Chapter 21

BEYOND NAFTA: THE EMERGENCE AND FUTURE OF NORTH AMERICA[1]

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For each of the three nations of North America, the decision to negotiate and sign NAFTA represented a sharp turn – almost a reversal – from previous policy. Canada and Mexico had long defined their vital interests in terms of autonomy from the great power next door. Both tried to keep their relationship with the U.S. at arm's-length for fear that a close embrace would be suffocating. Mexico constructed trade and investment barriers and championed a political doctrine of non-intervention to keep the U.S. from interfering in its internal affairs. Canada considered free trade at several moments in the twentieth century but each time retreated from the idea, fearful that U.S. investment would purchase the country's assets. The U.S. also resisted the idea of a regional free trading area because it believed that the optimal trading system was a global one, and as the world's wealthiest country and the initiator of the GATT after World War II, the U.S. government wanted to prevent any initiative that could undermine the global trading system.

While NAFTA was a departure from past policy for the three governments, in a paradoxical way it also represented a wholly natural response to the logic of integration. The three nations already were major trading partners of each other, and the international trading system had evolved in an unusual way. Instead of one world, there were actually three distinct trading regions: the EU, East Asia, and North America. Most of each region's trade with the world was actually within each region. Sixty-one per cent of the EU's trade with the world was intra-regional, and 58 per cent of North America's trade with the world was among the three nations. Together, however, all three trading regions were responsible for about 80 per cent of the world's gross product and trade (Pastor 2001: 21). In other words, the world trading system had rediscovered the benefits of proximity, and the three countries of North America recognized that their competitiveness in the world required a higher level of integration. NAFTA was a framework to achieve that goal.

NAFTA's purpose was to dismantle trade and investment barriers, and that explains why it reads like a business contract. Its architects planned neither for its success nor the crises that would confront it. Trade expanded as its proponents had hoped, but the three governments failed to build new roads, bridges, and border entry points, and thus the costs of delays exceeded the tariffs that were eliminated. Although NAFTA fueled the train of continental integration, it did not provide conductors to guide it. As a result, two setbacks – the Mexican peso crisis of 1995 and 9/11 – threatened to derail the integration experiment by disillusioning its members and erecting new barriers. In addition, NAFTA did not address many key issues – including the development gap separating Mexico from its northern neighbours, immigration, and energy. Moreover, the absence of any credible trinational institutions or any mode of North American governance has meant that the advantages of the continent were untapped and NAFTA's competitive edge eroded.

In this chapter, I will first explore the origins of NAFTA and the characteristics of the North American region. Then, I will evaluate NAFTA's impact on the region and its flaws of commission and omission. Finally, I shall propose an agenda for North America's second decade.

Origins and Characteristics

In 1990, when Mexico's President Carlos Salinas proposed a free trade agreement with the U.S., two years after CUFTA came into force, the GDP of the U.S. was about 20 times larger than Mexico's and ten times larger than Canada's. Asymmetry, whether in size of the economy or power of the military, is the defining characteristic of the relationship of North America's three states, and history has provided reinforcement of this unevenness. In contrast to Europe, where its catastrophic wars propelled its post-World War II leaders to unify, North America has been divided by its history and, more precisely, by its memory of nineteenth-century conflicts.

"Americans do not know, but Canadians cannot forget," writes Seymour Martin Lipset, "that two nations, not one, came out of the American Revolution." The U.S. emerged confident and proud of its revolution, whereas Canada defined itself to a considerable extent as "that part of British North America that did not support the [American] Revolution" (Lipset 1991). In 1812, the U.S. tried, but failed, to annex Canada, and the fear in 1865 that the formidable Union army might trek north to try again to expel the British was the principal reason why Canadians sought independence, and why the British accepted it in 1867 in the form of Dominion within the British Empire. Both judged correctly that the U.S. was less likely to make war against an independent Canada (Howlett, Netherton, and Ramesh 1999: 163).

Canadians remained wary of a close relationship with its southern neighbour. In 1911, Canadian Prime Minister Wilfred Laurier lost an election for concluding a free trade agreement with the U.S. Thirty-seven years later, Prime Minister William Lyon McKenzie King refused, at the last minute, to approve a freer trade agreement, evidently fearing a similar political result.

Having lost its war and one-third of its territory to the U.S. in the nineteenth century and having suffered several military interventions in the early twentieth century, Mexico's distrust of its powerful neighbour was deeper than Canada's. Because it has been less stable, prosperous, and democratic, Mexico also bears a heavier sense of inferiority and thus was averse to any proposal that would bring it into closer contact with the U.S. For this reason, any proposal from the U.S. to reduce trade or investment barriers was usually met with a curt rejection when officials deigned to respond.

