heated in the US, it became clear that wage differentials and the dynamism of the US economy continue to attract and assimilate the new cohorts of illegal migrants. Irrespective of their labor background in Mexico, around two thirds of illegal workers who entered the US during the past 15 years are employed in four industries – agriculture, construction, manufacturing and hospitality (restaurants, hotels, etc) – and are settling down in new areas apart from the traditional ones (in California, or in Texas), such as Atlanta or Raleigh, where there is a steady labor demand from the construction industry, or New York City, where hospitality industries employ newcomers. The job concentration in these four industries is higher for unauthorized migrants than the average legal resident in America, suggesting that Mexican migrants are not necessarily competing with regular Americans in the job market.

Apart from being concentrated in those specific industries, illegal labor continues to be the cheapest labor force available in the US. The midpoint or median of the earnings distribution of new cohorts of migrants is $300 per week, well below the median wage of $360 per week for all foreign-born Mexican workers and $384 per week for all foreign-born Hispanic workers in the US (Kochhar, 2005: 22). Consequently, the US economy is benefiting from a burgeoning labor force coming from Mexico which is better educated than the average Mexican and is paid below the bottom of formal wages.[7] These figures clearly show how Mexican migration is not only providing a 'subsidy' to specific industries in America, but how the reserve of cheap labor coming from Mexico operates at the cross-border level. In fact, three sorts of linkages connect Mexico's labor reservoir with the American economy: the bulk of the *maquila* trade, the flow of illegal migrants to the US who remain a cheap labor force, and the flow back to Mexico of remittances for compensating income shortages in their communities.

This said, President Fox's 'whole enchilada' main arguments had the merit of putting at the core of the negotiations the formalization of a de facto labor market already operating between the US and Mexico. Since a borderless economic space was emerging between the two countries, it

made sense to make the first steps for formalizing the integration of labor markets. It also made sense to launch social and developmental policies in order to stimulate the creation of job opportunities in those regions traditionally compelling people to migrate. Although the developmental agenda was not fully articulated by the Fox administration, it became clear that the simple liberalization of labor markets was not enough to stabilize labor markets between the US and Mexico. The need to embed market mechanisms according to the particularities of Mexican social organization became highlighted. Inspired rather by the integration experience of Europe, the possibility of establishing a sort of 'social fund' was even suggested, as will be reviewed later in this chapter.

However, the importance of the 'NAFTA-plus' proposal highlighted the limits and ideological biases under which NAFTA was constructed. Corporate America, the Washington consensus, and neoliberals championed the liberalization of markets and investments, but have remained completely silent about the liberalization of labor markets. They advocate more flexible labor conditions but refuse to accept the regionalization and globalization of labor trends. Mexico's 'whole enchilada' was not unorthodox in terms of the neoliberal credo; it became, however, very controversial and eventually was defeated, just to remind us that markets of any kind remain open or closed according to political and social calculations. Though President Fox's strategy was sound in economic terms, its major flaw was the political feasibility of such an ambitious project.

Last but not least, the 'NAFTA-plus' strategy reasserted once again the economic functionality of the Mexican space in North America: a space of manufacturing relocation thanks to the proximity to the two 'continental spokes' (i.e. California and Texas, see the previous chapter); a platform for cheap assembly production (*maquila*); and a reserve of cheap labor compelled to migrate to the US (and Canada more recently), and obliged to complement family incomes in the abandoned regions through remittances. When Mexico joined NAFTA, negotiators of the time highlighted low costs of labor as the 'comparative' advantage of the country. The post-NAFTA era seems to reinforce this functional positioning of the Mexican space, without even regaining historical rates of growth witnessed during the golden years of state-led industrialization. Furthermore, in a post-NAFTA era, Mexico has failed to articulate imaginative state-led development policies and has made of the migrant – who at the same time has become more targeted and stigmatized by the politics of security in the US – a pivotal axis of market-led infrastructure development in migrant towns.

## The functionality of erecting a barricaded border

According to the Fox administration, the migratory agenda was derailed in the US after the shock of the terrorist attacks of September 2001. However, it is difficult to believe that the goodwill of the two presidents would have been enough to overcome the principles, procedures and interests behind the elaboration of American migratory policies. American political elites and key sectors of the public opinion and voting population do not perceive labor markets with Mexico or any other country as 'informally' integrated. They perceive their country rather as a very successful economy pulling different types of talented people from all over the world. This explains why the American government has maintained migration quotas on a yearly basis in order to establish an orderly and legal migration from different parts of the world.

By contrast, unauthorized migration, though tolerated for decades, has traditionally been perceived in the American establishment as a breach to its own migratory laws and hence a violation to its sovereign right to decide who enters and circulates within its territory (cf. Torpey, 1997). Though the crafting of NAFTA was nested in a trilateral debate stressing the complementarities and interdependence of the three economies, migratory issues remained a sovereignty-centered policy for the three countries. In this sense, Washington never felt obliged to discuss or consult migratory issues with its two neighbors.

The major flaw, thus, of the 'whole enchilada' strategy is that it overestimated Mexico's bargaining capabilities vis-à-vis Washington, and wrongly underestimated the political complexity that constantly shapes American migratory policies. The major signs of that complexity were already manifested along the Mexico–US border before and after the signing of NAFTA. While NAFTA set the possibilities of building a business-friendly border between the two countries, the growth of illegal trade – mainly illicit drugs – and unauthorized migration, fueled in part by the burgeoning of a 'borderless economy', reinforced the need in the US to police more severely its border since the set up of NAFTA.

It was precisely in 1994 when the US Immigration and Naturalization Service (INS) – now absorbed under the Department of Homeland Security (DHS) – launched an aggressive multi-year strategy called the 'National Strategic Plan' (NSP), aimed at enforcing migratory laws at the southwest border, that is, along more than 3,500 km with Mexico. The NSP was realized in a strategy known as 'Prevention Through Deterrence', of which the goal was to deploy a massive build-up of agents and resources in the front line in order to deter the entry of illegal

aliens, instead of arresting them once they have already entered the country. This massive concentration of human and material resources, which included the build-up of physical barriers at specific points of entry, focused on the policing of major border urban settlements through which the highest levels of illegal migration took place (Seghetti et al., 2005: 21–2).

Thus, the emergence of a barricaded border at the turn of the century was done under the principle that the US maintains a 'state monopoly' for deciding who is entitled to enter and circulate in its own territory. This sovereignty-centered principle highlighting the monopoly of states for deciding the modalities of circulation of 'aliens', and that contrasts with the parallel 'pooling of sovereignty' that NAFTA ensured on trade, investment and corporate rights issues, was at the grounds of a political rebordering of the US–Mexico economic space until very recently. It was the shock of the terrorist attacks of 2001 that prompted Washington to a geopolitical rebordering of the whole region under different principles. This will be analyzed in the following chapter.

The barricading of the southwest border became, however, a 'politically successful policy failure', as Peter Andreas correctly labeled it (Andreas, 2003: 4). It became a policy failure because it failed to deter illegal migrants from trespassing the border. As I previously mentioned in this section, it was from the second half of the nineties that the increase in unauthorized migrants accelerated. Strategies such as Gate Keeper deployed at the San Diego border or Hold the Line as implemented in Cd. Juárez-El Paso, just rerouted migrants and smugglers to more hostile or sophisticated roads, such as the Arizona desert, sea routes, etc. Migrants became more vulnerable when trespassing the line, increasing their risks for losing their lives, but they were not deterred from finding a better-paid job in the US. Although the US Border Patrol (USBP) argues that this 'preventive' strategy reduced the criminality in major urban centers such as San Diego or El Paso, the numbers show that the massive build-up did not fulfill its major goal. By contrast, the strategy became a political success for domestic purposes: the USBP became better funded and reinforced, borderline populations perceived their cities becoming more secure and the federal government sent the symbolic message that it was concerned and doing something to curb the entry of illegal aliens, and hence raising the support of specific constituencies.[8]

The fact that border politics is intended to raise political gains domestically rather than effectively deter illegal migration (which is highly demanded by specific industries in the US), became reinforced during the second term of the Bush administration. In parallel to the

discussion in the upper and lower houses of Congress of an eventual regularization of unauthorized workers in the country, and the possibility of striking a guest worker program for Mexicans, President Bush and the lower house voted at the end of 2006 for the building of a border fence 1,500 kilometers long. Though the funding and feasibility of this 'Berlin-like wall' (as Mexicans perceived it) is yet to be ensured, the reinforcement of the barricades in the southwest line conveys exactly the same message as the 'Prevention Though Deterrence' project initiated in the aftermath of NAFTA: it will certainly make it more difficult and dangerous for smugglers and illegal human flows to trespass the line, it will probably neither deter nor curb their entrance, and it has reinforced the sovereignty-centered discourse, supported by nationalistic constituencies, that the US is still capable of deciding the mobility of 'aliens' in its own territory.

The vote for constructing this 'Big Wall' at the end of 2006 buried the spirit in which Fox's 'whole enchilada' initiative was presented at the beginning of his administration. Betting at 'rebordering' labor markets between the US and Mexico, as part of a Mexican strategy for 'deepening' the North American economic space, a stronger barricaded border between the two countries ironically emerged at the end of the Fox administration. The barricades will probably not restrain Mexicans and other than Mexicans (OTM) from crossing the line, but for American society they have become the material and symbolic evidence that its government still has the power for deciding who is entitled to circulate in the homeland. By contrast, the escalation of the barricades along the Mexican front line became the anticlimax of the continental 'deepening' trend sponsored by Mexicans at the turn of the century. NAFTA did not prove to induce a 'spill over' on other critical related areas such as labor markets and development. The trade and investment partnership did not prove to be extendable to other areas of Mexico–US negotiations.

## The nesting of a bilateral 'Partnership for Prosperity'

In spite of the setbacks witnessed in the migratory front of the 'NAFTA-plus' approach, President Fox was successful in negotiating a so-called 'Partnership for Prosperity' (PP) through which transfer of technology and resources between the US and Mexico could be facilitated. The alliance was announced in the midst of a summit of the three North American chiefs of state, held in Monterrey during the United Nations Conference on Funding for Development, in March 2002. PP was

originally anchored in four pillars: 1) access to private investment for small and medium size enterprises; 2) transfer of technology through targeted projects involving small entrepreneurs and American universities; 3) upgrading of infrastructure; and 4) promotion of institutional interconnectedness.

A major goal of this alliance was to reduce the costs of remittances transferred by Mexicans living in the US, regardless of whether they were legal or not. According to this plan, those resources originated in the US could now help to finance private construction projects, mainly private dwellings, to migrants' families living in Mexico. Projects for obtaining credits in the US to be disbursed in Mexico were also announced. The promotion of US franchises and tourist-oriented development projects were also considered. These market-based mechanisms had the goal to stop illegal immigration to the US, by rooting Mexican families to their own localities. This new economic alliance also claimed the promotion of Mexican handicrafts in the US, through institutional mechanisms, and to skill medium-size enterprises to get funding for their projects. The promotion of new investment in infrastructure, such as transport, power transmission, telecommunications, amongst other sectors, was also announced as well as the coordination among major multilateral institutions, such as the World Bank, and regional ones, like the Inter-American Development Bank (IDB), in order to fulfill this task (Sojo et al., 2002).

Though this 'development alliance' was publicized when Messrs. Fox, Bush and Chrétien met in Monterrey during the UN conference, this alliance engaged only the US and not Canada. Though the golden goal of this partnership was announced as to 'contribute to productivity increases in the parts of Mexico where growth has lagged and fueled migration' (US Department of State, 2002: 11), it never came out with a comprehensive strategy for dealing with the problem. In fact, so far the 'partnership' has featured fragmented projects for dealing with ad hoc issues. In some way this alliance was rather announcing the privatization of development policies in Mexico, through which originally public development banks and public programs targeted deprived populations through the transfer of resources from the better off. What became most ironic in this alliance was that Mexicans living in the US were anticipated to become major actors for propelling development in their country of origin. Their remittances became suddenly a strategic means for funding development programs in Mexico, while at the same time the entrance of Mexican labor in the US had become more and more barricaded.

In other words, the PP rather reinforced the neoliberal spirit in which NAFTA was crafted, betting to 'harness the power of free markets to boost the social and economic well-being of citizens, particularly in regions where economic growth has lagged and fueled migration' (US Department of State, 2002: 2). Announced as a public-private alliance, it introduced the idea that development gaps could be overcome through market incentives, trade integration and the active participation of private capital coming from either the US or Mexico. For Mexican standards, this bilateral deal introduced a new paradigm for overcoming social and economic inequalities through market mechanisms and incentives for the participation of US and Mexican capital. It is clear that the spirit of this strategy did not match the original idea of Fox's 'NAFTA-plus' vision of reducing income gaps between the US and Mexico and between north and south within the country. The bilateral partnership became, however, a political compromise through which the Mexican government could renew the promises of NAFTA for achieving development goals in Mexico.

During the span of its short existence, PP has been successful in formalizing and enhancing the remittances market between the US and Mexico, a market that has become crucial in Mexico's income coming from abroad. In year 2005, for example, remittances amounted to more than US$20 billion of foreign income, ranking only second to overall exports of crude oil. Remittances have also been targeted by agencies of some state governments in Mexico, offering three times the investment done in public works by families benefiting from remittances.[9]

Apart from the remittances market, PP has also launched a myriad of projects, most of them still in an exploratory phase, targeting the transfer of credits and resources to support infrastructure projects, upgrading skills for medium and small enterprises, strengthening capabilities in specific sectors, and facilitating cooperation between financial agencies, universities and research institutes of the US with their respective Mexican counterparts.[10] Though the purpose of this bilateral partnership is to target infrastructure needs and firms' skills and capabilities that NAFTA by itself will not do, its future and success is uncertain. In March 2005, 20 months before President Fox left power to his successor, PAN's presidential runner Felipe Calderón, who began a new administration in December of 2006 after a contentious election, President George W. Bush announced the creation of a so-called Security and Prosperity Partnership (SPP), this time encompassing not only Mexico but Canada as well. The nature and content of this emerging trilateral security and 'prosperity' regime will be analyzed in the following

chapters. Somehow, it is important to highlight that the focus of the 'prosperity' or economic dimension of the new trilateral alliance is not necessarily targeting development gaps between Mexico and the two other North American partners. The target has rather shifted towards increasing the competitiveness of the overall region, giving special importance to the continentalization of energy markets.

## Is there room for the 'developmental' state?

The bilateral alliance between Mexico and the US under PP was in part a response to a major claim made at the beginning of the Fox administration under the 'NAFTA-plus' strategy. It failed, however, to create the funding for new investments needed to create job opportunities in Mexico's deprived regions, according to the original vision of the 'NAFTA-plus' strategy. According to Fox and his Foreign Minister at the time, Jorge Castañeda, the problem of Mexican illegal migration to the US could not be solved if the 'push' factors at home were not tackled. Since NAFTA was not effective for creating new job opportunities in those regions compelling workers to migrate, a new development strategy should be devised in order to raise the incentives for would-be migrants to stay.

Castañeda's original idea was to link Mexico's oil resources as a bargaining leverage for building a sort of regional investment fund, backed by the US and eventually Canada, in order to increase public and private investment in Mexico's migratory regions. When international oil prices started to escalate, at the turn of the century, and after the terrorist attacks of September 11, it was evident to him that oil became again a strategic commodity from which Mexico could yield more than just market benefits. Oil was put in the bilateral agenda of the early years of the Fox administration in order to make Mexico a reliable and safe supplier, along with Canada, to the US, at a juncture where even Saudi Arabia had ceased to play that role (Interview with Castañeda, 2006).

Once he quit the Fox administration, and became an independent candidate for the presidential elections of 2006, Castañeda better articulated his position, and proposed that Mexico should create a North American Energy Fund (NAEF), backed with US securities and investment funds, from which Petróleos Mexicanos (PEMEX) could get the money for doubling its exports. Castañeda became in fact the first public personality to suggest that Mexico should increase its oil exports in order to reap the economic and geopolitical benefits of becoming a strategic and reliable partner of the US. According to him, to double Mexican exports in a

period of escalating prices would guarantee the reimbursement of the NAEF, and create the possibility of a parallel fund, a so-called Mexican Development Fund (MDF), from which infrastructure and development projects would be supported in order to multiply the benefits of a new oil bonanza. This formula of trading oil exports for development projects had the advantage, according to him, that no constitutional amendment was needed in order to make it feasible (Interview with Castañeda, 2006).

The proposal of increasing Mexico's oil output in order to support a sort of regional investment fund has not yet found an echo within the political circles of the country. However, prestigious academics and think tanks have further enriched and nuanced this proposal, making of it Mexico's 'Big Idea' for deepening regional integration in the region.[11] Robert Pastor has become the most prestigious and independent academic that has better elaborated, so far, the conditions and possibilities for establishing a North American Investment Fund (NAIF).[12] The rationale of his proposal stems from a thorough comparative analysis between the European integration experience and North America's. Conscious that the North American integration process follows a different strategy and architecture to that followed by Europe, he convincingly suggests that the latter entails some good lessons that North Americans could assimilate.

One of those lessons is precisely the role and impact of the so-called cohesion funds in those poorer countries joining the European integration process during the seventies and eighties of the past century. It is well known, indeed, that countries like Spain, Portugal, Greece and Ireland have narrowed their income gaps vis-à-vis the richest countries in the EU, i.e. Germany, France or Italy, during the past 20 years. By contrast, his argument follows, since the inception of NAFTA, Mexico's GDP per capita, regardless of how it is measured,[13] has increased more slowly relative to US per capita growth. While income convergence prevails in Europe, in part due to the impact of regional cohesion funds, income gap has widened between Mexico and the US in spite of NAFTA and the integrative trends that have prevailed in North America during the past 14 years. This trend could be reverted, according to Pastor, if a European-like regional investment fund is established in order to finance deprived regions in overall North America, but mainly in Mexico's south.

The creation of a NAIF could be a bright idea, but it could turn into a great failure if its functioning and operations are badly designed. According to a study funded by the North American Development Bank (NADB) (Robinson et al., 2005), Mexico needs to grow at a rate of

6 per cent during the next 20 years if the income gap with the US is to be reduced by half. To do so, Mexico needs to invest around US$17–20 billion per year, mainly in infrastructure development and human capital, two strategic variables which are thought to increase overall productivity. Since such an amount cannot be funded entirely by foreign savings, Robert Pastor suggests that half of it could be raised domestically, if the Mexican government dares to articulate an aggressive fiscal reform.[14] The other half, that is, around US$10 billion annually, could be afforded through a NAIF whose resources could be funded by US investors to 90 per cent, and Canada's by 10 per cent. Though the funds could be used for helping lagging regions within the overall North American space (following the European example), most of them should be committed to fund infrastructure and human capital in Mexico's south, with the clear purpose of integrating the most lagging region of North America to the dynamism of the continental trend. The proposal is believed to be a win–win project since a faster Mexican growth will increase Mexican imports from the US and Canada.

Since sound national policies also proved to be crucial for narrowing gaps in the European space, Pastor argues that the setting and implementation of the NAIF must also be conditioned to a further restructuring of the Mexican economy (fiscal and energy reforms, for instance) and Mexico's judicial system. The question of conditionality for the establishment of a NAIF has become crucial for other key American publicists. In a task force called by the US-based Council of Foreign Relations, a think tank editing the influential magazine *Foreign Affairs*, all participants from the three countries sponsored the benefits of creating a NAIF. However, key American participants in that task force, such as Carla Hills, made clear that prior to the establishment of such a fund, Mexico should continue the restructuring of its economy according to market-oriented and transparent-oriented policies (Council on Foreign Relations, 2005).

In parallel to the discussion about the merits and possibilities for establishing a NAIF, the Fox administration launched an ambitious project for developing infrastructure in deprived regions under the so-called Plan Puebla-Panamá (PPP). In contrast with PP, the PPP acknowledged a regional approach for tackling economic gaps in southern Mexico and became an innovative mechanism devising cooperation between Mexico's deprived south and Central American countries, most of them, with the exception of Costa Rica, exhibiting similar economic and social imbalances to the Mexican south. Funded initially with Inter-American Development Bank (IDB) resources, the PPP tried to attract funding from public and private sources within the sub-region in

order to build and/or improve a 5,000-kilometer-long Pacific corridor going from southern Mexico up to Panama. It also tried to build a so-called 'Atlantic corridor' with the purpose of linking the State of Veracruz up to the Cortés port in Honduras. Funded through the same mechanisms, the PPP aimed to build a 1,830-kilometer-long electrical grid interconnecting all six Central American countries (Inter-American Development Bank, 2002: 138–41).

Although the construction of infrastructure could eventually boost the potentiality of the sub-region, it is not clear whether building the two above-mentioned corridors, linking Central America with central Mexico, will be the most appropriate policy. As some studies have suggested, just building roads in deprived regions does not necessarily lead to the improvement of productivity. The development and rationalization in the exploitation of key ports and airports could be more crucial (Esquivel et al., 2002). For the Mexican south, the construction of a coastal road, linking Chiapas or Oaxaca with key ports in the north Pacific, could be more crucial than linking them to the south. In fact, the PPP attempted to link deprived regions among themselves, with no clear connection with any economic hub. During the Fox administration the PPP lacked funding and social support. Criticism was raised throughout the region for not responding to the interests of the most deprived populations, and rather favoring corporate and business interests.[15]

During the Felipe Calderón administration, which began in December 2006, a renovation of this 'south–south' collaborative project was activated. In March of 2007, a summit of state representatives of the former PPP members, plus the president of Colombia, took place in Campeche, Mexico, announcing new members and projects for the initiative; i.e. Colombia joined as a permanent party and Dominican Republic (DR) and Ecuador will join as 'associated' members. Since Mexico withdrew from the G-3 FTA with Venezuela and Colombia at the end of 2006, the enlargement of the PPP with the latter country has given a sort of political profile to the initiative. If so, development priorities will be once again subordinated to political and strategic imperatives (i.e. to secure the southern border) pursued by Mexico in the region.

## The politics of oil wealth. The challenges for keeping Mexico in the continental energy market

As previously said, the link between oil wealth and development policies was established within the 'NAFTA-plus' strategy pursued by the Fox administration. The migratory aspect of this strategy became the major

point in US–Mexican relations during the most recent years and the inception of a PP and the surrounding discussion about the pros and cons of establishing a NAEF became its corollary. Consequently, the prospects for expanding Mexico's oil production have become at the grounds of post-NAFTA development policies for the country. However, oil came back to the center stage of North American politics and economics not only as part of a Mexican strategy for exploring new funding possibilities to improve the Mexican south, but as part of a US agenda focusing once again on energy security at the turn of the century, and, certainly after the attack of the Twin Towers. In the last chapter of this book I shall review how the continentalization of energy markets has become a major pillar of the 'prosperity' dimension of the SPP. In this section I shall explore how the prospects for keeping or increasing Mexican oil exports became rapidly politicized under partisan cleavages during the second term of the Fox administration, and how this eventually undermined any connection between energy resources and development policies.

