Free trade's false promises

Nafta has hurt the Mexican economy, and the US-Colombia free trade deal stands to replicate its mistakes

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John McCain has just returned from his so-called "free trade tour" in Mexico and Colombia where he highlighted the success of the North American Free Trade Agreement (Nafta) and showed his support for the stalled and controversial US-Colombia Free Trade Agreement.

It is unusual for a presidential candidate to travel abroad during a campaign and even more unusual to cite Nafta as a success story in Mexico. One can debate the benefits of Nafta in the US, but there is a consensus that Nafta has not lived up to its expectations in Mexico. Rather than learn from Nafta's mistakes, the US-Colombia Free Trade Agreement replicates Nafta and is projected to make Colombia worse off as well.

After Nafta, Mexico did witness a surge in exports and foreign investment, and for a while a bump in employment. However, such increases did not translate into growth and prosperity - economic growth in per capita terms has been just over 1% annually and poverty and inequality remain persistent.

Although foreign investment has surged, total investment has lagged at less than 20% of GDP - one of the reasons why Mexico's economy has barely grown in per capita terms since Nafta. More recently, foreign investment has waned as China became increasingly competitive. Moreover, foreign investment created an "enclave economy" the benefits of which are confined to an international sector not connected to the wider Mexican economy. In fact, foreign investment put many national firms out of business and transferred only limited amounts of technology.

It was hoped that Nafta would make Mexico an export powerhouse and that manufacturing exports would serve as the employment engine for the developing nation. Unfortunately manufacturing generates only 100,000 jobs per year, nowhere near the amount needed to satisfy the close to one million new entrants into the workforce. The result is that 500,000 people enter the US each year (another major controversy in the campaign), and the rest migrate to Mexican cities and tourist areas to work in the informal economy where there are no benefits or job security.

On the environment, the Mexican government estimates that the economic costs of environmental degradation have amounted to 10% of GDP each year.

The Colombia agreement seems to be on the same path. According to new estimates by the UN Economic Commission for Latin America, the agreement will actually make Colombia worse off by up to $75m or one-tenth of 1% of its GDP. According to the study, the losses to Colombia's textiles, apparel, food and heavy manufacturing industries that will face new competition from US imports will outweigh the gains in Colombian petroleum, mining and other export sectors.

What's more, reducing tariffs will strip the government of funds needed for combating guerrillas, fighting crime and developing their economy. According to a new study by the Inter-American Development Bank, the tariff revenue losses for Colombia will amount to $520m per year.

Nor is it clear that the agreement will bring foreign investment to Colombia. The World Bank's 2005 Global Economic Prospects report warned that, across the globe, trade and investment agreements themselves would not necessarily translate into new foreign investment. More recent studies have similar findings for Latin America. Articles in peer reviewed journals the Latin American Research Review and the Journal of World Investment and Trade found no independent correlation between foreign trade or investment agreements and increases in foreign investment in the region.

On the environment, the deal amounts to a rollback of small but significant steps that Nafta took. Unlike Nafta, the Colombia deal does not create a significant commission for environmental cooperation committed to improving the laws of the signatories, nor do does it provide any new funding for cooperation, clean up or compliance. Finally, the deal has a little secret not allowed under the WTO but taken from Nafta: it leaves open the possibility that ad hoc investment tribunals will interpret social and environmental regulations as "indirect expropriation" and allow foreign firms to directly sue governments for billions of dollars.

Nafta signalled a detour in US trade policy that has led to a long road of agreements that have been detrimental to our trading partners. The best trade deals for the United States is one that helps our trading partners grow their economies. Growth leads to political and macroeconomic stability and (selfishly) the ability to import more US goods.