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OP-ED CONTRIBUTOR

The Broken Promise of Nafta

By JOSEPH E. STIGLITZ

The celebrations of Nafta's 10th anniversary are far more muted than those involved in its creation might have hoped. In the United States, the North American Free Trade Agreement has failed to fulfill the most dire warnings of its opponents and the most fervent expectations of its supporters. In Mexico, however, the treaty remains controversial and even harmful — as do America's efforts to liberalize trade throughout the hemisphere.

There is some good news. In America, the "giant sucking sound of jobs being pulled out of this country" that Ross Perot predicted never quite materialized. The first six years of Nafta saw unemployment in the United States fall to new lows. (Of course, to most economists there was little basis for Mr. Perot's worries in the first place. Maintaining full employment is the concern of monetary and fiscal policy, not of trade policy.) Nafta has brought some benefits to Mexico as well; it was trade with America, fueled by Nafta — not the bailout of Wall Street lenders — that was responsible for Mexico's quick recovery after the financial crisis of December 1994.

But while Mexico benefited in the early days, especially with exports from factories near the United States border, those benefits have waned, both with the weakening of the American economy and intense competition from China. Meanwhile, poor Mexican corn farmers face an uphill battle competing with highly subsidized American corn, while relatively better-off Mexican city dwellers benefit from lower corn prices. And as all but one of Mexico's major banks have been sold to foreign banks, local small- and medium-sized enterprises — particularly in nonexport sectors like small retail — worry about access to credit.

Growth in Mexico over the past 10 years has been a bleak 1 percent on a per capita basis — better than in much of the rest of Latin America, but far poorer than earlier in the century. From 1948 to 1973, Mexico grew at an average annual rate of 3.2 percent per capita. (By contrast, in the 10 years of Nafta, even with the East Asian crisis, Korean growth averaged 4.3 percent and China's 7 percent in per capita terms.)

And while the hope was that Nafta would reduce income disparities between the United States and its southern neighbor, in fact they have grown — by 10.6 percent in the last decade. Meanwhile, there has been disappointing progress in reducing poverty in Mexico, where real wages have been falling at the rate of 0.2 percent a year. These outcomes should not have come as a surprise. Nafta does give Mexico a slight advantage over other trading partners. But with its low tax base, low investment in education and technology, and high inequality, Mexico would have a hard time competing with a dynamic China. Nafta enhanced Mexico's ability to supply American manufacturing firms with low-cost parts, but it did not make Mexico into an independently productive economy. When President Bill Clinton first asked the Council of Economic Advisers about the economic importance of Nafta, early in his administration, our response was that potential geopolitical benefits were far more important than the economic benefits. (Similarly, the European Union, for all of the economic benefits that it has brought, is mainly a political project.)

America perhaps stood more to gain economically than Mexico, but the concrete gains were likely to be small on both sides. Tariff rates on both sides were already very low, with Mexico's tariffs being slightly higher than America's, and Nafta would not eliminate important nontariff barriers. The disparity in income across the Mexican border is among the largest anywhere, and the resulting migration pressure was enormous. Doing what little America could do to enhance growth in Mexico would be good for Mexico, and good for America; and it was the right thing to do for our neighbor to the south.

Unfortunately, much of the goodwill that the United States might have expected has been squandered. First, America attempted to use barriers to keep out Mexican products that began to make inroads in our markets — from tomatoes to avocados to trucks to brooms. Despite the impressive efforts of workers' rights groups, efforts to ease the life of immigrants have stalled. Recent moves in California to prevent illegal immigrants from receiving driver's licenses and medical care have been a depressing sign that conditions for Mexican immigrants in this country are getting worse.

Of course, Nafta was a far more modest project than the European Union. It did not envision the free movement of labor, though that would have had a far larger effect on regional output than the free movement of capital, on which it focused. It did not envision a common set of economic regulations, or even a common currency. But hidden in Nafta was a new set of rights — for business — that potentially weakened democracy throughout North America. Under Nafta, if foreign investors believe they are being harmed by regulations (no matter how well justified), they may sue for damages in special tribunals without the transparency afforded by normal judicial proceedings. If successful, they receive direct compensation from the federal government. Environmental, health and safety regulations have been attacked and put into jeopardy. To date, suits with claims in excess of $13 billion have been filed.

While many of the cases are still pending, it is clear that there was not a full and open debate of the consequences of Nafta before passage. Conservatives have long sought to receive compensation for regulations that hurt them, and American courts and Congress have usually rejected these attempts. Now businesses may have accomplished indirectly, through treaty, what they could not get more openly through the democratic political process.

Meanwhile, those harmed by the actions of the foreign firms, for instance by what they do to the environment, do not have comparable protections of appealing to an international tribunal and receiving compensation. The concern is that Nafta will stifle regulation, no matter how important for the environment, health or safety.

All of this has important implications for the proposed Free Trade Area of the Americas, and for countries thinking of signing onto bilateral trade agreements with the United States. Signing a free trade agreement is neither an easy nor an assured road to prosperity. The United States has said it does not want agriculture or nontariff barriers to be on the table in these talks. But while it refuses to give in on these points, it wants Latin American countries to compromise their national sovereignties and to agree to investor "protections."

In fact, the United States has been demanding that countries fully liberalize their capital markets just as the International Monetary Fund has finally found that such liberalization promotes neither growth nor stability in developing countries. Unfortunately, many of the smaller and weaker countries will probably agree in the quixotic hope that by linking themselves to America, they will partake of America's prosperity.

In the long run, while particular special-interest groups may benefit from such an unfair trade treaty, America's national interests — in having stable and prosperous neighbors — are not well served. Already, the manner in which the United States is bullying the weaker countries of Central and South America into accepting its terms is generating enormous resentment.

If these trade agreements do no better for them than Nafta has done for Mexico, then both peace and prosperity in the hemisphere will be at risk.

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