## The sustainability and potential increase of Mexico's energy output

According to Mexico's Constitution and energy-related regulatory legislation, hydrocarbon resources belong to the State and it remains the only entity to explore, develop and produce hydrocarbon resources. This also includes the generation and distribution of electricity, nationwide, and downstream activities in the case of crude oil. Until 1994, when NAFTA came into law, no private participation – either national or international companies – was allowed in Mexico's energy sector, with the exception of turn-key projects and subcontractors providing specific services to one of the two major state monopolies: Petróleos Mexicanos (PEMEX) and Comisión Federal de Electricidad (CFE).

Mexico's legislation reflects its own history, throughout which state energy monopolies played a major role for industrializing the country during most of the twentieth century. The two companies became icons of nationalism and state-led policies promoting growth and welfare during the second part of the twentieth century, by keeping domestic energy prices below international levels. Since this monopoly survived NAFTA (see Chapter 2) the Mexican government may still differentiate between national and international markets when fixing energy prices. From the early eighties up to the present, when PEMEX became a major oil exporting company, it became as well the major source of fiscal income for government (currently 35 per cent of overall government

income). From then on, all succeeding governments, up to the current Calderón administration, have used this oil rent for state purposes.

In other words, the monopoly over hydrocarbon resources became a strategic tool and income source in the hands of the state for pursuing ambitious social and macroeconomic policies. The use (and misuse) of this fabulous oil rent made possible the financing of the so-called 'oil boom' of the late seventies and early eighties, during which oil production almost tripled. When international prices collapsed and Mexico's foreign debt skyrocketed, the oil rent became the guarantee of the repayment of 'fresh loans' that the government needed during the eighties and early nineties (see Morales et al., 1988). In early 2005, after the peso crisis and the financial bail-out prompted by President Clinton (US$20 billion in loans) was put in place, Mexico's oil rent and reserves became the backbone of the whole financial architecture.

Thus, keeping the oil monopoly in the hands of the state is a matter that goes beyond historical, nationalistic and policy considerations. For the Mexican government, the administration of an oil rent (either for the better or for the worse) has become strategic for funding government expenditures and for backing a growing foreign debt, both from government and PEMEX. That is why no major actor within the Mexican political elite, attempting to impact Mexican public opinion, dares to suggest, at least openly, a privatization of the oil sector if he or she doesn't want to risk his (her) own political career. So far, nobody has seriously raised the point of privatizing the state monopolies. What became an issue during the second half of the Fox administration was how to modify (or not) the investment climate in the energy sector in order to widen the scope and possibilities of private capital participation in order to maintain, even increase, the energy output of the country.

Indeed, the sustainability of Mexico's oil and gas production is currently at stake. During the past 15 years most investments in PEMEX were channeled to increase production, and consequently exports.[16] If this could be explained by succeeding money-hungry governments pressed by international creditors or domestic constituencies, the final outcome was a serious decline in Mexico's proven stock of crude oil, and a deficit in gasoline and natural gas production for supplying a growing domestic demand.

The dramatic fall in proved reserves[17] of the past recent years is explained by a reclassification made by PEMEX in 2003 (in order to comply with international standards), and by the inability of the company to compensate for the depletion of its stock with additional reserves. Still more concerning is the fact that most current oil production

is sustained by just one field, Cantarell, the offshore reservoir located south of the Gulf of Mexico. In 2004, 72 per cent of oil production and 17 per cent of natural gas came from this highly productive field (Petróleos Mexicanos, 2005). Experts estimate that this wealthy field is about to begin its decline, halving its production by the year 2010 (Baker, 2005).

The Secretary of Energy and the Director of PEMEX in the Fox administration conceded that Mexico needed to maintain annual investments reaching 10 Bdls if Mexico's oil production is to be sustained and even increase to 4 Mbd. According to them, investments should be as high as 15 Bdls annually, or 25 Bdls during the following 12 years, if Mexico wants to increase its production to 5 or 6 Mbd, respectively (Shields, 2005: 87).

During the Fox administration investments increased compared to previous years, reaching almost US$11 billion in 2004. However, since 1997 more and more of those investments are not being made by PEMEX, but by outsourcing services in drilling and exploration to private companies. Those companies raised the funding and once their services were accomplished, PEMEX started paying them with the additional income it got from them. This formula, labeled in Mexico as infrastructure projects whose payments are re-scheduled for public expenses purposes (known as *pidiregas*),[18] began functioning during the Zedillo years, but President Fox made it the backbone for financing new investments in the oil and gas sector.

In 2004, 90 per cent of PEMEX overall investments were funded by private companies through this mechanism (PEMEX, 2005: 8). The Fox administration praised this investment design as the way to go if PEMEX wanted to maintain and/or increase its production while maintaining the constitutional gridlocks pending in this industry. At the same time, this formula released the government from diverting its oil rent for funding the recovery of its oil reserves and other energy-related projects. As in the past, the current administration kept 'confiscating' most of the PEMEX revenue.

From 1998 to the present, PEMEX has been operating under a financial deficit, since the Ministry of Finance levies more than 60 per cent of the company's revenues, in spite of the windfalls of the recent years. Ultimately, if private investments funded through the *pidiregas* formula are not paid directly by PEMEX (because of this huge transfer of resources), they become a liability for the company or for the Mexican government. This has raised the criticism of opposition parties to this formula, because it prevents a major reform to the fiscal regime of the state company, and at the same time it has obscured the level of its indebtedness.

In fact, the way that new investments have been funded in recent years in the oil and energy sector, has unleashed a major debate in Mexico on the sustainability of the status quo or the need to look for a new investment regime in the industry. There was no agreement during the Fox administration on this, and this was part of the debate during the presidential campaign of 2006. Currently, there is a general consensus that the status quo is not sustainable. The differences explode when the debate is turned to the nature of a new investment regime for the industry. This has been very well reflected in the case of gas and power generation.

NAFTA made it possible for private utilities to participate in the production of electricity and in cross-border transactions if they were small producers, or were producing for self-consumption or through co-generation. In all cases power production was understood as a surplus that a company had and that it could be traded only through the national transmission network, in the hands of CFE, the Mexican power monopoly.

In August 2002 President Fox submitted an initiative (which was never voted) geared towards a constitutional amendment which would have entitled private power producers to generate and commercialize electricity. According to this proposal, the monopoly of the state was confined to the supply of power in the category of 'public service'. The proposal envisaged two types of consumers, residential and small users whose power needs were guaranteed by state-owned enterprises, under the 'public service' category, and big or industrial users whose needs were planned to be covered either by state enterprises or private ones. However, the proposal envisioned that the threshold distinguishing between 'small' and 'big' consumers would be progressively reduced, so the former could eventually access the electricity markets of private producers.[19] The transmission grid would remain a 'natural monopoly' under the state's control. Under this initiative, CFE and Luz y Fuerza del Centro (LFC)[20] were to remain state companies, but the transmission grid would have come under the control of an autonomous public body guaranteeing the functioning and open access of the national grid.

The rationale of Fox's proposal was grounded in the need to increase power generation capacity by around 32,000 megawatts (MW) in the coming decade, a capacity growth that the two state-owned companies could not afford due to their financial restrictions. The reform was also heavily needed, according to this proposal, since technological changes had reduced the construction of power plants and the costs for generating electricity, so private competition could be encouraged in an area which traditionally was considered to function as a natural monopoly.[21]

Fox's proposals were severely dismissed by members of the PRI in the Senate, led at the time by Senator Bartlett, who articulated what I could call the nationalistic vision of Mexico's energy reform. The rationale of this position embraces both technical and principled considerations. On the technical side, this 'nationalistic' position dismisses the argument that CFE has not the financial capacity to respond to an increased demand in the coming years. Since growth in demand has been overestimated in official figures as well as the requirements for new investments, PRI Senate members estimated that state utilities have enough resources and capabilities for funding a more realistic growth in future demand. However, the major argument against a gradual privatization of electricity markets stemmed from the conviction of these senators, shared at the time by many members of the left-wing *Partido de la Revolución Democrática* (PRD), that electricity generation should still be considered a public, strategic good, and not a commodity. Private businesses should be kept out of this industry, whose main goal is to avoid profit, maintain open access to the grid and compensate through subsidies deprived social sectors. There was also the fear that a gradual privatization of the sector could eventually give private utilities enough market power to impose their prices, despite federal regulation.[22]

In the natural gas domain, what was distinctive of the Fox administration was the enlarged participation of private investors in the development of the Burgos Basin. This gas reservoir, located in northern Mexico with attractive reserves of non-associated gas, became the target of Fox's energy policies in order to abate growing imports of natural gas for that particular region. Mexico still has a large amount of gas reserves, although most of them remain associated with oil or remain prospective. Furthermore, PEMEX has traditionally lacked enough transmission pipelines in order to supply the growing level of consumption from northern industrialized states, especially Nuevo León, whose capital, Monterrey, has become the major post-NAFTA industrial site in the country (see Chapter 3). Imports from Texas became more attractive than pumping gas from southern fields. When the country shifted to gas for substituting fuel and residual oil as a feedstock for producing electricity in the nineties, demand for natural gas increased dramatically, lifting imports to 27 per cent of current domestic consumption. If consumption trends keep this pace, imports could become 50 per cent of overall consumption in the year 2012 (Shields, 2005: 63).[23]

This is the reason why the development of the Burgos Basin became important for the Fox administration, since this reservoir contains

non-associated gas and its production could easily supply additional gas to the Nuevo León region. From 2003 to 2005, PEMEX bid what has been called Multiple Service Contracts (MSCs) for developing Burgos. MSCs continue the PEMEX tradition of outsourcing specific services the company cannot develop itself. However, the difference this time is that MSCs encompass several services in just a few companies to be developed in the span of 15 to 20 years. They are long-term clustered contracts. As in the past, these contracts do not allow for any share or participation in Mexico's gas reserves or production. A fixed amount is paid for the services provided by companies on a yearly basis, regardless of the output they get from the gas fields they develop. According to PEMEX's estimates, US$5.9 billion has been invested by private companies through this mechanism, which will let them boost gas production from the Burgos fields up to 605 million cubic feet daily (MCFD) in 2008 (see www.csm.pemex.com/).

MSCs were criticized, however, for several reasons. They did not attract any of the major oil and gas companies, perhaps because they are not allowed to have a share of gas reserves. Since a fixed amount is paid to service contractors, the development of some fields could become more expensive than anticipated if their productivity is not high. A major criticism came, however, from opposition parties, arguing that MSCs violated the Mexican Constitution, since they let private companies drill and keep maintenance services in exploration and production activities. This time, Senator Manuel Bartlett was not successful in challenging the legality of these operations in the Supreme Court of Justice. Nevertheless, he attempted to block them before civil tribunals, though unsuccessfully (Fuentes, 2005).

The fact that MSCs remained controversial in Mexico discouraged potential investors in the Burgos Basin, and heated the debate about the need to change the status quo in the energy sector of the country. The debate split in two directions: while President Fox proposed a constitutional change in order to let private investors legally and clearly participate in the exploration and production of non-associated gas, congressmen heatedly debated the need to push a fiscal reform to partly reduce PEMEX transfers to the Ministry of Finance. Since the company was transferring more than 60 per cent of its gross income to the Treasury, a tax cut was badly needed in order to raise money for urgent investments and expenditures. The battle for this cut in taxes became rapidly politicized and entangled with partisan positions in both Houses of Congress. Each of them made their respective proposals in mid-2005,

only to be recast after a veto coming from President Fox. The tax cut, which set the basis of a future and more ambitious fiscal reform for the energy sector, was passed at the end of 2005.

Fox's plea for opening exploration and production activities in the gas sector to private companies and fiscal reform finally passed by Congress framed in many ways the debate of the so-called 'energy reform' with which the current President, Felipe Calderón (2006–2012), must come to terms. Calderón's proposals claim to continue and deepen Fox's failed reforms in the electricity, gas and oil sectors. When he was at the head of the Ministry of Energy (2003–2004), he defended Fox's initiative for privatizing electricity markets before the Senate, whose main opponents were members of the PRI. From then on, the rationale of Calderón's position has been to abate domestic energy prices as a condition for redressing the competitiveness of the Mexican economy. According to Calderón's estimates, the cost of generating power from CFE is twice as much compared to the costs for independent producers. If private producers are allowed to enlarge their market shares along the lines of the proposal already submitted by President Fox to Congress, domestic prices of electricity will go down. This would also be true for gasoline, the price of which could also be reduced if private investors are allowed to participate, jointly with PEMEX, in downstream activities.

Calderón and his team also argued during the presidential campaign that technological skills for exploiting Mexico's potential reserves located in the Gulf of Mexico cannot be obtained in arms-length markets, so they suggested that the only way to develop new reserves for sustaining current production levels was to craft 'strategic associations' between PEMEX and private oil companies, a measure which most probably will need a constitutional reform. Gas imports are anticipated to continue growing, so they will be supplied by the US and by growing imports of Liquefied Natural Gas (LNG). Since imports from the US are expensive, impacting domestic prices of both gas and electricity, Felipe Calderón preferred to increase imports from overseas via LNG shipments, as a means to reduce domestic prices. He also introduced into the debate a new legal designation for gas, for 'self use' purposes. This new category would allow private industries to produce natural gas as a feedstock for final products, such as electricity or petrochemicals. During his presidential campaign, he also advocated a fiscal reform aimed at further increasing the resources of PEMEX, coupled with changes in the governance of the state enterprise in order to make it more accountable, transparent and less overstaffed (Calderón, 2005 and interview with Cordero, 2006).

# Part III

# Re-shaping the Geopolitical Space of North America and its Contours

# 5

# Policing Borders in North America after September 11: From Barricaded Borders to the Growing Governmentalization of Human and Material Flows

## Introduction

NAFTA was not conceived as a mechanism for promoting political cooperation, let alone strategic integration among the three North American nations. After September 11, the region seems to have rapidly moved toward a continental security regime. After the terrorist attacks to the US, the geopolitics of borders became heavily grounded on a generalized politics of fear in the region, by which Washington pursues its own war against terror through military, political and institutional means. Although the building and proliferation of 'barricaded borders' continues to be a pillar of this strategy, I argue in this chapter that a more subtle and, perhaps, more effective security regime is emerging in the region betting to a soft power technology of governmentalization of human and material flows. The ultimate goal of this emerging regime is to permanently oversee and tactically intervene on the daily movement of cross-border flows within and throughout North America. In contrast with the 'politics of borders' pursued before September 11, the new 'politics of fear' seems to defuse the national fragmentation that prevailed in the past and to make of North America a geopolitical fortress ready to maintain a long and lasting 'war against terror'. If this scenario prevails in the years to come, the 'deepening' of continental integration

will be dominated by a geopolitical imperative to which trans-boundary economic and social trends must be accommodated.

## Towards the emergence of a North American security regime: the US 'great idea' for inducing political cooperation from its NAFTA partners

The terrorist attacks of September 11, 2001 have already become a watershed in the 'new' world order that loomed after the end of the Cold War. Traditional conceptions of security are being challenged, political and economic alliances are being remade all around the world, and political and economic partners of the US are being obliged to react and adapt to the new security agenda drafted and implemented by Washington. Canada and Mexico were no exception to this.

The fact that the terrorists who attacked the Twin Towers in New York and the Pentagon premises entered legally to the US and overstayed their visas, made foreign visitors and visa holders a security concern. Immediately after the September attack, US borderlines, either through space or land, were closed. Since most of both Canada's and Mexico's trade to the US goes by truck, the shutting of borders disrupted the supply chain of their respective industries provoking serious economic costs. The post-NAFTA borderless continental economic space became the first casualty. This was particularly the case in highly integrated industries across the three countries, such as the automotive sector, relying heavily on the exchange of inputs and just in time operations.[1] Both countries realized at that time how vulnerable their trade flows were to border disruptions or shutdowns.

Canada was the first partner to react to the sudden changing situation, perhaps because intellectual and economic elites were celebrating at the time the 'vanishing' of borders between the two countries, and the north–south linkages already in place in key provinces above the 49th parallel.[2] Canadians suddenly feared a sort of 'mexicanization' of their border, so their government took the initiative to craft what was called a smart border strategy.

In December 2001 an action plan of 30 points resulted from bilateral talks between the then Prime Minister Chrétien and President George W. Bush. The plan became the touchstone of a 'great idea' for deepening the integration between the two countries. The smart borders initiative combined intergovernmental cooperation, even at the inter-operability level, with regulatory measures giving incentives to private firms to 'internalize' the costs for upgrading the safety of their trade volumes and

exchanges. As an example of the former mechanisms I should highlight, among other activities, the coordination of visa policies, the attempt to harmonize refugee/asylum processing and legislation, the efforts to build and share compatible immigration and customs databases, the moving of customs and immigration inspection activities away from the borderline (pre-clearance operations) in order to detect in advance any threat to security, and the common will to jointly enforce law and legislation concerning border issues (White House, 2002d).

An example of the second mechanism was the setting up of the so-called NEXUS and Free and Safe Trade (FAST) programs. The first of these is an alternative inspection program allowing pre-screened, 'low-risk' travelers to clear borders with no delay (normally on dedicated lanes), provided they exhibit an issued photo-identification and a proximity card. This program is geared towards so-called 'NAFTA travelers' whose business interests compel them to frequently make cross-border trips. Since NEXUS is a harmonized program, individuals eligible to apply are approved by both governments (White House, 2002b). The NEXUS program already covers 12 land crossing points, two Canadian international airports (NEXUS-AIR) and there are plans to expand it to the Windsor/Detroit marina area (NEXUS-Marine) (see Seghetti, 2004: 5).

The FAST program was built on a similar basis to NEXUS but targeted at trade flows. Expedited clearance processes are guaranteed to those carriers and importers who have pre-registered and been accepted as 'low risk, legitimate trade' (White House, 2002d). The ultimate goal of these two programs and other similar ones is to facilitate risk management. By discriminating 'high risk' from 'low risk' transit of people and goods, customs and migratory agents concentrate their efforts on detecting any threat conveyed by carriers or travelers crossing borders or check points.

Similarly to the way NAFTA was crafted, this 'great idea' shared by the US and Canada spilled over to the US southern border. In March 2002 a 'smart borders' plan was signed between the US and Mexican governments. Targeting the same goal as the NEXUS (the Mexican initiative was called the Secure Electronic Network for Travelers Rapid Inspection (SENTRI)) and FAST programs, the bilateral program for the southern neighbor excluded some 'sensitive' issues for Mexicans, such as the harmonization of refugee/asylum legislation and customs pre-clearance activities (White House, 2002c). The extension of the smart borders program to Mexico was done during the Monterrey Summit for Funding Development sponsored by the United Nations, that is, at the same time that Presidents Bush and Fox launched the bilateral PP I referred to in

the previous chapter, and which took the spotlight and diminished the profile of the border security deal.

Those three bilateral deals were eventually at the grounds of Security and Prosperity Partnership (SPP), launched in 2005. SPP became the backbone of an emerging and rapidly evolving security regime for North America, which in some aspects overlaps with the economic space articulated by NAFTA and its interconnection with DR-CAFTA. It has crafted the new geopolitics of the North American space, since the nature of the 'terrorist threat' and its agents (acting through global networks rather than depending solely on state sponsorship) have redefined US notions and strategies on security. In fact, one year after the terrorist attacks it became clear that the enlargement of the US security perimeter to its North American partners through the 'smart' policing of borders was part of a major security architecture aiming to reduce the risks of physical, bio-chemical, and even cybernetic attacks to US territory.

Washington's new security strategy targets two major fronts: abroad and at home. On the foreign front Washington has engaged in a long term 'war against terror', a major pillar of which is the use of force, either through preemptive action or 'preventive war'. Preemptive action is still grounded on a sovereignty-based concept of self-defense as understood by the United Nations Charter, although the US prompts other countries not to use it. It was under this principle that the US army invaded Afghanistan, in order to destroy Al-Qaeda forces that supposedly attacked the US and threatened to repeat their attacks. The notion of 'preventive war' has become, however, a major departure from sovereignty-based United Nations principles and calls for a military attack in case that a country threatens to become a major risk for 'democratic' countries, the US or US allies. This was the rationale under which Washington built a coalition for combating the 'axis of evil', epitomized in the first half of the present decade by Saddam Hussein in Iraq. Constructed as a 'rogue state' because of harboring terrorists and developing 'weapons of mass destruction' (WMD), which could eventually be used for terrorist purposes, Iraq became the first target of this so-called 'preventive war'. Its political regime and weapons build-up were destroyed in order to prevent Hussein's regime from becoming a risk in the so-called 'era of terror'. Regime change, preemptive attacks and preventive wars all became part of the same strategy, the goal of which is to destroy the new enemy, which could be scattered worldwide and at the same time concentrated on specific territories (Daalder and Steinberg, 2005; AI Symposium, 2005).

The 'war against terror' has also modified the notion of the enemy. Enemies currently may operate within state territories, through

cross-border networks, or through a composite of states and networks. 'Rogue' states are defined as those that harbor terrorists, such as Iraq – under Hussein – Iran, Syria or Libya; those that develop WMD, such as North Korea, Iran and Iraq; or just simply those tyrannical countries which combine 'brutality, poverty, instability, corruption, and suffering, forged under the rule of despots and despotic systems' (White House, 2006b: 3). Transnational terrorist networks are conceived, on the other hand, as exploiting the 'proud religion of Islam', calling for violence and murder as a means for establishing a 'totalitarian empire that denies all political and religious freedom' (White House, 2006b: 9). Thus, terrorists aim to destroy democratic institutions and any world order built by democracies. This justifies not only military preemption and prevention, but also 'regime change' in those 'despotic' countries which become a 'risk' for maintaining international peace.[3]

As for the domestic front, a national strategy to enhance 'homeland security' has been grounded in four pillars – intelligence and warning, security in borders and transport, domestic counter-terrorism, and infrastructure protection – all of them to be supervised and administered by the newly conceived Department of Homeland Security (DHS). Due to the subordination of border issues to this security architecture, the US Immigration and Naturalization Service (INS), and the Customs Service, among other agencies, became integrated to the newly conceived department (Bush, 2002a).

According to the new 'homeland security' scheme promoted by Washington, 'smart borders' and transport are intertwined, in the sense that every community in the US, be it small or large, is interconnected with a worldwide transport infrastructure. Harbors, railroads, airports, highways, energy grids, virtual networks, and any flow conveying people or commodities are currently considered to be part of that 'world-wide transport infrastructure'. Smart borders have thus the goal to promote, by using modern technology, the efficient and safe transit of people, goods and services across borders (White House, 2002a; Bush, 2002b). Framed in those terms, Canada and Mexico became a de facto extension of the US homeland, and were suddenly committed to cooperate with US authorities, even in their respective territories, for ensuring the security of the North American 'transport' and 'conveying belt' networks.

