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Statement of
John M. Melle
Deputy Assistant U.S. Trade Representative
for North America
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Committee on International Relations
Subcommittee on the Western Hemisphere
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Mr. Chairman, Members of the Subcommittee on the Western Hemisphere:

Thank you for the opportunity to appear before the Subcommittee today. I am pleased to represent the Office of the United States Trade Representative and provide an overview of our trade and investment relationship with Mexico.

Our commercial relationship with Mexico is defined by the North American Free Trade Agreement, the NAFTA, which has been in force since January 1, 1994. The NAFTA is a comprehensive trade agreement, covering trade in goods, services and investment, as well as government procurement, intellectual property rights, standards, and dispute settlement. Twelve years after implementation of the NAFTA began, essentially all of the agreement's transitional implementation periods are now complete with the exception of a handful of tariffs that fall to zero on January 1, 2008.

In evaluating the impact of the NAFTA on both the United States and Mexico, the appropriate place to start is with trade and investment flows.

- For goods, trade with Mexico has increased over three-and-one half times the pre-NAFTA levels; this increase is nearly double the increase in trade between the United States and the rest of the world.[1] Mexico has passed Japan to become our second largest trading partner and export market, trailing only Canada.

- There has also been a qualitative transformation in goods trade; in the 1980s, 80 percent of Mexico's exports were oil and raw materials. Today, value-added manufactured goods account for 90 percent of Mexico's exports.

- Much of the recent concern about U.S.-Mexico trade is with agriculture. In fact, agricultural trade has been remarkably balanced since 1993, with U.S. exports to Mexico increasing by $5.7 billion, and our imports from Mexico increasing by $5.6 billion, setting 2005 records in each direction. Numerous studies, completed both by the Mexican government and independent researchers, have documented that the NAFTA is not the cause of the challenges faced by parts of Mexican agriculture.

[1] 256 percent vs. 137 percent for 1993-2005. Source: World Trade Atlas, U.S. Census.

- Many of the most impressive export successes for the United States are also agricultural. Mexico is our largest market for a wide range of products – beef, dairy, swine, rice, turkey, apples, and dry beans among them. Our share of Mexico's imports is above 90 percent, due in part to the preferential access we have under the NAFTA for five of these seven products.

As a result of the NAFTA, we are already very close to free trade in goods with Mexico, with the average U.S. duty on Mexico falling to about 0.1 percent in 2005. Mexico's duties on U.S. goods are even smaller -- 0.003%.

We see similar trends for bilateral services trade, which has increased 76 percent since 1993. Since 1993, Mexico has also liberalized its banking sector, where the United States has a large presence.

Foreign Direct Investment (FDI) has also increased in all directions since 1993 - the United States and Mexico are investing more in each others' economies, and the rest of the world is also investing more in our economies.

- This change is especially important for Mexico. Since 1994, annual FDI inflows have averaged $15 billion, compared to less than $3 billion in the 1980s. Mexico's outward FDI flows have increased fourteen-fold since 1990, and it is now one of the largest developing country overseas investors.[2]

- Investment growth in Mexico has not come at U.S. expense. Even excluding housing, U.S. business investment has risen by 104% since 1993, compared to a 37% rise between 1981 and 1993.

The NAFTA is not the only trade agreement that has expanded U.S.-Mexico trade. Through the World Trade Organization, we have increased competition in Mexico's telecom market, conducted primarily by U.S.-affiliated companies. Following our recent win at the WTO, the wholesale costs of calling Mexico fell from 19 cents a minute in 2003 to under 5 cents a minute today. As a result, cross-border telephone traffic has witnessed extraordinary growth, almost doubling from 6.5 billion minutes in 2002 to 12.5 billion minutes in 2004, and saving U.S. consumers hundreds of millions of dollars while putting Mexico firmly in first place (above Canada) as the country Americans call most.