Given this history and the imbalance in power, perhaps the only way for NAFTA to be implemented was for the smaller countries to take the lead. And, of course, that is what occurred, starting in the mid-1980s by Canada. In the 1970s, the Liberal Party under Pierre Trudeau had given Canadian nationalism an edge that made many Canadians proud and others very uneasy. In 1984, a national election brought the Progressive Conservative Party under Brian Mulroney to power with a large majority. Although his party had also opposed free trade with the U.S., Mulroney recognized a change in the public mood in favour of experimenting with more open trade. Not only had trade already increased, but a second reason for pursuing an agreement was to prevent the U.S. from arbitrarily shutting down trade in a particular competitive sector. President Ronald Reagan responded positively, and the two governments negotiated and signed a free trade agreement in 1988.[2] In the same year, Mulroney called an election, and the free trade agreement was hotly debated, with the Liberals strongly opposed. Mulroney won re-election, but by a narrower margin.

The reversal on free trade by Mexico and its President Carlos Salinas was even more startling than Mulroney's. However, when the debt crisis threatened to bankrupt the country in 1982, Mexico's leaders reassessed their development strategy and embarked on an export-oriented policy. The government imposed fiscal discipline, sharply reduced tariffs and limitations on foreign investment, and privatized state corporations. When Salinas took office in December 1988, he understood that the success of the Mexican economy depended on whether it could attract large sums of private investment, and neither Europe nor Japan were prepared to invest. He turned to Washington for a free trade agreement and for the key that he hoped would unlock the door of foreign investment.[3] The agreement was signed in December 1992 and came into force on 1 January 1994.

Evaluating NAFTA

NAFTA aimed to eliminate all trade and investment barriers and level the playing field on procurement, telecommunications, banking, services, and other sectors.[4] To secure the market, the three governments created a state-of-the-art dispute-settlement mechanism. Instead of trying to establish an institution for negotiating the reduction or harmonization of regulations, as the EU did, NAFTA selected a few sectors and harmonized the policies. The agreement was a minimum one that reflected the Canadian and Mexican fear of being dominated by the U.S. and the U.S. antipathy toward bureaucracy and supra-national organizations. It was an "invisible hand," classical liberal framework whose principal shared goal was the elimination of impediments to trade.

The vast literature on the consequences of NAFTA reflects to a certain extent the debate that preceded it.[5] In an astute review of the debate, Sidney Weintraub shows that many of the arguments of both advocates and opponents use similar criteria, which are related to the balance of payments or the gain and loss of jobs. Weintraub argues persuasively that these criteria are misleading and that a more useful assessment of NAFTA's progress would be based on its effect on total trade, productivity, intra-industry specialization, industrial competitiveness, the environment, and institution-building (Weintraub 1997).

With regard to NAFTA's principal goals on trade and investment, the agreement has been a resounding success. In 1993, Mexican tariffs averaged about 10 per cent, 2.5 times those of the U.S. By 1999, they had fallen to 2 per cent while import licensing and other non-tariff barriers were eliminated. Today, nearly all goods traded between the U.S., Mexico, and Canada enter each country duty-free. Agricultural products are the most sensitive, and thus freer trade in this area is delayed until 2008.

As barriers declined, trade and investment soared in all three directions. U.S. exports to Mexico increased almost fourfold, from $36 billion in 1990 to $140 billion in 2005, and exports to Canada more than doubled, from $100 billion in 1990 to $244 billion in 2005. Annual flows of U.S. direct investment to Mexico went from $1.3 billion in 1992 to $15 billion in 2001. U.S. investment flows in Canada increased from $2 billion in 1994 to $16 billion in 2000, while Canadian investment flows to the U.S. grew from $4.6 billion to $27 billion over the same period. More than 36 per cent of the total energy imports of the U.S. now come from its two neighbours. Travel and immigration among the three countries also increased dramatically. In 2000 alone, people crossed the two borders legally 500 million times. But the most profound impact came from those people who crossed and stayed. The 2000 census estimated that there were 22 million people of Mexican origin living in the U.S. Nearly two-thirds of them arrived in the last two decades. As many as 600,000 Americans living in Canada were eligible to vote in the 2004 U.S. election, which is more than those voting in six U.S. states (Brautigam 2004).

Intra-regional exports as a percentage of total exports – an index of integration – climbed from around 30 per cent in 1982 to 58 per cent in 2002. As in the auto industry, which makes up nearly 40 per cent of North American trade, much of this exchange is either intra-industry or intra-firm, two other indicators of an increasingly integrated economy. Many industries and firms have become truly North American.

There are still other signs of an increasingly integrated community. After 75 years of single-party rule in Mexico, in the year 2000 a highly professional electoral service, trained in part by Canadian election officials, conducted an election that was very closely contested. The result was an unprecedented acceptance of the process and outcome by all Mexican parties and the international community and a peaceful transfer of power. Indeed, the Mexican election was much more effectively administered than the one in the U.S. in the same year.[6]

The signatories of NAFTA deliberately wanted to avoid establishing any bureaucratic or supra-national institutions. The core of the agreement was therefore self-executing or designed to be implemented by *each* government. With regard to the dispute-settlement mechanism, William Davey, a Canadian scholar, concluded that it "worked reasonably well … the basic goal of trade dispute settlement … is to enforce the agreed-upon rules. By and large, these dispute settlement mechanisms have done that" (Davey 1996: 288-89).