This became clear with the creation in October 2002 of the US Northern Command (USNORTHCOM), housed alongside an older defense institution, in Cheyenne Mountain, Colorado, the North American Aerospace Defense Command (NORAD). NORTHCOM is led

by a US Air Force four-star general who at the same time commands NORAD. The latter is a Canada–US command established during the Cold War, in 1957, the aim of which was to keep aerospace warning and control of what was then understood as North America (Canada and the US). Renewable each five years, NORAD has traditionally had preventive functions, aimed at warning and detecting in advance any attack against the two countries whether by aircraft, missiles, or space vehicles. NORAD was activated during the September 11 attacks. The commander is appointed by, and responsible to, both the US President and the Prime Minister of Canada (see Granatstein, 2002: 10 and NORAD's home page: http://www.norad.mil/).

USNORTHCOM is by contrast a byproduct of the terrorist attacks of 2001 and its mission is to deter, prevent, and defeat aggressions targeting the US homeland, as well as to provide defense support to civil authorities. However, USNORTHCOM's fields of responsibility include air, land and sea operations in an area embracing the continental US, Alaska, Canada, Mexico, and the surrounding water out circa 500 nautical miles[4] (see USNORTHCOM's web page: http://www.northcom.mil/). In other words, this command has extended the 'security perimeter' of the US homeland to the overall North American space. The fact that the commander of NORAD has been integrated to that of USNORTHCOM witnesses the degree of involvement of Canadian defense forces in the protection of the enlarged US security perimeter. This 'upgraded' involvement has unleashed a debate among Canadian elites about the best way to balance their interests to maintain a strong North American space with the need to protect their sovereignty in military matters. This issue shall be analyzed in the last section of this chapter.

The very notion of 'smart borders' shifted the focus from solely 'barricading' territorial borders (e.g. the Mexico–US front line) to a whole rebordering of North America under a new geopolitical perspective through the deployment of moving checkpoints. Smart borders are in fact intelligent checkpoints – assisted by sophisticated surveillance mechanisms and complex inter-agency and interoperability bureaucratic operations – the goal of which is to detect in advance would-be enemies and visualize threat assessment. In contrast with the territorial borders defined across national narratives and identities, 'smart borders' are constantly moving and changing; they could be an embassy or consular house; they could be at customs clearance or pre-clearance; they could be activated when a cargo in a container is being registered in advance; they are in airports and aircrafts, in shipping routes and pipelines. These

moving checkpoints do not aim to restrain people or goods from trespassing specific territorial borders; they rather aim at detecting and constructing the 'spaces of threat and vulnerability' of the enlarged homeland.

This notion of 'threat assessment' to protect the 'continental territory' from within and from without has become a major goal of SPP. It is geared to tackle this on three fronts: to secure North America from external threats, to secure the region from threats coming from within the region, and to secure the movement of 'low risk' traffic across shared borders (White House, 2005). In this three-tier security regime cooperation is grounded in both government inter-agency and interoperability, and in incentive mechanisms in order to spur the involvement of private 'stakeholders'. So far, different issue areas have been crafted and drafted between the three countries, although some of them have remained in operation on a bilateral basis with the US. A major characteristic of this emerging security regime is that the leaders of the three countries have scheduled several tasks and goals to be achieved in specific spans of time. The implementation and monitoring of these activities, and the new ones that will be added, have remained in the hands of ad hoc inter-agency working groups. The major issue areas conforming this regime are as follows:[5]

*1. Security measures and preparedness against external threats*

Although SPP is not a military alliance, it envisages policy cooperation for the protection of North America as a common territorial unit. So far, the bulk of initiatives and scheduled targets aim at preempting the entrance (legal or illegal) of presumed terrorists to the overall region. A major task that is being undertaken among the government agencies of the three countries is the development and implementation of equivalent biometric standards and systems to enhance security for passports, visas, residence cards, transportation credentials and other similar documents for travelers coming from outside the region. The North American countries are also considering the creation of a real-time information sharing mechanism in order to detect high-risk individuals and cargo before they arrive at any port of entry in the region. This initiative encompasses the negotiation of terrorist screening information agreements between the three countries.

More recently (as of April 2007), working groups and agencies involved in this security regime are developing and implementing compatible screening methods for goods and cargo prior to departure from a foreign port and at the first point of entry to North America. In

other words, SPP is continentalizing the FAST program already operating at the 'domestic' borders of the region. Groups are also discussing different strategies for controlling trade on nuclear and radioactive materials, as well as the diversion of 'sensitive' goods or technologies from any of the three countries to 'mutually agreed upon' prohibited countries or end-users.

*2. Security measures against threats coming from within the region*

Since for strategic reasons the North American space is to be considered an extension of the US homeland, security measures for protecting the continental territory are currently targeting three major areas: the development and implementation of strategies for securing aviation and maritime transportation; preparedness to confront cross-border public health emergencies (avian flue, bioterrorism) or any other type of emergency (e.g. preparedness in advance of the 2010 Winter Olympics in Vancouver); law enforcement cooperation to combat transnational threats to the three countries; protection of cross-border and interconnections of 'critical infrastructure' (electricity generation and distribution, oil and gas pipelines, dams, telecommunications, transportation, defense industrial bases, cyber-systems, etc.); and the enhancement of cross-border intelligence gathering and cooperation in order to share terrorist watch-list data and the establishment of appropriate linkages between the three countries.

Since the primacy of security has dominated the post-NAFTA agenda in North America after the terrorist attacks of 2001, the panoply of measures and strategies to be undertaken and the issue areas to be covered for securing the continental territory will probably deepen in the years to come. So far, some of the common strategies already scheduled to be accomplished include, among many others, the formalization of the role of the North American Aviation Trilateral (NAAT) in achieving common security goals; the development of compatible strategies for achieving the security of ports and vessels according to international standards; cooperation at the bilateral and trilateral level in order to improve and enforce information sharing, deportation agreements, prosecution of cyber-attackers, and other related measures; the development of a coordinated strategy to identify and manage threats to food supply and agricultural sectors; and the common identification of critical infrastructure assets requiring vulnerability assessments.

*3. Securing the movement of 'low risk' traffic across shared borders*

Last but not least, the third pillar of SPP is to deepen and enforce what was built by the US on a bilateral basis under the 'smart borders'

agreements of 2001 and 2002. Though the approach still operates according to the characteristics and sensibilities of the two US neighbors (i.e. Mexico has not yet accepted pre-clearance processes in its own territory), the whole idea is a convergence towards a common strategy. So far, as of April 2007, the SENTRI and FAST programs have been expanded to new ports of entry at the US–Mexican border; the NEXUS-AIR pilot program is being expanded to Vancouver and possibilities are being explored for starting to implement it in Mexico; transit times are being reduced at the Windsor–Detroit gateway and will probably be also reduced in some checkpoints at the Mexican border. Finally, the three countries have begun to cooperate in the development and deployment of new technologies to promote the legitimate flow of people and goods in the 'domestic' borders of the continental area. The whole idea is to clearly detect the identification of travelers to the US (through biometric verification) from their very entrance until their departure.

Although this emerging security regime heavily overlaps with NAFTA's trade and investment regime, the scope, goals and mechanics of the former are quite different from the latter. While in the first two chapters of this book I attempted to demonstrate how the NAFTA regime aims to internalize in the region a legal disciplinary governance of state policies vis-à-vis firms and markets (i.e. a so-called retreat of the state from the economy), the security regime rather aims at a growing control and regularization of human and trade flows according to the strategic thought and priorities defined by Washington in its war against terror.

While the disciplinary governance of states and markets are staked on the crafting of a new legal and regulatory body for empowering markets and corporate rights against 'unreasonable', distorting or abusive state policies, the panoply of bilateral and trilateral policies encompassed by SPP aims at establishing a permanent cross-border surveillance mechanism, the goal of which is the constant classification and reclassification of individuals and populations, in order to detect their level of risk. While NAFTA's disciplinary governance embodied principles, rules and judicial mechanisms that aim to contain, even restrain, state involvement in cross-border economic exchanges and corporate rights, policies nested on SPP aim at monitoring, surveying and controlling the mobility – of people and goods – across continental and domestic borders in the region as a security tool for crafting preemptive action and nourishing a 'state of war'. While the NAFTA regime is targeting state behavior in order to make markets work, the SPP regime is targeting individuals and specific populations in order to keep them predictable as a means to keep out of risk the US territory, its interconnections and population.

SPP-based policies convey in fact a sort of regional governance of security policies in North America (i.e. bilateral or trilateral cooperation between government agencies according to a moving agenda, cross-border inter-agency and interoperability operations, 'incentives' for gaining the involvement and support of private firms, and various types of civil organizations, etc), although it is not yet clear how Mexico and Canada will accommodate their own interests. Mexico in recent years perceived cross-border human flows as a byproduct of informal job markets operating between the US and Mexico; the US, by contrast, traditionally perceived them as a breach to their nationality and migratory legislation. After September 11, Washington started to conceive these illegal flows as an additional threat to the homeland, so smart borders were created to detect in advance their level of hazard. As for Canadians, they have feared a potential 'mexicanization' of their border, since Americans have realized after the terrorist attacks how porous and defenseless their northern border was.[6] Conscious of their trade dependence on the US, Canadians have ever since made the best of efforts, either bilaterally or under SPP, to avoid the emergence of a barricaded border in their front line.

## Securing the Mexican borderline: from deterrence to prevention

After September 11, the US politics of borders seemed to shift from the sovereignty-centered discourse of protecting and exercising the monopoly of the state to decide the transit of 'aliens' to its territory, to a rather war-centered paradigm in which the protection of the homeland, not only its territory, but also its population, resources and all their interconnections with the 'outside world' is at stake. The war-centered paradigm does not substitute the 'sovereignty-based' one; they rather overlap and reinforce each other. The historically embedded territorial border is still to be protected against 'illegal aliens', but the focus is being shifted against those illegal aliens potentially linked to or exploited by terrorist purposes. In this sense, the latter is rather anchored in a generalized 'politics of fear' re-launched by the US government after the terrorist attacks.[7] In parallel, 'smart borders', conceived as moving technology-and-knowledge-intensive checkpoints, are there to set the divide between risky and non-risky people, to screen the vulnerabilities of specific spaces, and to reinforce the barricades in the territorial front lines.

Once the 'war against terror' was launched by the US on the 'global' front, barricaded and smart borders became tools of the domestic front of the war. They either deter 'aliens' from trespassing illegally on the US

homeland (with all the flaws already indicated), or allow US agencies and counterterrorism offices to prevent ongoing threats and vulnerabilities in the US homeland and its conveying territories. While on the global front the war against terror is targeting rogue populations and territories, on the domestic front barricaded and smart borders attempt to detect and target risky people and devise 'inner' spaces of vulnerability. In other words, the new politics of borders has become another means of conducting the 'war against terror' at home.[8] However, and in contrast with the deterrence approach followed during the previous years, which highlighted the legal and sovereign dimension of the territorial border, the smart borders approach is instead heavily grounded in a governmentalization of human flows.[9]

As I explained in the first chapter of this book, a growing number of principled governance regimes are becoming more and more invested by knowledge- and science-based technologies measuring and calculating specific behaviors of individuals and social groups. Their goal is to modify human behavior or to correct deviations (income gaps, social gaps, etc.) according to established standards, norms or desired outcomes. By so doing, the activity of individuals and/or specific populations is increasingly governmentalized by a savvy technology of measurement and observation in order to devise a strategy of tactical intervention. In this sense, new organizational strategies of governance (i.e. post-sovereign or networked ones) are also becoming invested by a growing governmentalization of their strategies and goals (see Chapter 1). This is exactly what is at stake in the smart borders approach in North America. The overall technological and knowledge investment deployed by this new organizational approach aims at discriminating risky or 'rogue' populations and commodity flows, from safe or 'NAFTA' flows, in order to make cross-border mobility in North America measurable, predictable and submitted to a space of desirable outcomes.

Within this complex and overlapping space, in which security and trade regimes encounter each other, the trade disciplinary regime targets states' policy outcomes while the security machinery targets individual and social outcomes. In this sense, while state policies have become the focus of disciplinary control at the macro level, the 'illegal alien' has become the target of the most intensive and contradictory observations, scrutiny, and social constructions at the individual level in a post-NAFTA North America. The illegal alien has become construed either as the symbol of the entrepreneurial *homo economicus*, or as the criminal suspect potentially conveying a terrorist threat. The non-authorized worker has become, on one hand, the proof that in post-NAFTA North America the Mexican space remains a major reservoir of cheap labor

through which Americans get a subsidy from Mexicans, and Mexicans anticipate complementary income through remittances for stabilizing income shortages at home. This is how trans-boundary informal labor markets normally stabilize in the region. By keeping these markets illegal, although tolerated by American authorities and patronized by specific industries, non-authorized labor remains cheap and available. This is perhaps why former President Fox called Mexican migrants 'heroes'. These heroes contribute to boosting the productivity of the American economy in some specific areas and to stabilizing (an enlarged) family income in their place of origin.

On the other hand, non-authorized workers remain the figure of the criminal whose level of threat varies according to a new hierarchy of risk and vulnerability redefined according to the new politics of fear prevailing in the US. They have become at the interface of various illegal markets, ranging from the more predictable – labor – to the most uncertain – drug and human smuggling, terrorist trafficking. The growing governmentalization of those markets will definitely have an impact on cross-border labor networks and on the way Americans and Washington perceive their 'southern connection'. It seems that after September 11, Americans still perceive Mexico as a functional economic space, but also as a fragmented one in which new zones of risks and challenges to overall North American security must be tackled at the cross-border level, regardless of the degree of support or preparedness of Mexican authorities. The growing criminalization of informal labor markets is being thus reinforced by the growing fragmentation of the Mexican territory in spaces of 'failed authority'. This double trend has caused the governance of borders in the region to evolve in two directions: while US–Canada security policies seem to converge at least in the core issues of the American agenda, US–Mexico security relations seem to become more asymmetrical, contentious and difficult to handle. In the remaining part of this section I shall summarize how the growing governmentalization of cross-border flows is at the grounds of major changes in how American authorities organize 'borders security' and the governance of Mexico's 'risky spaces'. In the last section of this chapter I shall review how, by contrast, US–Canada security policies seem to converge.

## Screening and targeting risky people and flows in North America

As a representative of 10,000 front-line USBP employees stated it, the high visibility of border patrolling within a few meters of the Mexico–US border compelled by the strategy of deterrence, has made agents more

vulnerable to all sorts of attacks, going from thrown rocks to bullets (Committee on the Judiciary, 2006: 25). This vulnerability embedded in the visibility of control is precisely what the smart borders approach attempts to avert. By using rather disciplinary and knowledge-intensive technologies, the new border approach shifted the focus from deterrence to detection and prevention. Through constantly monitoring, measuring (by using biometrics or other devices) and identifying moving people and flows, across a myriad of checkpoints and intelligence sharing operations, risk assessment and vulnerabilities are addressed under new hierarchies.

While the barricaded border is targeting the 'illegal alien' or the illegal commodity (narcotics), the smart border aims at targeting, in priority, the terrorists, the would-be terrorists, and their weapons – whether WMD or not – that they eventually may convey. Within this new hierarchy of risk, the unauthorized migrant is still a risk, but not a priority target. Illegal flows – either human or commodities – are still a risk since they need an interface to enter the 'wider' (North America) or the 'core' (the US) homeland: the smuggler. Smuggling has become a high risk activity since terrorists may use them as conveying belts for penetrating the homeland. As a patrol agent warned, the new concern is that '... terrorists and violent criminals may exploit smuggling routes to illegally enter the United States' (Committee on the Judiciary, 2006: 21). This is why the new approach is not only targeting risky people or flows before they enter the homeland, but also once they are at home. The DHS has conferred the first task to the Customs and Border Protection (CBP) agency, and the second to Immigration and Customs Enforcement (ICE). They both coordinate with each other in order to detect a risk before it enters the homeland or once it develops at home (see Siskin, 2006: 24–30).

These new agencies in coordination with local and federal authorities and intelligence services attempt to define, classify and modify according to the circumstances, the new priorities for targeting and detaining people under suspicion. According to a recent memorandum sent by the Under Secretary for Border and Transportation Security to both CBP and ICE, the rationale is as follows: apart from those cases requiring mandatory detention for breaching the Immigration and Naturalization Act (INA),[10] '[a]liens who exhibit specific, articuable intelligence-based risk factors for terrorism or national security concern not solely based on the alien's race, ethnicity, nationality or religion' are among those who must be detained on a 'high priority' basis. 'Suspected alien and narcotics smugglers' are classified (so far) on the 'medium priority' list, while in

the 'lower priority' category were put those arrested in a worksite enforcement or other aliens not subject to required detention (Department of Homeland Security, 2006: Appendix D).

This new hierarchy of risk clearly differentiates criminal and terrorist-related populations from unauthorized labor populations, since illegal aliens are not required by current federal legislation to be under detention. However, this list clearly establishes the link between the illegal (the unauthorized workers) the criminal (the smugglers) and the priority target (the terrorists). Smugglers are the interface between illegal and all kinds of criminal populations. Consequently, by differentiating populations according to their level of risk and the way they relate with other types of populations, the new strategy devises security policies which attempt to become more efficient in their outcomes. Accordingly, agents and agencies linked to the DHS are demanding more staff and space to increase the number of detainees, according to the changing priorities crafted by the security of the homeland (see Department of Homeland Security, 2006). Priorities are being framed according to what those agencies understand by 'intelligence-based' or 'terrorist-based' risk. New risky populations are being defined by a combination of ethnicity, nationality, religion and other cultural factors stigmatized by the evolving 'war on terror'. New typologies are constantly emerging for being part of the mandatory or 'high priority' list. Agencies are, for instance, currently giving more importance to the movement pattern of the 'Other than Mexican' (OTM) illegal migrant population. These OTM migrants have increased in recent years and have become the target of observation and policy intervention, mainly the subpopulation whose origin are from 'State Sponsors of Terrorism' (SST), or from a list of 35 countries to be considered of 'Special Interest' (SIC). DHS agents are pushing for including this subpopulation in the 'high-priority' detention list.

The targeting and screening of 'suspicious' and risky populations becomes powerful and effective when it is embodied in inter-agency and interoperability policies taking place in calculated spaces. This is the case, for instance, of 'Operation Black Jack', put in place in 2005, at the twin cities of Laredo-Nuevo Laredo, in the Texas-Tamaulipas border. This task force operation aims at building a multi-agency agreed-upon threat assessment identifying 'the most violent and prolific human and drug-smuggling organizations and cells', from which a priority list for dismantling them is drawn (Committee on the Judiciary, 2005: 12). This multi-agency task force involves DHS agencies (both ICE and CBP), the Laredo Intelligence Center, the Drug Enforcement Administration

(DEA), the Texas National Guard, the Union Pacific Railroad Police, and the Laredo Police Department. The unit works in coordination with the Federal Bureau of Investigation (FBI), the McAllen Intelligence Center, the El Paso Intelligence Center, and the US Border Patrol intelligence unit in Laredo. At the same time, this task force shares data and intelligence activities with Mexican agencies, conforming units such as the Binational Alien Protection Unit (BAPU) (targeting human smuggling operations at the San Antonio area) or the Operation Against Smugglers Initiative on Safety and Security (OASISS).

Operation Black Jack accomplishes its activities through two major channels: it gathers and disseminates information between federal agencies that are responsible for border security and state and local law enforcement agencies in order to trace the violence linked to drug cartels; and it devises strategies for attacking human and smuggling organizations that contribute or are linked to that violence. Thus their goal is to build up 'calculated spaces' of risk, by tracing and monitoring criminal and/or illegal behavior, their connection with illicit flows – either human or material – and their eventual link with 'homeland security' concerns.

Though still a relatively young task force, Operation Black Jack has already detected the furious rivalry between two cartels (the 'Gulf' and the 'Federation') for gaining control of a 'Plaza'. In the mafia language a 'Plaza' is understood as a controlled space, out of which a sort of 'tax' is being levied from all smugglers or criminal groups that want to develop any kind of operation. In the case of the Gulf Cartel, this 'Plaza' encompasses the corridor going from southern Mexico to the Nuevo Laredo area. Control of this corridor means control of all smuggling, both of humans and drugs. Task forces like Operation Black Jack have the goal to make transparent these criminal-run spaces, whose control is under dispute or mafia-based. From this, all illicit connections and interfaces with non-drug illegal flows are established. Through these multi-task operations, for instance, the eventual connection of youth gangs, such as *Mara Salvatrucha* or MS-13, or of paramilitary groups, such as *Los Zetas*, *Los Negros* or *La Hermandad de Pistoleros Latinos*, with drug or arms traffickers is established, and 'safe houses' where smugglers keep smuggled people, arms or drugs are being detected. The ultimate goal of this type of intelligence and law enforcement operation is to dismantle networks, confiscate arms, drugs or any other 'risky' commodities, and as an agent of ICE put it, '... to prevent acts of terrorism by targeting the people, money, and materials that support terrorist and criminal activity' (Committee on the Judiciary, 2005: 11).

## Crafting a new cartography of risk

The politics of fear and the enforcement of law, either at the borderlands or the homeland, have become part of the same strategy of the 'war against terror' pursued by the US on the domestic front. This politics of fear and law enforcement is at the grounds of the checkpoint approach of smart borders. They provide for a permanent surveillance of human and material flows heading to the homeland or already moving within it. Their goal is to detect, in advance, the actual or potential level of risk of these human and material flows to which the US economy and society is connected. Detection, diagnosis and prevention are essential components of this growing governmentalization of 'moving borders'. They involve a new governance on security issues, as witnessed by specific inter-agency and interoperability operations as previously mentioned (e.g. Operation Black Jack, also involving Mexican agencies), or 'great' policy environment designs such as SPP in itself. The building up of new hierarchies and reclassifications of moving populations and commodities is a major by-product of this governmentalization process of fear and law enforcement. The redrafting of 'spaces of risk', whether territorial or not (e.g. cyberterrorism, nuclear terrorism, etc), is in fact another major consequence of all this.

Spaces of risk were calculated and constructed during the Cold War years in the US. They were embodied, for example, in the security concerns about the depletion of natural resources, i.e. oil and hydrocarbon resources. The vulnerability of the US economy was assessed (in terms of the recoverable stock of its traditional energy reservoirs, trends in energy consumption and imports, etc.) in relation to its dependence on oil (and gas) imports coming from the largest reservoir in the world, the Middle East. A geopolitical cartography was thus derived from this asymmetric distribution of oil wealth in order to detect the 'secured' or 'out of risk' energy basins in the world. A cartography of risk was also at the basis for the construction of a 'nuclear umbrella' to protect Western Europe and the North Atlantic space and territory from a nuclear attack coming from the former Soviet Union.

The new politics of fear, premising that terrorism has become the post-Cold War major enemy, is radically transforming this cartography of risk. Rogue states (hosting terrorists or WMD, or both), failed states, and global terrorist networks have become the grounds for drafting a new spatial location of threat. The notion of critical infrastructure protection is being redrafted in order to include any terrorist attack to strategic connections to the US homeland or to the wider North American space.[11]

Within this changing context, Mexamerica (that is, the cross-border region along the US–Mexico border), is being perceived as more risky according to the new security grid. From being the encounter of the North–South divide, the southwest border and its entrenched social space have suddenly been perceived, by US politicians, officials and agencies, as a conflictive territoriality fragmented by 'lawlessness spaces', that is, areas where Mexican authorities have failed to enforce the rule of law. These areas where Mexican authorities – either local or federal – failed to enforce their authority are either controlled by drug barons or under dispute of 'informal forces'. Corruption, crime, violence and all sorts of unlawful activities are the major characteristics of these lawlessness spaces, able to be exploited by terrorist networks in order to attack the US homeland. It is in this sense that areas where legal authority fails to enforce its faculties are becoming more and more considered as new 'spaces of risk' according to the new mantra of the security discourse circulating in the US.