How much the NAFTA affected the changing trends in goods and services trade and investment cannot be measured precisely. This is especially true when looking at broader measures of economic performance since the NAFTA entered into force. However, there is a wide range of economic indicators that have grown more rapidly since the NAFTA was implemented.

- For the United States, job creation, industrial production, real compensation for manufacturing workers, business productivity and investment have all increased by higher rates in the period since 1993 compared with prior years.

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[2]UNCTAD World Investment Report 2005; page 310.

- Mexico has seen consistent GDP growth - 40 percent since 1993 - and annual real wage growth since 1995. This has been accompanied by much lower interest rates and rapid development of consumer finance services, such as home mortgages that have created a boom in consumer lending and home purchases.

There is substantial evidence trade has played a very positive role in Mexico's development.

- Firms that export have created more than half of Mexico's new jobs since 1995, and those jobs pay on average 40 percent more than jobs in Mexican firms that do not export.

- Mexican wages and employment tend to be higher in states with higher FDI and trade, and outward migration from those states is lower.

Current Challenges

To address the challenges the U.S.-Mexico trade relationship faces today and in the future, there are three circumstances to consider.

The first is implementation of the remaining NAFTA commitments by January 1, 2008.

- While less than 1 percent of our trade remains subject to duties, final removal of these duties has raised concerns in some sectors. As the three NAFTA trade ministers made clear at their annual oversight meetings last month in Mexico, they are committed to full implementation of the NAFTA and will not consider any reduction to our NAFTA obligations.

A second set of challenges must take into account the changes in global trade since the NAFTA entered into force. Simply put, Mexico and the United States have been reducing trade barriers with other countries, meaning the margins of preference provided by the NAFTA ten years ago are shrinking.

- In 1993, for example, the average United States duty on imports from all countries in was 3.2 percent. By 2005, it had fallen to 1.4 percent. Mexico still has a larger margin of preference today than it did before the NAFTA, but it is has begun to fall.[3]

- The United States also faces more competition in Mexico's market: Mexico has free trade agreements with 42 other countries today, compared with one (Chile) in 1994.

- And of course we both face the challenge of increased competition for goods and resources with economies such as China and India.

A third set of challenges is how to best address today's security concerns while not creating trade barriers, an issue my colleagues from Homeland Security describe in greater detail.

[3] The average tariff on Mexican goods in 1993 was 2.07 percent, a margin of 1.13 percentage points below the average U.S. tariff; the margin in 2005 is 1.3 percentage points.

I will conclude my remarks by briefly describing the work we are undertaking to meet these challenges, coming out of both the NAFTA trade ministers meeting held on March 24 and the meeting of Presidents Bush and Fox and Prime Minister Harper the following week in Cancun.

As I noted above, the key to our efforts is the recognition that the NAFTA has been a tremendous success for Mexico, the United States and Canada, and all are fully committed to the full implementation of the NAFTA in 2008.

Second, trade ministers have also launched a review of the NAFTA. This review will identify more ambitious disciplines in our more recent regional FTAs that could be candidates for incorporation into the NAFTA. As a part of this review, we will also identify work that could be undertaken to remove remaining trade barriers and explore how the NAFTA countries can work together to respond to current challenges faced in the global economy.

In Cancun, Presidents Bush and Fox and Prime Minister Harper affirmed their commitment to advancing the productivity and competitiveness of the region through the Security and Prosperity Partnership of North America (SPP), as noted in the State Department testimony. The SPP builds on and complements the NAFTA, and we can use both processes to advance common strategic North American goals. For example, under both the NAFTA and the SPP, USTR is soliciting proposals from U.S. industries to liberalize and simplify NAFTA Rules of Origin, making it easier to use the benefits of the duty-free access that the NAFTA provides.

To conclude, with the NAFTA firmly in place, the United States and Mexico have not only become better customers for each other but better neighbors, more committed partners, and effective colleagues in a wide range of trade-related international organizations.

I am pleased to answer any question the subcommittee may have.