During the summer and fall of 2005, the governors of three American states bordering with Mexico – New Mexico, Arizona and Texas – declared a 'State of Emergency' along their respective borderlines. The reasons were manifold: kidnappings of US citizens, violence triggered by drug barons and their paramilitary groups, illegal incursions to the US territory of all kinds,[12] and in general terms the erosion of the social and political climate along some points of the borderline (Committee on the Judiciary, 2005: 32, 2006: 2). The mushrooming of 'spaces of risk' along the US–Mexico front line became echoed by the US Ambassador in Mexico, Tony Garza, who has constantly warned against the insecurity prevailing in the southwest border. During the summer of 2005, Tony Garza closed the US consulate in Nuevo Laredo for some days, seeking to put pressure on the Mexican government in order to stop the violence triggered by the drug cartel wars.

It was in this context that one year later, in August 2006, an official encounter took place between the four US governors sharing a common borderline with Mexico (California, Arizona, New Mexico and Texas) and the six Mexican counterparts from the other side (Baja California, Sonora, Chihuahua, Coahuila, Nuevo León, and Tamaulipas). A bilateral task force was created with the purpose of combating drug and human smuggling, in an effort to reduce the potentiality of risk along the US–Mexico front line (*El Universal*, 2006a, 2006b). The participation of the DHS in this renewed effort for reinforcing security in the region made clear that the new imperatives of security prevailing in the US have prompted the political and intelligence collaboration of Mexican

authorities at the federal, state and local level. This pattern of collaboration will probably continue and become more solid during the Calderón administration, since his early days in power featured a major prosecution, incarceration and extradition (to the US) of key drug barons operating in central and northern Mexico.

## Protection without protectionism: Canada's approach for securing its borderline

The Canadian debate on how to reinforce the security of the territory and the security of its southern neighbor has become heated since the breakthrough of the terrorist attack in the US homeland. As Canadian former Secretary of Foreign Affairs, Lloyd Axworthy, clearly stated it, 'security will be the watchword for defining [Canada's] relationship with the United States' in the years to come (Axworthy, 2003: 106). He warned his fellow citizens, however, that Canadians must be prepared to avoid the US being the only author of the definition of security. This is in fact what is at stake for Canadians, after more than 15 years of formal integration with the US and after suddenly becoming part of the US continental 'security perimeter' when NORAD became integrated with the USNORTHCOM.

Though the response of the government of Canada to the security concerns of the US has been construed with caution, following in some way Lloyd Axworthy's advice, influential think tanks, representing mainly corporate and market interests in Canadian society, have promoted a 'new paradigm' for deepening cooperation with the US. The Canadian Council of Chief Executives (CCCE), representing 150 leading powerful Canadian enterprises, launched and proposed after one year of debates and consultation, the most articulated and ambitious strategy for linking Canadian economic interests in the US with US defense interests involving Canada. Premising that Canada is both a trade-dependent economy and an immigrant-based society, the goal of the CCCE's strategy is to enhance economic security and physical security for Canadians, by devising a comprehensive policy of integration and cooperation with the US. As opposed to a piecemeal approach, a 'big idea' or 'strategic bargain' was needed, according to the supporters of this proposal,[13] in order to capture the interest and mobilize the leadership of the US.

It was in fact the CCCE that first proposed the building of SPP between the US and Canada, which could eventually involve Mexico, a year before the US formalized the new security and prosperity regime

with its two neighbors. Corporate Canada was right in the sense that a 'big idea' was necessary in order to mobilize and capture the interest for North American affairs in Washington, and in many ways its proposal became the blueprint of the emerging post-NAFTA security and economic regime emerging in the region from 2005. Corporate Canada's proposal was grounded in five pillars:

*1. The rebordering of North America*

Though the ideal for Canadian firms and businesses is to consolidate a borderless economy, with a front line operating in a similar way to the Schengen space in the EU, Corporate Canada is aware that this is not yet possible in a time where the US is being threatened by rogue states and suspicious populations. Thus, the smart borders strategy must be consolidated and release unnecessary inspection of those flows (human or material) previously screened or certified. As the proposal states: 'a smarter border is one that eliminates unnecessary work and shifts other activities away from the border' (Canadian Council of Chief Executives, 2004: 6). Apart from enhancing the technology for screening and recognizing populations and commodities (such as the creation of a single biometric identificaion card, or a NAFTA retirement visa for easing mobility), the envisioning of a common external tariff, at least between the US and Canada, could be part of this rebordering of the continental space.

*2. Regulatory convergence*

Since Canadian industries are heavily integrated with American businesses, a myriad of rules and regulations enforced at the border have become costly and unnecessary. The two countries should move to outright harmonization, mutual recognition, acceptance of the 'tested once' principle and cooperative enforcement.

*3. Security of access and of supply for the resource sector*

As Canada was a resource economy with pending non-tariff barriers in the US for its agricultural and forest products (see Chapter 2 of this book), Corporate Canada introduced the concept of 'economic security' for capturing both Canadian and US interests. Since the crafting of CUSFTA, Canadians have pursued the 'security of access' to the American market, mainly by abating protectionist measures against its resource-based products.

As I reviewed in the second chapter of this book, neither CUSFTA nor NAFTA could eliminate the imposition of trade remedies in the

region; the two harmonized the notion of neither subsidy nor dumping. This explains the pending barriers still existing in the region. Since the US has become at the turn of the century, and certainly after the invasion of Iraq, concerned once again with securing the supply of oil and gas from its two neighbors, Corporate Canada suggested linking the enhancement of energy security at the continental level (where Canada is anticipated to play a major role, as will be discussed in the following chapter) with a long-term solution of key trade disputes in the resource sector (softwood lumber, wheat, etc). Security of access and security of supply (mainly of energy resources) should become, according to this vision, part of the same strategy.

*4. Reinvigorating the security perimeter at the continental level*

On the premise that Canada must remain a safe country for the US if it is to remain attractive to foreign businesses and investments, Canadian defense and military capabilities should be reinvigorated in order to remain credible for the protection of its own territory and its neighbor's. The best way to accomplish this, according to this proposal, is by formalizing Canadian collaboration in the protection of the continental perimeter. Canadian commitments under NORAD should consequently be enlarged in order to cover ballistic, land and maritime defense.

*5. Institution building to manage better the deepening of continental integration*

Once the trade and investment effects associated with both CUSFTA and NAFTA are waning (see Chapter 3), the need for building new institutions to give momentum to the economic and political space already emerging in North America has become part of this 'great idea'. Though market actors and academics are conscious that North American integration is following a different pattern to that followed by Europeans, the consolidation of new institutions, such as an independent NAFTA Secretariat, a Trade and Investment Court, or sectoral commissions to deal with key issue areas, has become necessary in order to shape the future of North American integration (see Chapter 2). The new security regime constructed around SPP in March 2005 incorporated well the first three pillars of the original CCCE proposal.[14] It has been, however, cautious in the last two ones. The consolidation of a continental security perimeter has become the most controversial point in the future of US–Canada integration. Critics to the comprehensive strategy linking the extension of Canadian defense commitments within NORAD with the consolidation of a borderless economy between Canada and the US

have highlighted the threat of compromising political sovereignty. They warn that Canada and Canadians must maintain their differences with the US regarding their social (mainly the welfare system) and political organization.[15]

In parallel to the rich debate entangled by think tanks and different civil society groups around the eventual commitments of Canadians to the emerging security regime looming in the region, the government of Canada has progressively crafted a made-in-Canada comprehensive strategy for dealing with security threats coming from within and from without. In 2003, the government created a new department, Public Safety and Emergency Preparedness Canada (PSEPC), encompassing five major agencies dealing with security and protection at different levels.[16] This department has become in fact the homolog of the American DHS, and deals on an interrelated basis with issues of intelligence collection capacity, emergency planning and management, threats to public health, transport and border security, and accomplishment of security measures abroad.

The normative goal of the Canadian security strategy is not grounded on a politics of fear, as that prevailing in the US, but in the imperative of assuring an open society nourished by values of liberty, the right to life, and tolerance. As the National Security Strategy spelled out, 'the new and more complex security environment requires Canada to deal frankly with the reality that in an open society, tensions can develop among communities ... [Consequently], Canadians stand together in reaffirming that the use of violence to pursue political, religious or ideological goals is an affront to our values and must be met with a determined response by Canadians and by their governments' (Privy Council Office, 2004: 2). By condemning violence, Canadians condemn as well terrorist networks, acts of terrorism and states sponsoring terrorism. However, the Canadian government has equally acknowledged that religious extremism, violent secessionist movements, domestic extremism, proliferation of WMD, failed and failing states, organized crime, natural disasters, pandemics, and the vulnerability of critical infrastructure, among other risks, are part of the new security threats facing the country.

In order to pursue its tasks, PSEPC has sponsored the creation of a Cross-Cultural Roundtable on Security in order to engage Canadians and the government in a long-term debate about how national security issues impact a diverse and pluralistic society. At the same time, the government has set up the building of an integrated security system, the goal of which is to establish a multi-agency threat assessment for

envisioning policy implications. At the end of 2004, a new Integrated Threat Assessment Center (ITAC) began operations in conjunction with the National Security Advisor to the Prime Minister. ITAC's threat assessments are to be distributed within the intelligence community, to policy makers and to relevant first line responders, and it has become the liaison with the National Counterterrorism Center in the US. Needless to say, PSEPC's activities and duties encompass all interoperability operations linked to transport security, cross-border trade and infrastructure involved in the 30-point action plan between Canada and the US (Privy Council Office, 2004, 2005).

As for space, land and maritime defense, the government of Canada has also moved to an interoperability approach with the US. The Canadian government has been conscious that Canadian territory and space must remain safe in order to assure both its own security and its neighbor's. Failing to do this will prompt the US to take charge of the security of the Canadian territory with all the political and legal consequences of this. This is the reason why Canada became a military allied with the US since the Second World War, and reinforced this alliance by becoming a member of the North Atlantic Treaty Organization (NATO) during the Cold War. NORAD was nested in this context but has remained restrained to warning measures against a threat to the sovereignty of the two allies' space. After September 11 the Canadian government has had to cope with pressures for enlarging the scope of this spatial alliance, by incorporating within NORAD antiballistic,[17] maritime and land defense. Since Canadians remain 'deputy-commanders' under NORAD, such an extension has been perceived by Canadians as a surrender of their military sovereignty (Fergusson, 2005: 12). The Canadian government has rather made a compromise by agreeing with the US to establish an interoperability command, the Binational Planning Group (BPG), under which continental land and sea protection is ensured. The commander of the BPG is a Canadian (who at the same time is the deputy-commander of NORAD) and the headquarters is also located in Colorado, near NORAD and the USNORTHCOM (Mason, 2005; Fergusson, 2005).

# 6

# Post-NAFTA Deepening and Widening Trends: Towards the Continentalization of Energy Markets and the Enlargement of the Southern Periphery

## Introduction

For years, Europeans have debated about the virtues of strengthening communitarian institutions and inter-state political cooperation for ensuring the consolidation of a single economic and social space. The 'deepening' of integration has generally been translated into a further pooling of states' sovereignty to communitarian institutions, such as the European Commission, the European Court or the Parliament. The debate has split opinions about the virtues of deepening commitments with only a few members – say, the original six founding members – or enlarging the *'acquis communautaire'* to new ones, but without extending the commitments agreed by an 'inner circle'. Europeans have in fact shown that they can do both without putting too much pressure on the communitarian architecture.

Alhough North American elites have subsequently stated that integrative trends in the region follow a different path than Europe's, the deepening and/or widening debate has already been unleashed within political and academic circles. Though SPP should not be considered as a political spin-off of 14 years of commercial integration, the linkage between border security and 'economic security' – as Canadians prefer to say – have spurred the possibilities of a further deepening commercial integration in the region. This is especially the case with energy markets.

The post-September 11 most recent trends in this growing continentalized market will be discussed in the first section of this final chapter. Similar to the European experience, the 'deepening' process has been activated at different speeds in North America; the Ottawa–Washington axis featuring the driving force.

The second part of this chapter will review how a NAFTA-like architecture has been expanded to other countries, mainly to those contiguous to Mexico: i.e. five Central American (CA) countries and the Dominican Republic (DR) that signed the DR-CAFTA with the US, in August 2005. I argue in this part that DR-CAFTA should be considered a de facto expansion of the North American economic space to the CA and Caribbean frontier. This expansion has been performed through the unilateral moves of the three original NAFTA members, a major trait of the North American integration that highly contrasts with the European one, where most of the 'deepening' or 'widening' decisions are being taken by the consensus of all members. The enlargement of the North American space has become a by-product of Mexico's decision to strike bilateral FTAs with its CA neighbors. Canada is following suit and DR-CAFTA signaled a strategic move done by the US, where some specific sectors, such as that of apparel and textiles, is to be considered as a single market including Mexico and Canada. Since the CA and Caribbean region features similar traits and tendencies to those prevailing in the Mexican south, and DR-CAFTA does not convey any development strategy for a region full of imbalances and social contrasts, I also argue in this final chapter that the extension of NAFTA-like treatment is consolidating an enlarged southern periphery in North America.

## Towards a continental energy partnership: a two-speed 'deepening' for the region?

While the focus in the security aspect of SPP is on rebordering the limits and front lines of North America, according to the imperative goal of reducing the risk of a terrorist attack, the rationale of the 'prosperity' side of this trilateral alliance has been put on improving the overall competitiveness of the region. That is, in contrast to the bilateral partnership between Mexico and the US, which put the emphasis on reducing income gaps between the two countries and within Mexico, the trilateral deal, being sponsored by major business interests in the three countries,[1] shifted the point of cooperation towards the general goal of boosting productivity. Since the evolution of the bilateral partnership is

uncertain, most probably the interests of big businesses in the region will prevail in the evolution of the prosperity agenda.

So far, different working groups have been created focusing on issues for improving market access while enhancing the 'quality of life'. Ad hoc groups have been created dealing with e-commerce, a field not covered by NAFTA but by second generation agreements, such as DR-CAFTA. Groups dealing with food and agriculture, transportation and health issues have also been created in order to overcome the loopholes featured by the NAFTA regime (see Chapter 2). However, the field where cooperation and further integration is most anticipated is energy. Though energy markets in the three countries have become continentalized since the inception of NAFTA,[2] they have become strategic at a new juncture where oil markets seem to swing to net-exporters' decisions (in this case Canada and Mexico) while the Persian Gulf has become a major target on the war against terror pursued by the US.

In 2001, Presidents Bush and Fox and Prime Minister Jean Chrétien created a North American Energy Working Group (NAEWG), an interministerial task force with the goal of sharing information and data for improving and enhancing energy trade and interconnections within North America (North American Energy Working Group, 2005). The meetings and publications of this trilateral group became more relevant after September 11 and the fall 2005 hurricanes in the Gulf of Mexico. Accordingly, the future of both Canadian and Mexican energy markets became reframed under a 'continental' strategy once energy became a major pillar of SPP (cf. Dukert, 2005).

SPP called for the creation of a 'policy environment' in which a sustainable supply and efficient use of energy could be promoted (cf. Security and Prosperity Partnership, 2005). It also recognized that energy has become 'critical to the prosperity and security' of the nations. Those high-level initiatives, and the growing pressures prevailing in energy markets due to a tight supply combined with natural disasters striking the US Gulf Coast, made regional energy cooperation a priority.

Although the security aspect of SPP entails in some cases strong state involvement and cross-border policy coordination in sensitive areas, the enhancement of energy security in North America has heavily remained anchored on market-oriented incentives combined with strong regulatory intervention at the state/provincial, federal and cross-border levels. That is, in contrast with other post September 11 security concerns in the region, such as border surveillance, migratory flows or air and space defense, which require different degrees of state involvement and inter-agency or

interoperability collaboration, as reviewed in the previous chapters, the security of energy flows and interconnections is still perceived as better guaranteed if market signals drive major decisions of overall stakeholders (consumers, producing companies, energy developers, government interests, etc). Thus, Washington's best option for dealing with energy risks and uncertainties is the development of conventional and non-conventional energy resources either at home or outside 'out of risk' areas,[3] for which the evolution of international oil prices remains the main indicator.

Current Bush administration's strategy is anchored in an optimistic perception on the fundamentals of energy markets. At present, high oil prices are not perceived as fueling inflation and hampering economic growth, as it was perceived and witnessed during the oils shocks of the seventies and eighties; the current American administration is rather betting to a new era of 'expensive oil' (ranging from low to top forty real terms US dollars per barrel for the next 25 years), during which several energy options could become possible: the development of 'non-conventional' hydrocarbon resources (tar sands, synthetic oil, shale oil, cold bead methane, etc); a new boost to nuclear energy; a new boost to coal consumption as an input for electricity, thanks to technological changes that have reduced damage to the environment; the growth of renewable sources of energy and the technological feasibility of synthetic fuels.[4] In other words, the Bush administration is betting to the transition of the oil era of the past century to a new era in which oil continues to be a major source of world energy, but mainly for fueling the transportation sector, within a growing and more diversified energy mix in which the entrance of synthetic oil and fuels make a breakthrough (Energy Information Administration, 2006).

The rationale by which expensive oil is perceived as an advantage rather than a vulnerability (as in the past) lies in the fact that the US economy is less and less dependent on energy intensive industries, such as cement, steel, paper, chemicals and the like. According to most recent estimates, growth in the following years will come from services industries (currently 80 per cent of US GDP) and non-energy intensive manufacturing. This, combined with a secular decline in energy intensity ratios (i.e. less and less energy is needed per unit of GDP), and with technological innovation, a growing population and labor productivity, have led to a forecast that the US economy will keep growing at average rates of 3 per cent in real terms in the following 25 years in spite of the prevalence of high oil prices (Energy Information Administration, 2006: 63).

Another optimistic supposition of the Bush administration is that international oil prices will remain high because of economic fundamentals, that is, major consumers and importers such as the US, China and India will keep their demand growing due to high economic growth. Since the Organization of Petroleum Exporting Countries (OPEC) remains the residual supplier, the development of additional spare capacity of these countries remains crucial for the evolution of prices. The increase in spare capacity is estimated to lag demand growth. However, the Department of Energy estimations do not take into account the geopolitical fundamentals that also explain the fall of oil producers' capacity: i.e. the de facto embargo that the US has with key oil producing countries, such as Iraq, Iran and to a lesser extent Libya and most of all the uncertainties raised by the already announced and accepted 'long war' against terror, 'rogue states' and 'undemocratic' governments of the Middle East. In other words, market fundamentals are heavily intertwined with American post-September 11 geopolitical interventions and calculations pursued in the Persian Gulf.

Thus, the strategic role that both Canada and Mexico are called to play in this new security partnership agenda becomes clear if we take into account that, in spite of all policy efforts, the United States will remain a country addicted to oil and gas. According to most recent available scenarios, in year 2030 oil and gas will still amount to 61 per cent of overall US energy consumption. Oil gross imports will amount to 64 per cent of petroleum consumption and gas imports to 21 per cent of overall gas consumption (Energy Information Administration, 2006: 64). Consequently, the major goal of a North American strategic partnership, in terms of energy security, is to keep both Canada and Mexico reliable and safe partners of the US. Both Canada and Mexico play a major role as net suppliers of oil to the US. In 2005, the former supplied 16.3 per cent of US gross oil imports, and the latter 15.4 per cent.[5] Both countries were the two single largest suppliers of oil to the US. Canada is the major exporter of gas to the US, providing around 15 per cent of its domestic consumption. The fact that the energy grids of the two countries are highly interconnected with US markets (mainly in the case of Canada), reinforces the strategic perception that these two border countries have become an extension of the US homeland. The US is interested not only in the steady evolution of both conventional and non-conventional sources of oil and gas in each of its North American partners, but also on the safety and integrity of any critical infrastructure covering energy flows to its homeland.[6]

Thus, according to the new global strategy for enhancing energy security in the US, and the regional priorities raised by the Security and Prosperity

Partnership (SPP), it is anticipated that Canada will play a leading role in a further continentalization of energy markets in the years to come. This will eventually reinforce the two-speed track by which North America is accelerating its own integration. I have already mentioned in the previous chapter that after the terrorist attacks of 2001, Canadians have followed a pragmatic approach by which they pursue the consolidation of the borderless economy coupled with political cooperation on the security front. A further integration of their oil and gas industry in the north–south direction will reinforce those two goals: Canadians become both a strategic and a safe supplier for balancing US pervasive oil addiction. By contrast, the US–Mexico relationship, although incorporated in the trilateral approach of SPP, remains entrenched within past and new bilateral conflicts (drug trafficking, illegal migration, environmental problems at the border, the mushrooming of 'lawlessness' spaces, etc) and surrounded by many uncertainties about the evolution of Mexico's oil exports.

## Feeding US oil addiction: the new strategic positioning of Canada as a reliable and safe supplier

In recent years, Canada has become a major oil power due to its huge proven reserves of tar sands, from which bitumen (a heavy, low gravity oil) and synthetic oil are obtained. With the equivalent of 178 billion barrels (Bb) of established reserves, oil sands have made Canada (mainly Alberta) the second largest reserve in the world, second only to Saudi Arabia (National Energy Board, 2004: 4).[7] This is the equivalent to 40 years of current US oil consumption, which made of Canada the closest and safest reservoir to the US. Since Canada has liberalized its oil and gas markets with the coming into force of CUSFTA, there is no major structural barrier impeding the development of this major source of non-conventional oil.

In 2004, overall Canadian crude production reached 2.5 million barrels (Mb) per day, of which 90 per cent came from Western Canada. Most of Canada's conventional and non-conventional crude oil reserves and natural gas stocks are located in the Western Canadian Sedimentary Basin (WCSB), a vast region encompassing most of Alberta and parts of British Columbia and Saskatchewan. Currently, oil sands provide 1 Mb per day, and according to Alberta's Minister of Energy, Greg Melchin, this amount could reach 3 Mb per day over the next decade and possibly grow to 5 Mb per day by 2030 (McFall, 2006).

The distinction between conventional and non-conventional crude oil is not simply academic. Extraction methods are more complex and

costly for non-conventional crude oil.[8] The raw material is bitumen, a high-viscosity hydrocarbon with elevated concentrations of sulfur and metals, which makes it more useful for asphalts and residual fuels. Lighter blends are preferred because they have higher yields of 'white products' such as gasoline, the demand for which dominates the demand for crude oil. Synthetic light blends are the most expensive to produce from non-conventional sources.

Supply costs for bitumen range between C$10 and C$19; upgrading for synthetic fuels boosts the cost to C$28. Supply costs could either increase or decrease over time, due to investment and technological innovation the trend is toward a cost reduction.[9] Currently, experts estimate that a return on investment from oil sands becomes possible if crude oil remains above a US$25 baseline (McFall, 2006).[10] If prices remain above US$40 per barrel in real terms over the long term, as predicted in the most recent forecasts of US energy agencies, a boom in oil sands production is anticipated.[11]

Table 6.1 summarizes US projections of Canadian non-conventional oil production over the next twenty-five years. While conventional production declines, this is more than compensated for by the increase in non-conventional oil production. According to this 'reference case scenario,' overall Canadian production could reach 5 Mb per day in the next twenty-five years if average oil prices range between US$40 and US$50 in real terms. If prices are higher, non-conventional oil could amount to almost 5 Mb per day on its own, or half that amount if international prices are lower. In other words, non-conventional production in Canada will remain sensitive to world oil prices. However, with a production level of 4–5 Mb per day, a level similar to that of Iran in past years,[12] Canadians will have the opportunity to play a major role in international oil markets.

The possible evolution of Mexican production is also shown in Table 6.1, as it is assumed Mexico will freeze, or even reduce, its export share in the short term, due to financial and infrastructure limitations. In this case, net Canadian exports will be able to compensate for the Mexican decline, and will be able to gain a larger share of the US energy import market. However, it is estimated that in the long run Mexico will increase its conventional production to a similar level to Canada (see Chapter 4 for the possible scenarios), and together, the two countries will eventually have the capacity to influence world oil prices.

Apart from infrastructure logistics,[13] the further deepening of energy markets between Canada and the United States must manage regulatory and environmental constraints. Transmission lines and import

*Table 6.1* North America's international petroleum supply. US Department of Energy reference case

| | 2004 | 2010 | 2015 | 2020 | 2025 | 2030 | Annual Growth 2004–2030 Per cent |
|---|---|---|---|---|---|---|---|
| Crude Oil Prices[1] | | | | | | | |
| Imported Low Sulfur Light | 40.49 | 47.29 | 47.79 | 50.7 | 54.08 | 56.97 | 1.3% |
| Imported Crude Oil Price | 35.99 | 43.99 | 43.00 | 44.99 | 47.99 | 49.99 | 1.3% |
| Production (Conventional) | | | | | | | |
| United States | 8.41 | 9.39 | 9.62 | 9.51 | 9.13 | 8.92 | 0.2% |
| Canada | 2.40 | 1.66 | 1.43 | 1.45 | 1.45 | 1.43 | −2.0% |
| Mexico | 4.10 | 3.97 | 4.19 | 4.48 | 4.78 | 5.01 | 0.8% |
| Total (Conventional) | 80.5 | 86.09 | 89.98 | 95.68 | 100.87 | 106.29 | 1.1% |
| Production (Nonconventional)[2] | | | | | | | |
| United States | 0.22 | 0.48 | 0.72 | 0.94 | 1.31 | 1.5 | 7.6% |
| Canada | 0.92 | 1.79 | 2.32 | 2.67 | 3.16 | 3.58 | 5.4% |
| Total (Nonconventional) | 1.96 | 4.91 | 6.92 | 8.02 | 9.73 | 11.52 | 7.1% |
| TOTAL | 82.46 | 91.00 | 96.90 | 103.70 | 110.60 | 117.80 | 1.4% |

[1]2004 dollars per barrel

[2]Includes lease condensates, natural gas plant liquids, and other hydrogen and hydrocarbons for refinery feedstocks

*Source*: Energy Information Administration, 2006, Annual Energy Outlook 2006. With Projection to 2030, US Department of Energy, Washington DC, p. 162

connections are regulated at the federal level in the two countries. State and provincial authorities regulate most energy matters. The mix of jurisdictions risks both regulatory confusion and political interference.[14]

Canada has not only become a strategic long term supplier to the US, Canadians have also proved to move rapidly in the security agenda of the US in terms of the protection of 'critical infrastructure', a key point pursued within SPP. As I explained in the previous chapter, the safety of infrastructure and any other transmission mechanisms linking the US to foreign energy flows has become, after September 11, a major goal in the protection of the homeland. Since oil and gas markets between Canada and the United States are fully integrated through pipeline interconnections, the security of this infrastructure has become critical. Key oil producing reservoirs (encompassing large volumes of downloading and storage operations), such as those located offshore in the Gulf of Mexico, could eventually become the target of terrorist attack by surface, air, or cyber-network (Norman, 2004). Local, state/provincial, and federal authorities must be prepared for such a scenario, and must be able to coordinate efforts with their foreign counterparts when infrastructure and transmission lines cross national borders.

With the US DHS in charge of the protection of critical infrastructure, it seems that a combination of market incentives in the energy field, combined with stronger regulatory oversight, has become the model for ensuring security, at least at the preventive level. The model is being built upon the experience of regional electricity organizations for ensuring the reliability of the grid and its interconnections. This is the case of the North American Electricity Reliability Council (NERC), currently encompassing eight regional electricity organizations (REOs) which ensure most of the power generation and transmission in both Canada and the US. Founded in 1968 as a response to previous major power outages, the goal of NERC is to coordinate the activities of the different REOs to establish standards and oversight mechanisms to prevent transmission failures. The organization of NERC already reflects the way power generation and transmission operates between Canada and the US.

Twenty years ago, electricity markets were heavily regulated at the local, state, and federal levels in the US. As electricity is not a commodity like other energy products (i.e. it cannot be stored, and it must be produced at the time of its consumption), markets became very localized and heavily dependent on the vertical integration of power companies. The situation changed once the federal government initiated the liberalization of electricity generation and transmission across the US. Markets became more regionally oriented, with strategic interconnections

among them. The regionalization of electricity markets did not stop at the 49th parallel, as numerous REOs included Canadian provinces. The Western Electricity Coordinating Council encompasses not only the western states of the US, but British Columbia and Alberta as well. The US-based Midwest Reliability Organization includes Saskatchewan and Manitoba, while Ontario and Quebec are members of the Northeast Power Coordinating Council, which also represents the interests of the US East Coast states. NERC has remained a private organization with voluntary membership and no enforcement mechanism to ensure the security and reliability of the electricity grid. When markets were locally based and regulated, private companies were able to internalize the costs of protecting the security and reliability of their operations. It was in their interest to do so, and localized price controls covered the additional costs. Once competition began to grow at the generation and transmission levels, it became less clear how to fund and operate the security of the grid. In fact, deregulation created a sort of regulatory patchwork of jurisdictions that overlapped or competed with the different levels of government (Nervius and Vancko, 2005). While markets moved towards a regional and even cross-border configuration, infrastructure and transmission development remained stuck at the state level. This dissonance provoked, among other things, a lag between the construction of transmission lines and the growth of energy demands.

The governance of the electricity grid hit a major crisis in August 2003, when the largest electricity blackout in the history of North America occurred without warning. It started with three daytime shutdowns at power plants in Michigan, mid-Ohio, and Cleveland, and quickly cascaded into a major outage affecting around 50 million customers in the United States and Canada (General Accounting Office (GAO), 2003: 1–4). The joint Canada–US taskforce that was created to identify the causes of the blackout concluded that human errors were the major origins of the crisis, including the inability of system operators to visualize events on the system, ineffective operation communications and coordination, inadequate training of operators, and inadequate reactive power resources (North American Electricity Reliability Council (NERC), 2004). In other words, reliability standards already agreed to by NERC members were not respected and there was no way to ensure their adherence and enforcement.

As a consequence of this crisis, NERC advocated major regulatory reform to ensure the security of the continental electricity network. They called for the creation of a full oversight organization which would issue reliability standards, the enforcement of which would be assured

through a mechanism of incentives (for those who complied) and fines (for those who did not). This proposal was incorporated in the 2005 Energy Policy Act (EPA) and in the trilateral SPP initiative. Indeed, the EPA called for the creation of an Electricity Reliability Organization committed to the harmonization of the industry's security standards, its oversight, and enforcement. At the same time, the EPA enlarged the jurisdictional faculties of the federal regulatory body, the Federal Energy Regulatory Commission (FERC), to impose sanctions on organizations or firms who fail to comply with security standards and provisions. FERC also became the primary authority to design and establish National Interest Economic Transmission Corridors through which inter-state transmission lines will be constructed to meet the growth and geographic changes in energy consumption. In June 2005 the three governments of North America called for the conversion of NERC into a continental organization – the North American Electricity Reliability Organization (NERO) – in which Mexico would initially join as an observer. By so doing, current NERC reliability standards became obligatory nation-wide in January 2007 and enforceable through a joint NERO–FERC collaboration. Two major consequences derive from this major regulatory breakthrough.

The first implication is that NERO will play a major role in policy harmonization to ensure the reliability of the electricity grid and its interconnections, this time at the continental level. NERO will continue to be a cluster of private firms and associations, but will now also encompass some publicly owned electricity utilities, as is the case in both Canada and Mexico. In the years to come, its role will not only be to ensure the reliability of transmission grids in order to prevent blackouts, but also to progressively internalize the security of the entire grid to anticipate and avoid any physical or cyberterrorist attack.

The second implication of this regulatory breakthrough is the empowerment of FERC as a backup authority in transmission matters and other energy decisions. Since FERC will be the ultimate authority to determine sanctions in cases of non-compliance with reliability or any other security standards, it will most probably request a similar role to federal energy regulatory bodies in Canada and Mexico. In other words, FERC will soon become the leading regulatory body to set standards and levels of jurisdiction for similar regulatory bodies in Canada and Mexico. These two countries still have highly regulated and vertically integrated electricity markets. However, when FERC opens the US transmission grid to any power company, it asks for reciprocity. Thus, Canadian companies exporting to the US are required to open access to their

transmission grids to American companies. This has prompted the provinces of British Columbia and Quebec – in an effort to enlarge their export markets – to introduce transmission rates modeled on the FERC tariff. For years, the federation and the rest of the provinces have been discussing the best way to accommodate their respective access regulations with those currently prevailing in the US (see Doern and Gattinger, 2003: 84–8). Now that FERC has become more powerful for the supervision of the power grid, regulatory practices existing in electricity markets in both Canada and Mexico will have to adapt to the new continental trend.

NERO's role in assuring the reliability and eventually the security of electricity provision in North America could become a standard for how the combination of a market-based approach (involving multiple stakeholders, incentives and fines) with a strong regulatory approach (where electricity is seen as a commodity) including regulatory coordination at the regional level (to take place within SPP), could be implemented in the oil and gas fields. This sort of 'privatization' of security operations have proved to be more functional and cost effective for regulators, since market organization and stakeholder involvement is very similar in the United States and Canada within the oil and gas sectors.

## The widening of NAFTA: US hub and spoke trade policy with Central America and the western hemisphere

In parallel to the two-speed deepening of North American integration taking place in the energy field, Washington pushed for a sort of 'widening' strategy of NAFTA-like rules to the rest of the western hemisphere. In contrast with the European experience, where the enlargement of the communitarian space is being done by the consensus of all members, the enlargement of NAFTA-ruling has been done by unilateral initiatives of the original NAFTA members. Mexico in fact has championed the extension of the 'open regionalism' ruling from the 1990s to the present. It has extended NAFTA-like treatment to most of its trading partners.[15] So has been the case with Canada. This also became the case once President George W. Bush obtained the Trade Promotion Authority (TPA) from Congress, in 2002, by which the Doha Round and Free Trade Area of the Americas (FTAA) negotiations gained momentum.

Though President Clinton launched the FTAA, or 'minilateral' negotiations in 1994, during the Miami Summit of the Americas, he never obtained the TPA from Congress, undermining any credibility on what he could negotiate. As known, TPA entitles the Executive to negotiate

trade agreements under a specific temporality and a general mandate. Congress gives its approval by accepting or rejecting the entire 'package' that was negotiated. Without a TPA, the US president can still negotiate commercial agreements but Congress could eventually discuss and reject part or the entirety of what was negotiated. Once the TPA was granted, the Executive had until June 2005 to reach an agreement. The faculty granted to the president was extended by Congress for two more years and finally expired in July 2007.

This section explores the context and approach followed by Washington on ongoing hemispheric negotiations for an FTAA. Washington's position on hemispheric negotiations suggests that for the US, FTAs are part of the general strategy for 'leveling the playing field' on trade disciplines and coverage vis-à-vis its trade partners. In other words, for the US NAFTA is just a building block for advancing US interests on trade and trade-related issues either at the bi-, mini-, or multilateral levels. As I suggested in the first chapter of this book, NAFTA was nested as an interface between multi- and unilateral trade relationships, and this continues to be the case, as witnessed by the US position within FTAA negotiations. However, once Washington realized that to strike a NAFTA-like agreement at the hemispheric level was not that easy, mainly due to the 'space of dissent' construed by MERCOSUR's position, a 'hub and spoke' approach was preferred in order to enlarge NAFTA treatment to Chile, Central American (CA) countries (under DR-CAFTA), and some Andean countries such as Peru and Colombia.

## The strategic goal of US-led open regionalism in the Americas

Open regionalism aims at consolidating market-oriented reforms at the national level and 'disciplinary' convergence towards the trade and corporate-oriented agenda being crafted within the WTO, and other multilateral institutions and regional regimes, such as NAFTA. The US has championed the promotion of open regionalism in the Americas, by trading market access to its own market in exchange for a new body of trade-related disciplinary regulations to be adopted and enforced by trade partners. These principles and rules were first embodied in bilateral agreements and regional architectures, such as NAFTA (see the first two chapters of this book). Currently, those norms and disciplinary regulations are being framed under the negotiations gearing towards a Free Trade Area of the Americas (FTAA), the aim of which is to level the playing field in trade and trade-related issues by compelling parties to play by US standards and rules. This long-term strategic goal is most

important for Washington and regional trade institutions nested under FTAs, or at least as important as other goals such as economic gains anticipated from trade liberalization and market access.

Figure 6.1 captures part of the dynamics of Washington's multi-track approach on trade negotiations. The US Trade Representative (USTR) attempts to impact the global agenda (in this case within the Doha Round of the WTO) by signing bilateral or hemispheric FTAs (such as the FTAA) worldwide. In the particular case of the western hemisphere, Figure 6.1 shows what is at stake in terms of US exports for those regions or countries. Though 45 per cent of American exports are concentrated in the western hemisphere, most of them go to the NAFTA region (36.7 per cent). Less than 9 per cent goes to countries outside North America in the western hemisphere. This suggests that what is at stake in ongoing bilateral and hemispheric negotiations in the western hemisphere is not just export enhancement, but as I explained earlier in the first two chapters of this book, an overall legal transformation of an economic order, the aim of which is to consolidate market-oriented reforms at the national level and to regulate state involvement in the economy, either vis-à-vis markets, firms, or their respective national legislations in environment and labor. The use of economic sanctions and fines, by introducing the legal figure of arbitrated dispute settlement mechanisms,

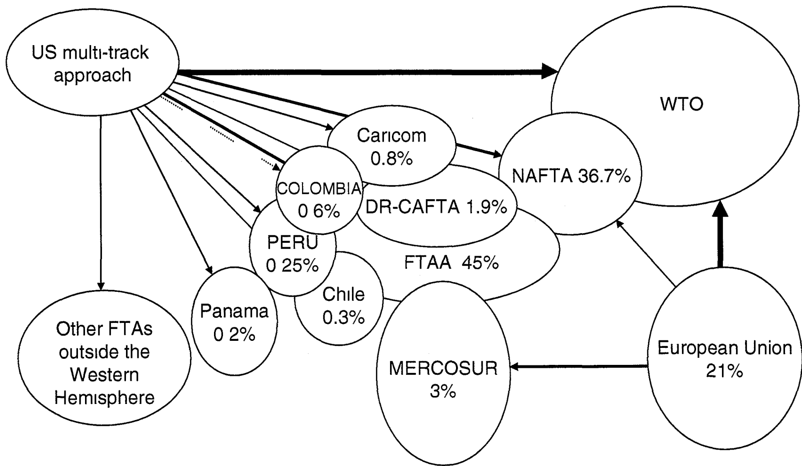


*Figure 6.1* The NAFTA regime as an interface between unilateral and multilateral approaches

is also generalized throughout this 'hub and spoke' strategy pursued by the US.

The foreign policy implications become more evident on bilateral deals, as for example in those clustered around the DR-CAFTA, covering just 1.9 per cent of overall American exports. During the seventies and eighties CA countries became the theater of civil wars and political instability. The linkage between trade and politics was done since those years when Washington enacted the Caribbean Basin Initiative (CBI) in 1982, through which preferential access was conceded to the Caribbean Common Market (CARICOM) and CA countries on a unilateral basis and during a span of time opened to succeeding renovations. The whole idea was to deter the upcoming of leftist or revolutionary governments in the area – as was the case in Nicaragua with the Sandinistas government or in El Salvador with the uprising of the *Frente Farabundo Martí de Liberación Nacional* (FFMLN) against a dictatorship. In 2000, Washington extended NAFTA treatment to Caribbean and CA countries through the Caribbean Basin Trade Partnership Act (CBTPA), to expire in 2008, and by which around two thirds of overall imports of those countries entered duty free in the US (Storrs, 2005: 59). The US thus has formally presented DR-CAFTA as the means to lock in unilateral market-oriented reforms extended to CA countries during the past decade and as a tool for fueling growth, abating illegal migration and consolidating new emerging democratic systems in the region (Ribando, 2005). As in the NAFTA negotiations, this time Washington asked for reciprocity, or as it was expressed in the jargon of the eighties, to 'level the playing field', by requesting CA and Caribbean partners to accept the body of disciplines and enforcement mechanisms already prevailing in the North American space.

Indeed, almost 14 years after NAFTA came into ruling, the US agenda for hemispheric and bilateral negotiations appears to be very similar, in both content and strategy, to the one followed when NAFTA negotiations were activated. As in those years, minilateral negotiations became intertwined with US multilateral positions within the WTO, and bilateral or minilateral approaches as witnessed by the US-Chile FTA and DR-CAFTA, and the Trade Promotion Agreements already negotiated with Colombia, Peru and Panama. As with past negotiations, minilateralism intends to promote an agenda more ambitious than what can be negotiated within a multilateral forum. In this sense, the optimal goal for the US is to get a 'Doha-plus' agreement at the regional level. Similar to the NAFTA negotiations, the US, and more specifically, the US Congress, once again set the timing and the coverage of the negotiations.

Both the FTAA and the Doha Round aim to deepen disciplinary rules and commitments reached in the Uruguay Round. Apart from phasing out remaining tariffs on manufacturing, further liberalization and regulation coverage in areas such as investments, services, property rights, government procurement and agricultural products is sought. In other words, agreements already reached under the so-called GATS, TRIMS and TRIPS of the Uruguay Round should be further developed. Regarding agriculture, market access should be widened, and the sensitive issue of regulating and/or suppressing export subsides and domestic supports should be addressed. Finally, the enforcement and surveillance of agreed-upon rules, mainly regarding investment and property rights, remains another sensitive issue to be resolved.

Since trade negotiations are commanded by the principle of 'single undertaking' and consensus, the common denominator that can be reached within multilateral forums is normally lower than what can be obtained in minilateral ones, let alone within bilateral deals. This explains why Washington still maintains the three-tier approach in trade negotiations (multi-, mini-, bilateral). In each of them, Washington tries to optimize the minimum it can get. After years of thorough negotiations, it is clear that what Washington anticipates obtaining from LAC countries increases in relation to the forum where negotiations take place. Within bilateral negotiations Washington increases its leverage to obtain the most of its partner, but at the same time the negotiating party has the opportunity, according to its bargaining capabilities, to 'customize' an agreement according to its own preferences. In multilateral negotiations Washington obtains less and weaker countries have the possibility of increasing their leverage by creating building blocs (as for example the G-20), for defending their interests. Minilateral negotiations, such as those for FTAA, remain in an ambiguous middle ground.

Following the TPA mandates, Washington's agenda was wider than that of the Doha Round since the launching of minilateral negotiations. The major features are market access, disciplinary rules and dispute settlement.

### *Market access*

Although Washington is still trading market access in exchange for a wider coverage of disciplinary rules, this time its goal is to circumvent the 'spaghetti bowl' created by the proliferation of FTAs in the Americas (cf. Inter-American Development Bank (IDB), 2002). Average MFN tariffs in LAC countries are much higher than those prevailing in the US.[16]

Trade has been liberated within sub-regional arrangements existing prior to the FTAA negotiations, such as the AC, the CACM, the CARICOM and the Common Market of the South (MERCOSUR). These FTAs have become discriminatory against US imports or outside-area countries, and could eventually become more discriminatory if new trade deals are struck with 'extra-regional' partners, such as the FTA currently being negotiated between the EU and MERCOSUR. Thus, in terms of market access, the US aims to circumvent the proliferation of FTAs in the region, and level the field for market access to all FTAA countries.

However, it is important to highlight that 84 per cent of all US merchandise trade with the Americas is concentrated between NAFTA partners. This gives leverage to the US in negotiations, mainly vis-à-vis trade blocs whose exports are highly concentrated in the US, such as the CACM, CARICOM, and to a lesser extent, the AC. In this respect, MERCOSUR countries benefit from a better bargaining position, because their trade is highly diversified, either within intra-regional exchanges, or with the EU, Asia and the US.

As for DR-CAFTA, market access was negotiated on a similar basis to NAFTA, that is, covering all the areas, including agriculture, although the phase-out of tariffs for sensitive products were conceded in a larger span of time (20 years). Sugar was exempted from zero duty free treatment by the US (similar to what was the case for Mexico), as well as white maize for entry in four CA countries (El Salvador, Guatemala, Honduras and Nicaragua) and potatoes and onions for Costa Rica.[17] The US also agreed to accept the use of special agricultural safeguards against import surges of selected sensitive products and performance requirements by importers (e.g. to buy a share of domestic crops during a phase-out period) (World Bank, 2005: 33–8).

However, the most contentious issue in agricultural opening is the role played by export subsidies – both direct and indirect – and domestic supports in the US. DR-CAFTA made no agreement on this, and neither did NAFTA, since the US has made explicit that disciplinary rules concerning subsidies and domestic supports could only be handled within WTO negotiations. This ultimately became a major difference with the Brazilian position in the FTAA negotiations.

DR-CAFTA also incorporates more flexible rules of origin, especially in the apparel and textiles sector, a major source of exports from the region to the US (see Figure 6.2). The agreement allows for the accumulation of origin from Mexico, Canada and all CA signatory-parties. Since rules of origin in this sector are based on 'yarn forward', this means that fabric coming from Mexico or Canada and transformed in any DR-CAFTA

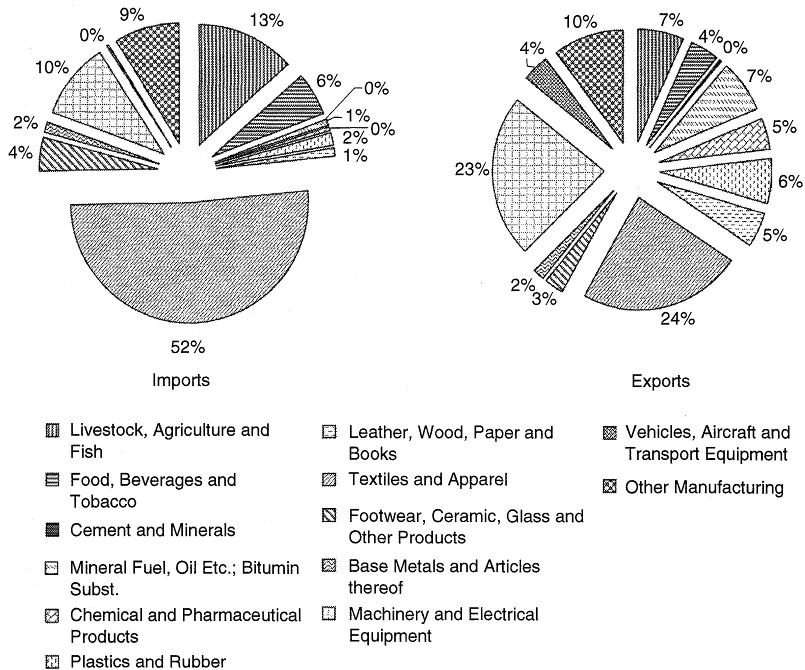


*Figure 6.2* US imports from and exports to DR-CAFTA members, 2005
*Source*: US Department of Commerce

country may enter duty-free in the overall extended region.[18] This has indeed made a de facto enlargement of NAFTA to the southern region. Moreover, since DR-CAFTA extended all the ruling and disciplines to the Dominican Republic and five CA countries equally, it is anticipated that a customs union and perhaps a sort of common market will be reached more rapidly than in the case of NAFTA.

### *Disciplinary rules*

According to the TPA mandate, Washington was bound to negotiate NAFTA-like agreements with its partners. Such an ambitious goal is difficult to reach within multilateral negotiations, where many countries don't want to move far beyond what was agreed upon within the Uruguay Round. In contrast, this has been the goal pursued by Washington during the FTAA negotiations. Apart from common disciplinary measures on trade remedies, i.e. AD, CVDs, and safeguards, Washington wants to widen the coverage of disciplinary measures to

include government procurement, investment, intellectual property, services, labor, and environmental standards.

NAFTA deregulated government procurement on a wider basis than negotiated within the GATT/WTO agreements. Since the Doha Round emphasizes the transparency of public procurement rather than widening the range of that market, Washington is betting on the latter within minilateral negotiations. DR-CAFTA deregulates government procurement on a NAFTA-like basis. As for investment rules, Washington is pushing for a NAFTA-like Chapter 11 deal for the FTAA, through which corporate rights will be empowered vis-à-vis state and public policies. DR-CAFTA struck an investment agreement similar to Chile's (see Chapter 2), incorporating an appellate body that is non-existent within NAFTA (World Bank, 2005: 46). This type of deal will be difficult to reach within the WTO. Since the US is still a major source of foreign direct investment for many countries in the region, and taking into account the fact that LAC countries have become a growing market for US investments over the past 20 years, Washington is very keen on negotiating an investment agreement in order to boost the confidence of their firms and investors in the region.

Furthermore, Washington is pushing for the deregulation of investment according to the guidelines of a 'negative list' approach, similar to what prevailed in NAFTA. Through the negative list method, a comprehensive agreement on investment liberalization is reached, and countries enumerate only those sectors which remain outside that coverage. This means that if new investment areas emerge in time, i.e. electronic commerce, these new areas are automatically covered by the new rules since they were not initially listed as exceptions. This approach highly contrasts with the one prevailing within the WTO negotiations, wherein investment deregulation is done following a 'positive list' methodology, whereby countries explicitly post the sectors to be covered by the new rules, and by doing so protect emerging fields that may appear in time.

This also points to a major difference between FTAA and WTO negotiations in the liberalization of services. Washington pushes for a liberalization process according to a negative list approach, while within the WTO negotiations are being done following the positive list method. Since trade in services is growing and new markets are emerging, Washington is keen on negotiating according to the first method with LAC countries. Due to the competitiveness of knowledge-intensive goods and services in the US economy (software, consulting, finance, pharmaceutical products, etc), Washington is also very keen on negotiating a NAFTA-like protective intellectual property rights agreement in

order to prosecute counterfeiting in the region. Both the US-Chile and US-DR-CAFTA incorporate these disciplinary areas. The enforcement of labor and environment legislation was not part of the Doha negotiations. In contrast, in the third draft of the FTAA, and in the text of both US–Chile FTA and DR-CAFTA, two new chapters have been included in this regard, according to the general guidelines of the TPA. Although the spirit of these two chapters reminds one of the so-called side agreements – on account of which NAFTA was accepted by the US Congress – the FTAA version goes beyond that. First of all, they contend to be part of the comprehensive agreement, and not a parallel agreement as was negotiated within NAFTA. Secondly, in the case of the enforcement of labor legislation, this particular draft calls for the respect of labor rights already encoded by the International Labor Organization (ILO). This means that the coverage is wider than in NAFTA, since the labor side agreement focused mainly on child labor, health and minimum wages.

*Dispute settlement*

Since NAFTA's coming into force and the establishment of the WTO, dispute settlement on trade and trade-related issues is no longer decided merely through diplomatic means. The introduction of quasi-adjudicatory arbitration either by NAFTA or the WTO means that dispute resolution is also being done by rules-based mechanisms. The goal is to avoid the politicization of trade conflicts and to increase the transparency and certainty for the enforcement of market access and trade-related regulations. The major role of ADSMs is to substitute national tribunals for reviewing or assessing the impairment or any breach to what was agreed upon. However, WTO's Body of Dispute Settlement relies on state-to-state arbitration, meaning by this that only states could eventually call for the installment of arbitrated panels for reviewing their decisions. By contrast, NAFTA for the first time introduced the formula of private-to-state dispute resolution, in the realm of investment liberalization (Chapter 11 of the agreement), which entitles private firms to call for a panel if they consider that a state impaired or breached their investment rights.

This so-called privatization of 'authority' has unleashed criticism and debate among NAFTA partners, as already explained in the second chapter of this book. For those reasons, it will be very difficult for the TRIMS agreement within the WTO to include such a formula for solving investment disputes. By contrast, Washington has pushed the NAFTA-like formula of arbitration regarding investment issues within the Chile

and DR-CAFTA agreements and the FTAA draft. In contrast with NAFTA, trade-related labor and environmental issues are to be enforced by teeth, since any dispute is to be addressed under the general ADSM of each of the agreements. Hence, state parties will be entitled to use trade sanctions or monetary fines to compel parties to abide by the rules.

*Extra items*

There are other non-NAFTA issues that have been integrated into the minilateral negotiations, such as the questions of 'smaller economies,' electronic commerce, and the role to be played by civil society during the negotiations. Since these topics are being discussed by 'non-negotiating' groups, that is, groups that are not entitled to produce a final text for the final agreement, their role is rather advisory. The 'smaller economies' group aims to attract the attention of negotiators to the need of providing preferential treatment for poorer and smaller countries. The civil society group has pushed, with some success, for a more transparent process of negotiation by publishing all drafts of the FTAA text and position papers coming from civil society groups.

The FTAA negotiations came to a stalemate at the beginning of 2004 due to the opposition of MERCOSUR, led by Brazil, to accepting an agenda that rather reflected US interests. The essence of the Brazilian dissent lies in the way open regionalism attempts to discipline and transform state policies. Although convinced that market-oriented policies are necessary for increasing the competitiveness of industries, Brazilia strongly believes that in some sectors, such as public health, government procurement and investment policies, the state must still keep a leading role. To accept the generalized liberalization of services, investment, government procurement along with a very strict corporate property rights agenda would have challenged Brazilian development policies.

Another reason explaining the Brazilian dissent was the imbalances of the FTAA agenda. While the US is campaigning for free trade policies as a means for regaining growth, it still maintains high domestic subsidies and barriers protecting its own agriculture. When the Brazilians asked for negotiations of the abatements of those structural barriers to be put on the agenda the US opposed it and provoked the interruption of the negotiations.[19] Ironically, the impasse on hemispheric negotiations reanimated multilateral trade talks within the WTO. Brazil and MERCOSUR were successful in bringing their own agenda in this forum and modified the whole set of negotiations by sticking to the need for discussing the reduction of subsidies. The Brazilian example shows that spaces of

dissent can be also construed in multilateral forums, provided there is enough flexibility for moving from regional to global settings.[20]

The way the US reacted to the Brazilian strategic move ended up by politicizing the space of dissent. The US renounced the maintenance of the single undertaking formula in hemispheric negotiations and decided to strike bilateral deals, NAFTA-like, with Chile, Central America, the Dominican Republic, Peru, Colombia, and Panama in a clear tactic to isolate MERCOSUR countries and Venezuela, its most recent member. The final outcome has been the polarization of trade blocs, in which the confrontational discourse of some radical dissenting countries have poisoned inter-American affairs. The polarization has also crunched some of the legitimacy of hemispheric trade negotiations, by eroding the appealing side of open regionalism and unveiling it as a unilateral US agenda.

## Towards the widening of NAFTA: DR-CAFTA and the enlargement of the continental 'southern periphery'

In August 2005, the governments of the Dominican Republic (DR), and five CA nations (Guatemala, Honduras, El Salvador, Nicaragua and Costa Rica), signed with the US what is now known as DR-CAFTA. Though negotiations were held on a bilateral basis with each of the participants this ultimately became an FTA, the rules and principles of which apply to all signatories and exceptions are addressed through a negative list attached by each country. Rather than opening the US market, Washington made permanent and reciprocal the unilateral opening all these countries had under the CBI of 1982 and the CBTPA of 2000. In exchange, DR and CA countries committed themselves to internalize the corporate-led disciplinary agenda in their respective economies. Similar to what NAFTA did in Mexico, DR-CAFTA has the intention to lock in previous market reforms that all countries in the region accomplished in the past decade. And similar to the Mexican case, countries of the region have to modify their respective legislations and policy practices in order to adapt their economies to the new corporate-led environment. The agreement covers a population of 45 million people, with all countries, except Costa Rica, considered to be low-income economies (according to the World Bank). DR-CAFTA came into ruling for all countries, including Costa Rica, where the ratification of the agreement was subject to a plebiscite in October 2007.

Since DR-CAFTA ruling embraces the core of NAFTA's market disciplines, it can be argued that the former agreement has instigated the enlargement of the North American space to the CA and Caribbean frontier.[21] In this

sense, I may also argue that the integrative trends in the region are not only becoming deeper, as witnessed by the continentalization of energy markets, but wider, as epitomized by the extension of a NAFTA-like regime from Guatemala to Costa Rica. Both deepening and widening are being done at different speeds and 'geometries', if we take the European integrative jargon. In the first section of this chapter I explained how the continentalization of energy markets is being done on a two-speed track, with Canada playing the leading position both in terms of enhancing the supply of energy and the security and reliability of the energy grid. In this second section I have explained how the widening of the NAFTA-like ruling is being done according to a time schedule negotiated by Washington with each participating member of the DR-CAFTA, and according to a 'customized' content in the agenda of negotiations. Though DR-CAFTA embraces the core of NAFTA disciplines, it must be understood as a 'second generation' FTA, in which some NAFTA-like chapters are missing (i.e. Chapter 19, reviewing the application of trade remedies by national bureaucracies, a chapter on competition policies), and new ones are introduced (i.e. e-commerce, transparency, and labor and environmental issues are this time part of the agreement).[22] Thus, the enlargement of the North American space is being done at different speeds and geometries, as witnessed by the differences embodied within DR-CAFTA.

How will the enlargement of the NAFTA-like ruling affect DR and CA countries? This time, the World Bank has become more cautious and less optimistic than 15 years ago, when NAFTA was signed. Though anticipating economic gains for export-oriented sectors that became consolidated during the past years, mainly *maquila* apparel and textiles, the World Bank has warned that the agreement should not be considered as a 'silver bullet' (World Bank, 2005: 3). And it will certainly not be. Table 6.2 summarizes different key economic and social indicators with the goal of comparing Mexico with the different members of DR-CAFTA. With the exception of Mexico and Costa Rica, most of whose indexes are rather similar (except that there is more poverty and inequality in the former country), the rest of the countries are to be considered small, unequal and low-income economies. However, there are several common threads for all these countries: they all depend on foreign trade for fueling their economies (as witnessed by the openness ratio index), the US remains their major source and destiny in their international exchanges,[23] manufacturing has become the driving force of their external sector, and they constitute a common geographic zone through which illegal migration and narcotics find their way to the US.

Apart from that, countries such as Honduras and Nicaragua are amongst the poorest in the western hemisphere (judged by their

*Table 6.2* Mexico, Dominican Republic and Central American countries: key development indicators

| | GDP per capita (US$)[a] | Openness ratio[b] | | Manufacturing Exports Ratio[c] | | Poverty rates | | Gini[d] | Average rate of growth[d] | Years[d] | HDI[e] 2006 |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | | 1995 | 2005 | 1990 | 2000 | 1990 | 2005 | | | | |
| Mexico | 9,803 | 58,2 | 61,4 | 57,6 | 78,2 | 47,8 | 35,5 | 0,57 | 1,5 | 27 | 0.821 |
| Costa Rica | 9,481 | 77,9 | 102,2 | 31,1 | 60,5 | 26,2 | 21,1 | 0,49 | 3,3 | 10 | 0.841 |
| Dominican Rep. | 7,499 | 75,8 | 59,8 | – | – | – | 47,5 | – | – | – | 0.751 |
| El Salvador | 5,041 | 59,4 | 72,0 | 29,1 | 80,9 | 60,2 | 47,5(2004) | 0,52 | 2,5 | 18 | 0.729 |
| Guatemala | 4,313 | 44,7 | 45,9 | 24,3 | 50,0 | 69,1 | 60,2(2002) | 0,58 | 1,5 | 39 | 0.673 |
| Honduras | 2,876 | 91,8 | 102,3 | 17,7 | 72,0 | 80,5 | 74,8(2003) | 0,57 | 0,4 | 240 | 0.683 |
| Nicaragua | 3,634 | 53,8 | 85,6 | 3,0 | 44,4 | 77,6 | 69,3(2001) | 0,59 | 0,7 | 102 | 0.698 |

[a]PPP adjusted. Source: http://hdr.org/hdr2006/statistics/indicatry/135.html, 2004
[b]Source: CEPAL, Anuario estadístico de América Latina y el Caribe, 2006, Santiago de Chile, March 2007, p. 143
[c]Source: Ros (2004)
[d]Source: Ros (2004: 12)
[e]Source: http://hdr.undp.org/hdr2006/Statistics

respective per capita income). El Salvador becomes a case on its own. Since the 1990s this country championed the adoption of neoliberal reforms in the CA region, by even adopting the dollar as its own currency. Table 6.2 shows, however, that the rate of poverty is still very high, although still lower than those prevailing in Honduras and Guatemala. El Salvador and Honduras have promoted the development of *maquila* settlements and strong military alliances with the US, but witnessed a serious social disintegration judged by the diaspora of illegal migrants and the proliferation of violent juvenile gangs known as the *'maras'* (Storrs, 2005: 32–5 and 53–4). This social disintegration has reinforced the authoritarian practices heavily embedded within fragile democracies.

The case of Costa Rica is also singular, but for opposite reasons to those prevailing in the rest of the CA countries. As shown in Table 6.2, Costa Rica is not only by far the richest country in the region, but features a poverty rate far below the Mexican standards and with the lowest index of inequality amongst all countries. However, what is singular about this country is that the good record of economic and social standards has been accomplished through strong state-led welfare policies. Until the 1980s, the state held a monopoly on banking, insurance, telephone and electrical services, railroads, ports and refineries. Following a debt crisis and the succeeding structural adjustment led by the IMF, the government started a privatization process according to the Washington consensus formula. However, insurance, telecommunications, electricity distribution, petroleum distribution, potable water, sewage, and railroad transportation industries remained state-owned (Storrs, 2005: 14–17). In this sense, and similar to the impact that NAFTA had in Mexico, signing a DR-CAFTA was for Costa Rica to lock in a second generation of market-oriented reforms. In fact, in December 2003 negotiations for opening the telecommunications and insurance industries of the country were suspended, and were resumed under the pressure of the then US Trade Representative, Robert Zoellick. This was finally accepted but spurred strong doubts and opposition to the agreement from professional sectors, fearing the demise of the developmental state, and the government was forced to call for a referendum in order to get ratification of the agreement.[24]

Column 7 of Table 6.2 also summarizes the rate of economic growth witnessed by our sample countries during the 1990s. Column 8, taken from an estimate done by Jaime Ros (2004), shows the number of years needed for each country (from year 2000) provided they keep growing at the same pace as past years, to reduce to a half their respective poverty rate. Although the estimates should be adjusted to most recent trends,[25]

Ros' estimates suggest that only Costa Rica, the least unequal country in the sample, will be able to halve poverty in a reasonable span of ten years. The conclusion is clear, the rest of the countries, including Mexico, should grow at higher rates if they want to drastically reduce pervasive poverty and income gaps.

In Chapter 4 I already explained the quandaries prevailing in Mexico's social policies for abating migration and reducing income gaps, whether vis-à-vis the US or the country sub-regions. Oil wealth and fiscal reforms have become the major tools for the country for redressing developmental policies in a post-NAFTA era. Needless to say, DR-CAFTA, like NAFTA, did not envision any means to bolster social policies for abating current asymmetries and inequalities that most probably will be exacerbated by the expansion and internalization of the disciplinary regime. Since DR and CA economies are already open, benefiting from market access to the US and heavily depending on *maquila* exports with low linkages with domestic chains, DR-CAFTA will most probably not be reflected in higher growth rates for the region.

Figure 6.2 shows that more than 50 per cent of overall DR-CAFTA exports to the US come from the apparel and textiles sector. Textiles also represent 30 per cent of overall imports, suggesting clearly the strong prevalence of *maquiladora* production. The World Bank's studies have suggested that additional gains might be reaped with the implementation of the DR-CAFTA, although they could be tempered by the elimination of world textile quotas in 2005 under WTO commitments (World Bank, 2005: 6).

This said, expanding the NAFTA formula to the southern region of North America will only expand and consolidate the role that Mexico has played so far in North America: a space for relocation according to locational advantages and a reservoir of cheap labor. Since most of the agricultural markets were opened by DR-CAFTA, and since the incidence of poverty rates is higher in the rural sector of each country, the disciplinary regime will probably exacerbate the push factors for moving populations further north. This potential scenario could eventually exacerbate ethnic cleavages, and the social inequalities and conflicts highly pervasive in the 'Puebla-Panama' region, such that political elites, from Washington up to Panama, could be prompted to reinforce a securitization of the extended region on a similar basis approached by SPP.

# Conclusions

Open regionalism is part of a legal transformation of an economic order, the aim of which is to consolidate market-oriented reforms at the national level and 'disciplinary' convergence towards the trade and corporate-oriented agenda crafted within the WTO. This new regional paradigm started its own articulation since the inception of the 'Washington consensus', in the early eighties, which bet to the liberalization of trade and the restructuring of state policies vis-à-vis markets. Under the leadership of the US, open regionalism was originally nested within NAFTA and became the model for trade negotiations for building future FTAs and the FTAA.

The new agenda did not present itself as the imposition of a hegemon, but as the 'natural universalization' of western liberal values and ideas on wealth creation and political organization which became highly legitimized by the end of the Cold War, and that reactivated a new wave of legalization and governmentalization of international affairs. The legalization trend has embraced fields such as trade, democracy building and human rights. The governmentalization process has become more intensive in the migratory arena, and more recently, after September 11, in the security field.

This double trend prevailing in Post-NAFTA North America – to discipline policy outcomes from state bureaucracies, and to calculate individual or social behavior from targeted populations – has become a major soft power technology in the hands of political elites for dealing with the pressures and dislocations provoked by globalization. Indeed, the growing legalization and governmentalization process in key issue areas is to discipline, shape and monitor the quality of state involvement in both 'global' and 'domestic' affairs, and to monitor and anticipate 'security risks' conveyed by moving populations and material flows.

Within the disciplinary domain, the US agenda for the FTAA negotiations appears to be very similar, both in its content and its strategy, to that followed more than ten years ago when the NAFTA negotiations were activated. The coverage of disciplines is similar: market access, government procurement, trade in services, opening of agricultural markets, liberalization of investment, and enforcement of property rights and of labor and environmental legislation. The whole agenda aims to discipline state involvement in the economy, either vis-à-vis markets, firms, or their respective national legislations in environment and labor.

In this sense, NAFTA and the US open regionalism of the eighties became a departure from the world economic order that had prevailed in the post-world war multilateral trade regime that featured 'embedded liberalism' as a framework for regulating state-market relationships. This departure consists in the introduction of a neoliberal agenda betting solely at restraining state intervention in trade and investment markets, as a means for creating an enlarged efficient regional market leading to productive efficiency and specialization. Until then, 'embedded liberalism' had aimed at creating and maintaining a multilateral liberal system compatible and consistent with state autonomy for using trade and financial policies to keep domestic stability, either economically or socially. Trade and employment creation, yet industrial protection, became 'embedded' in the liberal system of post World War II. The heritage of Keynes and 'new deal' policies remained entrenched in the system.

As we know, neoliberalism goes against Keynesian ideas, and its goal is to 'disembed' market mechanisms from state intervention, that is, the decoupling of the state from the market. According to neoliberal principles, states should just remain as credible regulators, promoting market efficiency by eliminating distortions, and through the enforcement of corporate rights. States are no longer buffers with policy tools for cushioning the economic and political costs that market openness brings with it. That is why the NAFTA principled regime does not make the linkage between trade and employment, or trade and development, but between economic openness and factor efficiency; it aims at the reduction of transaction costs provoked by state intervention in markets.

Mexico and Canada became without doubt the laboratory in which NAFTA's legalistic, disciplinary machinery was internalized, with the aim of transforming the previous state dirigisme prevailing (in the case of Mexico) or remaining (in the Canadian case) in each country. It is true that Mexico's institutional transformation of the state started

before NAFTA, but it is no less true that the new disciplinary body locked in previous reforms, and that deepened and accelerated the demise of state interventionism. The way Mexico joined NAFTA illustrates well how these new disciplinary machineries operate: institutional change was not the outcome of an imposition, or of Mexico's submission to a hegemonic agenda. It was construed as a means to release market mechanisms from inefficient and corrupted state control in order to increase welfare gains. It was not the demise of the state but its radical transformation into a regulatory agent according to good governance practices. In the case of Canada, entering into CUSFTA–NAFTA earmarked the end of 'nationalistic' Trudeau-style public policies and formalized and accelerated a north–south integration that had previously started on a sectoral basis (i.e. in the automotive sector).

However, NAFTA's disciplinary regime has not yet compromised Canada's welfare policies (education, health and social security) or Mexico's public policies grounded on the rents of its oil monopoly. The regional regime has rather put pressures and tensions in state–market relationships in the two countries, deepening domestic cleavages between those that advocate the primacy of markets over state intervention and those that claim that the role of markets and firms must remain embedded within social, political and historical institutions. In other words, what is at stake in a country such as Canada – and to some extent the US – is how welfare policies will survive or will be transformed after this restructuring of state–market relations. In developing countries such as Mexico, what is at stake is how social policies, dealing with poverty alleviation and inequalities, will survive the transformation of state capabilities. In this sense, North America is becoming the laboratory of a radical transformation.

The NAFTA regime and the transformation of the state and state policies has so far been a success, according to the original goals for which it was created. It has not only produced anticipated and desirable policy outcomes according to its institutional design, but anticipated positive expectations and rewards. This was proved during the Mexican peso crisis at the turn of 1995, when Mexico's political elite preferred to use more of the same medicine as a means to overcome the financial crisis. Now that NAFTA is about to accomplish its major goal of eliminating trade barriers in a span of 15 years, its own limitations have become apparent. The playing field for the three partners was not completely leveled. Subsidies, and trade remedies, remained anchored under national legislations explaining their overzealous use in sensitive products such as softwood lumber, dairy products, cement and steel.

NAFTA could not waive second and third generations of non-tariff barriers, as witnessed by the regulatory barriers pending between the US and Mexico in the transport sector. Within those sensitive sectors, NAFTA has in fact legitimized managed trade deals as 'second best' practices through which conflicts and impasses are defused.

The NAFTA regime has also harbored 'perverse effects' regarding the interpretation of Chapter 11, on investments, since firms have used it as a two-edged sword: for protecting their rights and for restraining governments from enacting policies addressing public concerns (mainly related to the environment). The Free Trade Commission (FTC) has already played a role in this by issuing some 'notes on interpretation' for limiting the scope of this chapter in relation to the overall NAFTA agreement. This move has reinforced the proposal, not yet supported by pubic officials, that stronger or new trilateral institutions are largely needed in order to deepen NAFTA commitments and consolidate a borderless economy. Suggestions range from the creation of a Customs Union to the building up of a strong North American Commission, staffed by a mix of civil servants and independent professionals. In contrast with the FTC, whose authority is limited to NAFTA-related issues, this new institution would be entitled to explore more ambitious architectures for deepening continental integration.

The consolidation of a North American economic space has become apparent during the post-NAFTA years. Regionalization trends have been accelerated since the inception of the CUSFTA–NAFTA, and have started to reverse at the turn of the century, once China became the fourth trade partner of North America. The consolidation of this economic space has become functional in terms of trade specialization and labor, as witnessed by two-way intra-industry trade flows between the US and its two neighbors, respectively. Thus, Canada consolidated as a high-tech competitive partner and a major reservoir of strategic primary resources (forest, water, oil and gas, fisheries and agricultural products), while Mexico affirmed itself as a space of manufacturing relocation and a major reservoir of 'competitive' cheap labor force, as witnessed by the high share played by *maquila* in Mexican exports and the growing amount of illegal workers going to the US during the post-NAFTA years.

The post-NAFTA functional economic space clearly features the consolidation of a continental hub, where the intensity of trade exchanges and specialization is most concentrated. This continental hub, conformed by the provinces of Ontario and Quebec, in Central Canada, and the US region going from the Great Lakes up to New England,

concentrates more than 50 per cent of overall Canada–US exchanges and hosts many of the most global and dynamic metropolises in North America. This hub is connected with two major spokes in the southwest American border, mainly conformed by the states of Texas and California, which function as an interface to most of the two-way trade coming from central and northern Mexico. Canada's and Mexico's trade and production specialization have also become functionally continentalized under the aegis of MNCs operating in the region, as depicted by the role played by both intra-industry and intra-firm cross-border trade. The networked production and exchange under the leadership of these companies have in many ways construed the continental economic space with its labor specialization.

In parallel to this continental spatial specialization, a sort of 'periphery' may be traced in the North American landscape. This periphery features lagging industries, mainly traditional agricultural activities, and populations that have become vulnerable to disembedded market forces unleashed by NAFTA. This periphery is located in Mexico's southern states and has become enlarged to include the DR and most of CA countries after the signing of DR-CAFTA. During the Fox administration (2000–2006), Mexico attempted to launch new social policies in order to abate development gaps that have widened during the post-NAFTA years between the Mexican south and the rest of the country. To release migratory constraints in the US labor market and to ensure the transfer of social funds to deprived Mexican regions were part of a failed strategy that President Fox named 'NAFTA-plus'. At the core of his strategy lay the premise that social and development imbalances in the country could only be addressed at the continental level, including a rise in oil exports and income for funding social expenditure. Though Mexico got neither migratory release nor transfer funds from the US, a market-oriented approach was earmarked in a bilateral 'partnership of prosperity' struck by the two countries in 2003, which became enlarged to Canada in 2005 when the Security and Prosperity Partnership (SPP) was crafted at the continental level under the common thread of security. Mexico's development agenda thus became compromised with the primacy of market values and, after September 11, by continental security concerns prevailing in the US, in which the reliability of continental energy flows became a priority.

September 11, 2001, not only adjourned the possibilities of implementing migratory and development policies favorable to Mexico, but it also meant the growing securitization of the overall North American agenda. Though NAFTA was not conceived as a mechanism for promoting the

political cooperation, let alone strategic integration, among the three North American nations, after that date the region moved rapidly to the building up of a continental security regime. At the basis of this security regime is the politics of fear under which Washington has articulated its war against terror. According to President Bush's national strategy, America has become vulnerable to an attack coming from terrorists located worldwide and rogue states harboring terrorists or WMD. In order to overcome this vulnerability, preemptive attacks and preventive wars have become legitimate in order to reduce America's vulnerability. This national campaign against terror translated first in a strategy of border security at the continental level.

The securitization of borders started in the US–Mexico front line prior to the terrorist attacks, through the erection of a barricaded line in order to deter the illegal trespassing of workers, human smuggling and narcotics. After September 11 the securitization of borders became extended to overall North America, embracing inner and outer borders under the principles implemented and overseen by the USNORTHCOM, located in Colorado Springs, by which Mexico and Canada became considered, under a security lens, a natural extension of the US homeland by surface and sea. Although there is a military component in this rapidly emerging security agenda, creating tensions with the US's two continental partners, the new security regime is so far still grounded in a soft power technology of governmentalization of human and material flows. The ultimate goal of this smart border approach (as opposed to the pre-September 11 barricaded border approach) is to permanently oversee and tactically intervene in the daily movement of cross-border travel within and throughout North America.

This new strategy attempts to defuse the national political fragmentation that prevailed in the past and to make of North America a geopolitical fortress ready to maintain a long and lasting war against terror. Though this strategy is still too young to know its own evolution and complexity (will it allow for a military alliance or rather deepen political collaboration? Will it allow US military or anti-narcotics staff the right of intervention in its extended homeland territory?), the growing governmentalization of human flows and commodities will facilitate US capabilities for classifying and identifying 'suspicious' and rogue populations moving within the US or the continental homeland. This growing governmentalization of human and commodity flows has become reinforced by the common fear of both Canada and Mexico of confronting new entry barriers to the US market grounded on security arguments.

That is why the two countries have rapidly adopted the smart borders agenda along the basic guidelines and concerns of the US. They attempt to accommodate the borderless economy crafted by NAFTA with the governmentalization of human and material flows conveyed by the smart borders strategy. Canada has become the model of this new economic and political collaboration under the framework of SPP by pushing NAFTA into a possible Customs Union, or ad hoc working groups for crafting bilateral deals on sensitive economic issues – such as resource-based products – and by striking a new interoperability military formula under NORAD and the BPG. Thus, an economic and political deepening is anticipated between these two countries in the years to come.

By contrast, Mexico, at the turn of a new presidential administration headed by President Felipe Calderón, has become the unsafe and perhaps the unreliable partner of the continental formula. In parallel to the construction of a new wall for deterring new non-authorized cohorts of workers coming from Mexican territory, the growing governmentalization of moving populations and commodities has crafted new spaces of 'lawlessness' along the Mexican territory. These 'failed-authority spaces' are being disputed by drug barons and smugglers and have become the focus of Washington's concerns at present. The message is clear: if the continental homeland is bound to remain protected and safe, Mexico's spaces of lawlessness must be eradicated. At present, President Calderón's strategy has been to empower and rely on Mexican armed forces for combating drug barons and trafficking, which sooner or later will compel him to look for the strategic and financial support of the US, as witnessed by the 'Mérida Initiative' announced by Presidents Bush and Calderón in October 2007.

Mexico has also become an unreliable partner as a key oil supplier in the region, at a time when the US is engaged in further continentalizing energy markets for keeping at bay its dependence on oil imports coming from Persian Gulf producers. Mexico's inability to enhance its oil reserves, and failure to promote an energy reform for fueling fresh money into the sector, will reduce dramatically Mexican oil exports – and heavily needed revenues – in the years to come. Though SPP bets at creating a favorable policy environment for developing energy markets at the continental level, Canada stands alone as the reliable partner for enhancing the energy supply needed by an oil-addicted American economy in the years to come. For Mexicans, rather than being a bargaining tool, the future of their oil wealth and production has become a quandary for them and for their North American partners.

Last but not least, the enlargement of the NAFTA space to Caribbean and CA countries – via the CBTPA and DR-CAFTA – puts additional pressure on Mexicans. Though the hub and spoke trade strategy followed by Washington in recent years attempted to boost the legitimacy of the disciplinary convergence formula earmarked by NAFTA, Mexican products will face stronger competition in the US market from similar products coming from the Caribbean and CA. Though some synergies could eventually be established between Mexican and CA exporters, social, migratory and security problems could become exacerbated in the extended region that I have depicted as the periphery of North America. Though sub-regional strategies such as the Puebla-Panama Plan have been devised and renovated in order to deal with both infrastructure shortages and social claims, those strategies still lack enough funding and strongly rely on purely market mechanisms. A sub-regional approach addressing the needs and imperatives of enhancing human development – and not only infrastructure needs and market-oriented incentives – is urgently needed. This urgency becomes more imperative in a sub-region where social and economic gaps are becoming rapidly intertwined with security concerns at the national and continental level (border control, migratory flows, drug trafficking, juvenile gangs, etc.). If social and economic gaps become rapidly 'securitized' under a similar formula to that conveyed by SPP for inner and outer borders, the North American periphery will be doomed to remain a space of strong inequalities, social conflict, peasant uprising, relocated populations and backwardness. A growing governmentalization of borders and human flows might defuse social unrest and threats to security, but it will not attack the roots of economic, social and political imbalances prevailing in 'lawlessness' spaces of North America. North American elites, whether economic, political or intellectual, must be conscious of the need to deploy social and development policies that go beyond simple market incentives in order to narrow gaps and inequalities exacerbated by continental trends.

# Notes

## 1 The Challenges of Globalization for US Economic Leadership: the Nesting of Regionalism in Washington's Neoliberal Trade Agenda

1. Hierarchical organization models have not been entirely substituted by network organizational models. The two of them rather coexist, and intermediate forms range between them. It seems that in technology-intensive industries, where innovations take place in a rapid way, the second model seems to become the best way to organize competition and production.
2. Mainly in terms of how states and chance play a major role or not in the creation of those competitive advantages.
3. The IMF, the World Bank (WB) and the General Agreement on Tariffs and Trade (GATT). The last of these became the World Trade Organization (WTO) in 1994, a by-product of the Uruguay Round that was launched in 1986.
4. For a discussion on the 'soft' to 'hard' law legalization process in global/ regional governance issues, see Abbot and Duncan (2000).
5. Hence, we should differentiate governance from government, in the sense that the latter is still identified with statehood, that is, the capacity of exercising power – including control of violence – of a certain ruling class in a territorial boundary. Governance is rather associated with the transfer of authority and power from the state to local, sub-national institutions on one hand, and to regional, multilateral, yet transnational institutions on the other hand, in order to deal with collective problems that can not be handled any more under the sole competence of states.
6. Joseph Nye defined 'co-optive' power as the capability of an agent or state to get others to desire, or want, what the first one is interested to promote. Soft power resources are considered to be ideological values, 'cultural attraction', and all range of principled institutions (cf. Nye, 1990: 188).
7. In a central part of his work, Michel Foucault showed how from the nineteenth century state policies in European countries became invested in these technologies of governmentality in order to deal with the social, technological and geopolitical changes provoked by industrialization. Though Foucault analyzed how 'subjects' were governmentalized in different cognitive-political periods (during Classical Antiquity and the Modern Era), the relevance of his ideas for our discussion lies in the assertion that the construction of a disciplinary- and science-based 'subject' (it could be individuals, populations, issues, domains, etc) was at the grounds of the rise of the modern state in the West (see Foucault, 1975, 1976, 1997).
8. Boas et al. also raise the issue between regional governance institutions and technologies of governmentality (2005: 9–11).
9. Good governance refers to a normative benchmark that different actors or 'stakeholders' involved in an issue regime must abide by in order to make the regime work. For a critical review of the concept see Weiss (2000).

10. What is also interesting in Foucault's approach around the governmentality of subjects, is that cognitive–disciplinary practices do not play a one-way role. Subjects are in some way obliged to be recognized through those techniques, but they can also revolt against them, that is, against the subjectivity imposed by those very techniques. Put in a mainstream language, construction and deconstruction are part of the same process in the creation of subjectivities, but are opposing struggles in the way domination and resistances are being defined in a society. At present, we are witnessing this double trend of re-objectivation and deconstruction of subjectivities. It is perhaps the most important sign of the kind of revolution globalization is provoking. In mainstream language it is what some authors call globalization from the top and globalization from the bottom. The first one referring to how hegemonic actors and organizations attempt to redefine their presence, rights and legitimacy in the emerging order. The second one referring to grass-roots and advocacy organizations aiming at challenging those new legitimacies in the making and at empowering alternative subjectivities (Foucault, 1975, 1997).
11. In his own words: 'The problem for the United States will be less the rising challenge of another major power than a general diffusion of power. Whereas nineteenth-century Britain faced new challengers, the twenty first-century United States will face new challenges' (Nye, 1990: 175).
12. That is the content or core goals pursued by an authority or a regime (see Ruggie, 1982: 382).
13. See Fernández-Kelly (2007), Harvey (2007) and Bradford, Grieco and Hufbauer (2005: 77–84). For a more systematized analysis on the epistemological and doctrinal fundamentals on how neoliberalism was conceived in the US, see Foucault (2004: 221–71).
14. Government purchases above US$225,000 were submitted to competitive bidding by the GATT. The CUSFTA reduced the threshold to US$25,000.
15. New rules concerning the use and definition of both subsidies and dumping were delegated, under CUSFTA and NAFTA agreements, to the decisions taken within the multilateral track.
16. For a thorough analysis on NAFTA negotiations see Mayer (1998). For an economic background on the genesis of NAFTA, see Weintraub (1990).
17. For a review of Mexico's foreign trade strategies prior engaging into NAFTA negotiations, see Bravo Aguilera (1989), and Olea Sisniega (1994).

## 2 The Governance of Economic Openness through Trade Regimes: NAFTA as a Model of US Open Regionalism for the Americas

1. As we know, these policy mechanisms are institutional arrangements normally bound by agreements or organizations through which consultation, negotiation, monitoring treaty compliance and other types of information are facilitated among members. As Stephen Krasner conceived them in a classical definition, regimes embody a set of principles, rules and decision-making procedures, both formal and informal, around which expectations of participants converge in a given issue area (Krasner, 1983: 186).

2. For some authors, the accommodation of divergent and/or contending interests is being done as a two-level game of negotiation; the first one being that of inter-state negotiation, the second one being that between national bureaucracies and local constituencies (see Milner, 1997; Putnam, 1988).
3. The classical study on this issue belongs to Keohane (1984,1989). See also Gilpin (1987) and Chayes and Handler (1995) for an updated discussion on the matter.
4. By 'soft law' is understood legal instruments that have a low level of precision (in terms of rules and norms), obligation and delegation (i.e. enforcement by third parties) (see Abbot et al., 2000).
5. As Hufbauer and Schott have highlighted, negative lists act as 'keep out' warnings, but at the same time point out the fields of future negotiations (as has become the case in Mexico's energy sector since the second part of the Fox administration (see Chapters 4 and 6). Many of the reserves in NAFTA are within Chapter 11, covering three types of exceptions: sectoral, such as is the case of the energy sector in Mexico or 'cultural industries' in Canada, reciprocal or 'tit for tat' and investment review reservations. Mexico was the country that posted most of the reservations under this chapter (89), while the US posted most of the 'tit for tat' reservations in the following fields: mining, petroleum reserves, pipeline ownership, cable television, ownership of US cultural industries, among other areas (see Hufbauer and Schott, 2005: 202–3).
6. We must remember that agreements are not just juridical forms which signatory parties have the discretionary capacity to comply with. They are institutions in themselves with practical and political consequences. They increase the efficiency in the making of policy options for states, because they don't have to recalculate their policy options each time they must make a decision in those areas already ruled by the Agreement. In this sense, as Friedrich Kratochwil has correctly asserted, rules and norms guide choices (Kratochwil, 1991: 43). Regimes and treaties thus embody an economy of procedural decisions and choices.
7. Chapter 14 of the Agreement, covering the treatment of banking, insurance and brokerage, also includes an ADSM which establishes a cabinet-level Financial Services Committee, entitled to make binding decisions. Ultimately, cases are submitted and decided under the guidelines of Chapter 20. So far, no disputes concerning financial services have been filed under either Chapter 14 or 20 (see Hufbauer and Schott, 2005: 210).
8. Within CUSFTA, the establishment of a panel under Chapter 18 required a mutual consent. Binding arbitration was also envisaged, if it was considered appropriate by the Trade Commission or when disputes arising from the Escape Clause (emergency and safeguard measures) were to be considered. The procedures for selecting panelists evolved; instead of choosing from one's own roster, as CUSFTA mandated, parties must choose under NAFTA from each other's roster, thereby giving to panels increased impartiality. Finally, the NAFTA gives to the complained-against party the right to activate a panel if it considers that the suspension of benefits exceeds the level of the grievance (Reisman and Wiedman, 1995: 19–21; Davey, 1996: 26–7).
9. Updated news of this bilateral pilot program may be found at Secretaría de Economía, www.economia.gob.mx, accessed on April 27, 2007.

10. In 2002 President George W. Bush lifted the ban for cross-border access of Mexican trucks, but two US Circuit Courts impaired this decision by alleging possible environmental breaches and threats (see Vega et al., 2005: 19–26; Hufbauer and Schott, 2005: 246–8).
11. At present, under the institutional framework of the Security and Prosperity Partnership (SPP) created after the US made homeland and continental security its priority, sectoral negotiations are taking place among the three members, including a working group discussing institutional differences and convergence among parties. For the political and economic aspects of SPP see Chapters 5 and 6. It is clear, that in cases such as transport services, NAFTA parties should move not to the homogenization of standards, but to the formula that has proved to be successful in the EU, which is a mutual recognition of standards.
12. Under the new WTO Dispute Settlement Understanding panel reports must be issued within six to eight months after the selection of the panelists. If the dispute is referred to the US Court of Justice, an adjudicatory decision could take more than two years (see Davey, 1996: 65).
13. According to Nakagawa (2006: 228), NAFTA partners choose WTO's ADSM if disputes arise under both WTO and NAFTA, according to exchanged notes in December 1993 where they agreed on this. Whatever the reason might be, the close interrelationship between NAFTA's ADRMs (mainly in Chapters 20 and 19) and WTO's reflects the close interconnectedness between the two trade regimes.
14. For a wider insight of the activities undertaken by both the labor and environmental agreements visit their respective home pages at: www.naalc.org/, and www.cec.org/. For a summary of the different cases presented before the Labor and Environment Cooperation Commissions, see Vega et al. (2005: 137–288).
15. This article grants Minimum Standard of Treatment to investors and investments. For the notes of interpretation, see NAFTA Free Trade Commission (2001).
16. Although the definition of investment in DR-CAFTA is wider than NAFTA's (it includes property rights, financial investments, services – such as turnkey, construction, management, production, concession, etc., and 'other tangible or intangible, movable or immovable property, and related property rights, such as leases, mortgages, liens, and pledges'), Annex 10C of Chapter 14 (the equivalent to Chapter 11 of NAFTA) clearly states that 'except in rare circumstances, nondiscriminatory regulatory actions by a Party that are designed and applied to protect legitimate welfare objectives, such as public health, safety, and the environment, do not constitute indirect expropriations' (DR-CAFTA agreement may be accessed in SICE: Foreign Trade Information System: http://www.sice.oas.org/trade/nafta/naftatce.asp (accessed on April 10, 2007)).
17. This is clearly stated in article 1904.8: '... If review of the action taken by the competent investigating authority on remand is needed, such review shall be before the same panel, which shall normally issue a final decision within 90 days of the date on which such remand action is submitted to it.'
18. The record is according to data collected from NAFTA's Mexican Secretariat home page.

19. In this case, the time elapsed was 734 days on average, and up to 1,210 days if decisions were appealed (see Mercury, 1995: 542).
20. We should highlight that out of the five cases remanded to the Canadian authorities, only one, compared to eight in the case of the US, were remanded more than once (Mercury, 1995: 543). This makes us think that US authorities were more reluctant to adapt to the new international ruling established by the CUSFTA. The fact that the three ECC were activated by the US makes sense on the same direction.
21. For a detailed analysis on how Chapter 19 has performed in dispute resolutions concerning the three countries see Vega et al. (2005: 35–80).
22. The dissident vote came from the two American panelists. For further information on this, see Davey (1996: 172–82).
23. Above that quota (which was fixed on 14.7 billion board feet per year with no tax), a progressive taxation was imposed on lumber imports, suggesting that the aim of the US government was to restrain Canadian exports, regardless whether they were subsidized or not.
24. The reference price was set at US$355 per thousand board feet. Below that price, exporters of lumber could choose between an option of export charges ranging from 5 to 10 per cent, depending on how low the price went, or to a lesser amount of charges (2.5 to 3 per cent) but subjected to a maximum quota of 34 per cent of expected US consumption for the month. For a complete version of the agreement see Softwood Lumber Agreement (2006).
25. See the dissent vote on Imports of Cut-to-Length Plate Products from the United States of America, (MEX-94-1904-02), in the NAFTA Secretariat: http://www.nafta-sec-alena.org.
26. For a thorough review of these institutional constraints in the activities of panelists and panels see Vega et al. (2005: 1–80).
27. R. Pastor makes the case for the creation of a sort of North American Community, that is, for a partnership that goes beyond commercial links and involves democratic and social values and the respect for cultural differences. He stresses that market mechanisms should be tempered '... by the obligation of the Community to assure that the distribution (of wealth) is not unjust, that disparities are reduced among peoples, nation-states, and regions, and that everyone has an equal opportunity to achieve his or her potential' (Pastor, 2001: 98).

## 3 After NAFTA: Trade Regionalization and the Emergence of a North American Economic Space

1. Our source for comparing Canada–US trade as well as Mexico–US trade is the US Department of Commerce. This makes possible any comparison among the three countries. Unless otherwise stated, trade data have this source and were mainly collected through electronic subscription to US National Trade DataBank (NTDB) (http://www.state-usa.gov/) and more recently from US Trade Online (http://www.usatradeonline.gov/).
2. According to UNCTAD, merchandise exports are classified according to the following ranks: primary products (minerals and agriculture), resource-based manufactures (processed food, tobacco, refined fuels, etc.), low-tech

manufactures (textiles, garments, footwear, etc.), mid-tech manufactures ('heavy industry' products, that is, that have complex but not fast-changing technology), and high-tech products (electronics, information, etc.). We use these definitions for the rest of the text. See UNCTAD, (2002: 180).

3. See Chapter 6 for the strategic role of Canadian oil in North America.
4. Industries in mineral fuels and textile sectors also encompass mid- to high-tech chains in their composition. This is the case, for example, of synthetic oil coming from bitumen and refinery products such as gasoline in the fuel sector and haute-couture and design in the garment sector.
5. This is also the case with trade in energy fuels. They were free of tariff before the CUSFTA and NAFTA so their rapid growth depends mainly on the energy needs (oil and gas) of the US economy. This same reasoning applies to Mexico–US exchanges in this sector.
6. In the case of US exports to Canada, apart from changes in volume traded, a slight decrease in real prices per unit of US goods exported impacted the overall outcome. That is, Canadians benefited from cheaper US products (Hillberry and McDaniel, 2002).
7. These are reviewed in the last section of Chapter 5.
8. Data are for year 2005 and were drawn from Banco de México: http://www.banxico.org.mx/, accessed in March 2006.
9. From 1994 to 2005 *maquila* imports have grown at AAGR of 14 per cent, while overall imports have grown at 11 per cent.
10. In 1995, exports of textiles and apparel to the US increased by 55 per cent in relation to 1994. This impressive increase was without a doubt nurtured by a peso devaluation of 50 per cent.
11. Figures for 1981 were drawn from Guillén Romo (2001), while most recent figures were drawn from official statistics coming from each country.
12. Figures obtained from Survey of Current Business, July 1996, July 1999 and August 2002.
13. All figures from Statistics Canada. Figures were estimated according to yearly net inflows and outflows coming or going to the sectors above mentioned and during the period 1988–2001.
14. In year 2005, the bulk of US–Canada trade accounted for 62 per cent of overall intraregional trade of NAFTA members. Mexico–US trade accounted for 35 per cent and Canada–Mexico exchanges for 2 per cent. See Figure 3.12 for sources.
15. When referring to north–south integration Canadians talk about a continental trend, by contrast to an east–west inter-provincial integration or transatlantic exchanges. According to Paelinck and Polèse (1999: 729) 'The term continental economic integration ... is defined ... to mean a situation in which nations of the same continent are increasingly linked to each other, in terms of trade and factor flows, rather than with parties in other continents'. The continental hub, thus, will make reference to this cross-border region encompassing the Great Lakes, Middle Atlantic and New England regions in the US and Ontario and Quebec in Canada.
16. 30.9 per cent of exports coming from this region were created by NAFTA.
17. At present, Canada has the equivalent of 178 billion barrels (bb) of proven reserves; oil sands have made Canada (primarily Alberta) the second largest hydrocarbons reserve in the world, second only to Saudi Arabia (National Energy Board, 2004: 4).

18. Chapter 6 reviews more in detail current trends on continental energy integration in North America.
19. If we assume that the South West is linked, through the South East and the South Central regions, to the 'continental hub'.
20. Data for 1997, MISER, July 1997.
21. These six geographical regions contain the following federal states: 1) Northern Border: Baja California, Baja California Sur, Sonora, Chihuahua, Coahuila, Nuevo León and Tamaulipas; 2) Central North: Aguascalientes, Durango, Guanajuato, Querétaro, San Luis Potosí and Zacatecas; 3) Central Mexico: Mexico City, Hidalgo, Mexico State, Morelos, Puebla and Tlaxcala; 4) Pacific: Colima, Jalisco, Michoacán, Nayarit and Sinaloa; 5) Gulf and Caribbean: Campeche, Quintana Roo, Tabasco, Veracruz, Yucatán; 6) South: Guerrero, Chiapas and Oaxaca.
22. The data used here for the rest of this and the following sections, are for 1999. All GDP information at the national and states level were obtained from the government-based data bank INEGI, Sistema Automatizado de Información Censal. SAIG 4.0. Censos económicos 1999, data stored on CD. We also consulted Sistema de Cuentas Nacionales de México. Producto Interno Bruto por entidad federativa, 1993–2000, México D.F. 2002. All data were estimated in real prices of 1993. Unless otherwise stated, figures used in this paper have this common source of information.
23. All data on FDI flows and firms, unless otherwise stated, come from Mexico's Secretaría de Economía's electronic webpage: http://www.economia.gob. mx/wb/, as of September 9, 2003.
24. As of 1999, 43.4 per cent of overall basic metals and metallic products were elaborated in the six northern states.
25. 80 per cent of all export-orientated *maquiladora*, employing 84 per cent of the overall labor force of this sector, are located in northern Mexican border states, from Baja California to Tamaulipas. Most of the *maquiladora* are clustered around the border line, on the Mexican side of Mexamerica (INEGI, 1998: 38–9).
26. The name of this organization in English is 'the countryside cannot take any more'.
27. The staples included barley, malt, wheat, rice, copra, soybean and sunflower. Poultry and pork also became fully liberalized in January 2003.
28. Mario Polèse and Richard Shearmur (2002) talk of the emergence of a sort of northern 'periphery' in North America conformed by the Atlantic Provinces and non-metropolitan regions of Quebec. According to him, these regions have become marginalized from the knowledge-economy already in place in Central Canada.
29. In order to tackle the growing politicization of agrarian claims, the Mexican government activated a two-tier strategy: it reinforced remedy measures for supporting key products and it started negotiations with the peasant bloc. During 2002, AD and CVD were imposed upon live swine, beef, apples and rice. The government also imposed SPS measures on pork, poultry, and apples. At the end of that year, Mexican trade law was modified in order to reduce timeframes for investigations, accelerating the imposition of duties and lowering the threshold for an injury finding. The new law also reduced the time needed for a safeguard investigation (Inside US Trade, December 4, 2002 and April 4, 2003). In January 2003 Mexico imposed a safeguard on poultry which

ended up, a few days before the ANC was announced, in a private undertaking of a five-year tariff-rate quota. SPS restrictions were also imposed on beans. For a detailed analysis of state–peasant negotiations during those years and their impact in Mexico's foreign trade policy see Morales (2006b).

## 4 The Rise and Demise of Mexico's 'NAFTA-plus Approach': the Scope and Limits of a North American Agenda Coming from the South

1. As of March 2006, 11.5 to 12 million people were estimated as being unauthorized migrants living in the US, out of which 6.2 million were estimated to come from Mexico (Passel, 2006: 1). Since not all these people are of working age or actively involved in the labor market, the number of unauthorized workers in the US is estimated to reach 6.3 million, out of which 3.3 million are Mexican (Kochhar, 2005: 1).
2. It is estimated that around 300,000 people cross the Mexican–US border illegally each year.
3. The issue of the so-called transfer funds for promoting development in deprived Mexican regions will be discussed in the following chapter.
4. Jorge Castañeda resigned as the head of the Foreign Ministry in January 2003, a few months before Mexico tuned its position vis-à-vis the US invasion to Iraq, a position that became highly controversial in Washington.
5. In 2002 the ratio of wage differentials between the US and Mexico in the manufacturing sector was 8.12, that is, American workers earned eight times more than their Mexican counterparts. In 1993 this same ratio was 7.07, showing how wage differentials between the two economies have widened in spite of NAFTA (see Pastor, 2005: 33).
6. For a general review of past US–Mexico migratory legislation and trends, see Secretaría de Relaciones Exteriores (1997).
7. In 2005, the US poverty line for a family of three was $16,090 a year. The median weekly wage of a migrant amounts to $15,000 a year, which means that many of them are automatically located below that line. Thanks to their family and friends' networks which allow them to abate the costs of housing and living, most of these workers can afford to live with these low wages and even transfer money to their families and relatives located south of the border (Kochhar, 2005: 22–5).
8. For a very interesting background on Mexico–US border politics, see Andreas (2000).
9. For an empirical study on migration and remittances see Marchand (2006).
10. For a review of this bilateral PP see its Mexican website: Partnership for Prosperity, http://p4p.fox.presidencia.gob.mx/p4p_us.php?seccion=sobre (accessed January 31, 2007).
11. The leading Mexican think tank, *Consejo Mexicano de Asuntos Internacionales* (COMEXI), published a document where Mr. Castañeda's original idea was further developed. See Rozental and Smith (2005), and Alberro (2005).
12. The following sections draw from Pastor (2001: 135–40; 2005).
13. Nominal or real terms, or in Power Purchasing Parity (PPP).

14. Pastor's proposal does not call for increasing oil output to fund this amount. However, he is clear in suggesting that the increase in government income, as a by-product of a major fiscal reform, ought to be committed to the funding of infrastructure and human capital in Mexico's south, and must not be diverted to other types of government expenditure.
15. For a critical review of this project, see Plan Puebla-Panamá (2003) and Bull (2005).
16. While in 1994 Mexico was still exporting 1.307 million barrels daily (Mbd), at the turn of the century exports amounted 1.603 Mbd. Exports also became progressively more concentrated to the US as a country of destination, going from 73 per cent in 1994 to 85 per cent of overall Mexican exports at the end of 2004 (Shields, 2005: 45). President Fox continued the upward trend, trying to reap the benefits of a tightening international market. In 2004, oil exports reached a historical high of 1.870 Mbd. In terms of value, exports income jumped from US$7.517 billion (Bdls) in 1994 to 23.397 Bdls in 2004 (PEMEX, 2005). Revenues have fluctuated during the past decade but have gained a new upward momentum since 2002, when a new era of 'expensive oil' seems to have started.
17. In 2005 they fell to 12,882 Bb, which at current levels of production will be depleted in ten years (Shields, 2005: 53; PEMEX, 2005). However, possible crude oil reserves amount to more than 20 Bb, most of them located deep offshore of the Gulf of Mexico.
18. In Spanish, this formula is called *Proyectos de infraestructura diferidos en el registro del gasto*, the acronym of which is *Pidiregas*.
19. Consumption below 2,500 kilowatts per hour (KWh) was to be supplied by state-owned utilities, representing around 60 per cent of current total sales. Above that limit, consumers would be entitled to buy directly from private utilities (see Bartlett, 2003: 237). The possibility of lowering the threshold would let private companies enlarge their market shares to residential consumers.
20. Covering mainly Mexico City and populations living in surrounding states.
21. Fox's proposals were embodied in four initiatives, one of which aimed at constitutional amendment. The four initiatives are accessible at the Mexican Senate website: http://www.senado.gob.mx/comisiones/directorio/energia/.
22. See Bartlett (2003: 242–301). For Manuel Bartlett, the privatization of electricity markets responded to the pressures of big electricity companies interested in increasing their profits and market shares, in coalition with Mexican officials interested in having a stake in the privatization process (Interview with Bartlett, 2006).
23. Growing imports are perceived in the country as a failure of the state monopoly to ensure self-sufficiency and as a means for transmitting higher international prices into the Mexican economy. Nonetheless, the government is currently anticipating that imports could be supplied by Liquified Natural Gas (LNG) shipments, entering Mexico's Atlantic coast through Altamira and the Pacific Coast through Baja California. The development of infrastructure and the construction of regasification plants are being accomplished and the government anticipates that part of the LNG shipments could eventually be re-exported to the US.

## 5 Policing Borders in North America after September 11: From Barricaded Borders to the Growing Governmentalization of Human and Material Flows

1. Canadians estimate that a one-hour assembly line shutdown costs around US$1.5 million. A 10 per cent increase in border costs could reduce by 25 per cent Canada–US volumes (The Senate, 2003: 7 and 9).
2. 'Vanishing Borders' was the suggestive title of the prestigious annual series 'Canada Among Nations' in year 2000, that is, one year prior to the terrorist attacks to the US (see Molot and Hampson, 2000). The Policy Research Institute of the government of Canada has also sponsored very interesting studies and surveys around the emergence of cross-border regions between Canadian provinces and the northern states of the US. For a synthesis, see Policy Research Institute (2006).
3. US Secretary of State, Condoleezza Rice, refined this strategy of 'regime change' through what she called 'transformational diplomacy' (see Rice, 2006).
4. The US Pacific Command is in charge of the defense of Hawaii and American territories located in the Pacific, whereas the defense of Puerto Rico and Virgin Islands is under the responsibility of the US Southern Command.
5. The following section is backed in official reports and information, mainly Security and Prosperity Partnership (2005, 2006a and 2006b).
6. This perception was nourished by the suspicion, outspoken by key political actors in the US, that some of the terrorists who perpetrated the attack on September 11 entered (legally) through the Canadian border.
7. According to Noam Chomsky, the US government has traditionally controlled social and individual behavior in the American space by articulating a politics (I would say a governmentality) of fear through which the notion of the enemy and insecurity is being construed and socialized. After September 11 this politics of fear has been renovated through a narrative on the 'War on Terror' (Chomsky, 2005: 18–41).
8. A representative in Capitol Hill from the State of Texas highlighted very well this double front of the 'war on terror' during a congressional hearing: 'No more serious of an issue could exist before this Congress, this Nation – than the WAR [sic] that is being waged on our southern border. While most of the country knows that we are actively fighting the War on Terrorism – only a small fraction of the American public is aware of the battle our local law enforcement officers are waging on our border with Mexico' (Committee on the Judiciary, 2006: 54). Indeed, 'law enforcement' to combat crime and terrorist-related activities, either at US territorial borders or within the homeland, has become the 'inner face' of the 'war against terror'.
9. In some ways Americans are being more and more governmentalized through what Chomsky calls a 'politics of fear'. Part of this governmentalization of fear is the growing discourse on 'border security' through which the monitoring, reclassification, targeting and detention of cross-border human flows is being done. See Didier Bigo (1998) for a general discussion on what he calls the governmentalization of fear and the security of borders in the western world.

10. INA warrants the detention of any alien who has committed a felony or an aggravated felony. This law contains many definitions of aggravated felony, including terrorist activities. The fact that the memorandum includes intelligence-based terrorist-related factors as a 'high priority' reason for detention highlights the nature and priority of screening operations. So far, trespassing illegally across the border is not a felony, but a civil violation, which allows for expeditious or voluntary deportation with no prosecution.
11. SPP has, for instance, established a bilateral group between the US and Canada in order to monitor the security of pipeline interconnections. See Chapter 6.
12. According to John Hostettler, a Representative in Congress from the State of Indiana and Chairman of the Subcommittee on Immigration, Border Security, and Claims at the House of Representatives in 2006, there had been 200 military incursions by Mexican military units into the US from 1996 to 2006. Although some of them were accidental, Mr. Hostettler presumed that some of the incursions appeared to support narcotics and/or human smuggling activities (Committee on the Judiciary, 2006: 2–3). Although Mexican authorities have argued that paramilitary groups supporting illegal activities at the border sometimes wear uniforms similar to those used by the Mexican military or police, the legal and political loopholes have become pervasive in specific points of the borderline.
13. See Canadian Council of Chief Executives (2004). Wendy Dobson (2002), from the University of Toronto, has also argued for pursuing a 'strategic bargain' with the US through which seamless access to the US market would be ensured (via a customs union or a sort of common market) by deepening security and military cooperation with the US.
14. CCCE's ideas were also incorporated in the trilateral task force sponsored by the US Council on Foreign Relations (2005).
15. Stephen Clarkson has been one of the major critics of both NAFTA and the deepening of military defense relations of Canada with the US (Clarkson, 2002). An insightful summary of the debate prevailing in Canada around the deepening of economic and military integration with the US may be found in Cámara de los Comunes (2002) and The Senate (2003).
16. Canada Border Services Agency; Canadian Security Intelligence Service; Correctional Service Canada; Royal Canadian Mounted Police; and National Parole Board.
17. The Bush administration has renewed the race for ground-based mid-course ballistic missile defense, alleging that rogue states or terrorists could use them for attacking the US.

## 6 Post-NAFTA Deepening and Widening Trends: Towards the Continentalization of Energy Markets and the Enlargement of the Southern Periphery

1. Convened for the first time in June 2006, by US Secretary of Commerce, Carlos Gutiérrez, the North American Competitiveness Council (NACC) has openly endorsed the spirit and working groups featured by SPP. NACC is

conformed by the respective national-based councils of the three countries whose membership includes the most important business groups in the region. For detailed information of NACC and its membership visit the website of the Council of the Americas, at: http://www.americas-society.org/coa/NACC/indexNACC.html (accessed on February 14, 2007).

2. Based on CUSFTA, Canada guaranteed energy supplies to the US by keeping the proportion of energy exports relative to total supply, and by avoiding dual pricing. Through NAFTA, Mexico began liberalization of cross-border energy trade in gas and electricity, although maintaining state monopoly on upstream and downstream activities. Private investment was also permitted in domestic gas distribution and transportation, as well as for independent electricity producers, provided they sold their output through the national electricity network still monopolized by the state.
3. The main risky area for the US is certainly the Persian Gulf, from where 21.7 per cent of overall American oil imports come. However, other countries such as Azerbaijan or Venezuela could eventually turn risky, depending on Washington's political calculations and interests.
4. The Energy Policy Act of 2005 launched the incentives for going into that direction. (See United States Senate, 2005).
5. Import shares from Saudi Arabia and Venezuela amount to 14.3 and 12.24 per cent, respectively. Imports from Gulf oil producing countries (including Saudi Arabia) amount to 21.7 per cent (US Department of Energy: http://www.eia.doe.gov).
6. It may be also argued that the US is highly interested in keeping, or increasing, its import share from either of these two countries in the foreseeable future. According to some authors, it is irrelevant for the US to reduce its oil imports from the Gulf producers (21.7 per cent of its imports in 2005), since oil markets are global and fully integrated (Cordesman and Al-Rodhan, 2005). This is true in terms of the evolution of crude oil prices. Any disruption in any part of the world is immediately transmitted to all importing countries. However, in terms of strategic options, the US's growing reliance on 'high risk' countries or areas could become a liability. Since the fall of the Shah, the US does not import oil from Iran. Washington has imposed sanctions – through oil embargos – to Iraq and Libya. If the 'war on terror' is going to last, as has been repetitively announced by the Bush administration, Washington will be keen to keep and-or increase its oil imports from 'out of risk' regions.
7. In contrast, the proven oil reserves of the other two North American countries are paltry: 22 billions of barrels in the United States and 15 billions of barrels in Mexico.
8. For all the technical procedures involved in oil sands production, see National Energy Board (2004).
9. For supply costs of Canadian oil sands, see National Energy Board (2004: 7). In the past decade, costs for bitumen were in the range of US$30–35 per barrel (McFall, 2006).
10. A US$30 range is established by American experts, see Energy Information Administraion (2006:52).
11. According to United States EIA estimates, the higher the price, the higher the volume that will be produced from non-conventional oil. In Mexico, the

opposite trend is anticipated, since Mexico's PEMEX is still a rent-seeking company which will attempt to optimize the value of its oil according to the fluctuation of prices. See Energy Information Administration (2006: 182).

12. From 1972 to 1978, that is, before the fall of the Shah, Iran's production of crude oil was above 5 Mb per day. Although Iranian production was below 3 Mb per day during the eighties, in 2005 it reached 4.05 Mb per day. See British Petroleum (2006).
13. Practically all of Canada's crude exports go to the United States, with the consumption of fuels concentrated in the northern and central states. Exports are shipped through a grid of seven pipelines going from north to south, the largest of which is Enbridge, carrying around 72 per cent of western Canadian crude oil shipments. This line crosses the western provinces and goes south to Chicago, creating a cross-border economic region between western Canada and the US Midwest. According to official estimates, the anticipated production of oil from bitumen will increase exports to the United States in the near term and will reach Canada's central provinces in the mid to long term if appropriate infrastructure is developed.
14. For a more detailed analysis on how different levels of jurisdiction and regulatory authorities interact on specific energy issues between the two countries see Ziff (2004).
15. From 1994 to 2005, Mexico signed and implemented 12 commercial agreements with its major trading partners: the US and Canada; Colombia and Venezuela (though Mexico cancelled the agreement with the latter country in November 2006); Costa Rica; Bolivia; Nicaragua; Chile, the European Union; Israel; El Salvador, Guatemala and Honduras; Iceland, Norway, Liechtenstein and Switzerland; Uruguay; and Japan.
16. 87 per cent of US merchandise imports from FTAA countries were already duty-free in the year 2000. Trade-weighted average US tariffs on imports from those countries were less than 1 per cent in the same year. However, most of the duty-free trade already existing in the region is explained by NAFTA. The duty-free share of US imports coming from the Andean Community (AC) is 39.7 per cent, from the Central American Common Market (CACM) is 40.4 per cent, from the Caribbean Common Market (CARICOM), 63.4 per cent and from MERCOSUR, 61.4 per cent. By contrast, average tariffs prevailing in LAC countries for manufacturing range from 10 per cent and for agriculture are even higher. All figures come from General Accounting Office (2001).
17. The US agreed to double the quotas for sugar imports from 99,000 metric tons in the first year to 140,000 over fifteen years. Tariff-rate quotas were accepted for imports coming from the US of beef, pork, poultry, potatoes, maize, rice milk and butter. See World Bank (2005: 33–5).
18. There are, however, quantitative limits for this. For the special regime of apparel and textiles under DR-CAFTA see World Bank (2005: 40–1).
19. For a thorough analysis of MERCOSUR's position in trade forums see Thorstensen (2003).
20. However, Brazil must be mindful that the political payoffs must be balanced with economic ones. For many years MERCOSUR has been accepted as an 'imperfect' customs union, meaning that managed-trade deals still prevail, and the return to safeguards and tariffs is considered 'business as usual' in a bloc where there is no macroeconomic convergence yet. If Venezuela uses

the bloc as a venue for confrontation with the US, different from the space of dissent that Brazil has built so far, the bloc risks fragmentation due to the exacerbation of national disputes and mistrust that still prevails among members, such as the current 'paper war' between Argentina and Uruguay (see Malamud, 2005; Motta Veiga, 2003).

21. Mexico had previously signed bilateral trade agreements with the five CA countries, while Canada already had one with Costa Rica and is currently negotiating one with the four remaining CA countries.
22. For a thorough analysis of the substantive and technical differences between NAFTA and DR-CAFTA see the excellent technical work done by the IDB, OAS and ECLAC (2005).
23. By and large, Mexico's foreign trade is the most concentrated in the US market. For the five CA economies, 36.7 per cent of their exports and 33 per cent of imports were intraregional, that is, concentrated in LAC countries (CEPAL, 2007: 229–230).
24. In October 2007 Costa Ricans voted in favor of the agreement. For an academic debate about the pros and cons of DR-CAFTA for Costa Rica see Flórez-Estrada and Hernández (2004).
25. Take, for example, the sudden reduction of Mexico's poverty rate during the span of 2000–2005, data not considered under Ros' analysis.

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