Both the Commission for Labour Cooperation (CLC) and the Commission for Environmental Cooperation (CEC) provide citizens, corporations, unions, and NGOs an avenue for presenting their complaints. Since 1994, the CLC has received 23 complaints – 14 were directed against Mexico, seven against the U.S., and two against Canada.[7] Both commissions have done some useful work, and NGOs from the U.S. and Canada have helped their counterparts in Mexico to develop and pursue complaints. Both commissions reflect the caution of their governments. No one has criticized them for being too aggressive or trying to forge common responses on difficult questions such as pollution on the border or labour rights in the apparel industry (McFayden 1998; Hufbauer, Orejas and Schott 2000). Nonetheless, Mexico's environmental standards and capacity have actually improved faster than those of the U.S. or Canada, not surprising given the initial level, but encouraging nonetheless.

Another institution established under NAFTA was the North American Development Bank (NADBank), which has channeled funds into the border area to improve the environment. On a parallel track, the U.S. and Mexico negotiated the establishment of a Border Environment Cooperation Commission (BECC) to assist border states and local communities to design and coordinate environmental infrastructure projects. The BECC, based in Ciudad Juarez, Chihuahua, involves local communities in the development of projects and then seeks financing from the private sector and NADBank, which is based in San Antonio, Texas. Mexico and the U.S. have each contributed $225 million of paid-in capital, which gives the bank a lending capacity of $2 billion. The combination of chronic poverty and rapid urbanization and industrialization on the border have created a multiplicity of health problems, involving water and waste treatment, solid and toxic wastes, and air pollution. The two institutions were very slow in getting organized, but by 2000, 29 projects had begun or been completed.

During the past decade, Mexico has changed from an oil-dependent economy to an urban one based on manufactured exports. The impact on Canada was also quite pronounced. NAFTA deepened Canada's dependence on the U.S. market, but it also helped diversify and internationalize its economy. Canada's trade as a percentage of its GDP expanded from 52.4 per cent in 1990 to 89 per cent in 2002, making it the most trade-oriented country with the best economic performance in the G-7/8 (DFAIT 1999: 1).

As for the U.S., its total trade as a percent of GDP increased by 25 per cent during the 1990s. Those who predicted substantial job losses were wrong as the 1990s witnessed the fastest expansion of U.S. employment in decades. While Mexico and Canada grew more dependent on the U.S. – up to 90 per cent of its trade and with exports accounting for roughly 35 per cent of each GDP – the U.S. also grew more dependent on its two neighbours, with whom it does more than one-third of its total trade. More broadly, many firms became continental and more competitive.

An evaluation of NAFTA should not be confined just to trade and investment criteria or the side-agreements. One needs to view NAFTA as the centre of a unique social and economic integration process and of an effort to redefine the relationship between two advanced countries and a developing one.

The flows of people, cultures, food, music, and sports across the two borders have accelerated even more than the trade in goods and services. In 1996, the first destination for most U.S. tourists abroad was Mexico; 20 million Americans went there. The second most popular destination for U.S. tourists was Canada; 13 million traveled there. In 2003, the same pattern held, although fewer Americans traveled abroad – only 15.8 million to Mexico. Of the millions of tourists who visit the U.S. each year, the vast majority -- 20 million -- come from Canada. The second source is Mexico -- 7.5 million in 1996 and 10 million in 2003 (Crosette 1998: IV5; Fry 1992: 78; Chicago Council on Foreign Relations *et al.* 2004: 14).

The increase in numbers of immigrants understates their social impact. While the overall population of the U.S. grew by 13.2 per cent in the last decade of the twentieth century, the Hispanic population increased 57.9 per cent (from 22.4 million to 35.3 million) and the Mexican population by 52.9 percent (from 13.5 million to 20.6 million). About 30 per cent of the immigrants living in the U.S. today are from Mexico (Martin and Midgley 2003: 31). While half of all Hispanics live in California and Texas, during the past decade, the Hispanic population in Oregon doubled; in Minnesota, tripled; in Georgia, quadrupled; and in North Carolina, quintupled (Guzman 2001).

Remittances have played an increasingly important role in the relationship between Mexicans in the U.S. and their relatives. The most recent Mexican government report estimates that Mexican workers send their families about $17 million a day; in 2000, that amounted to $6.2 billion; and in the last decade, it totaled $45 billion (*La Jornada* 2000).[8] A recent survey found that 61 per cent of Mexicans had relatives living outside the country, mostly in the U.S., and 21 per cent received remittances from family members working in the U.S. (Chicago Council on Foreign Relations *et al.* 2004: 14).

The result of the social and economic integration of North America is that the region now represents the largest free-trade area in the world in terms of gross product and territory. In addition, North America is almost as integrated after one decade as the EU is after five decades. There has been a lack of compliance in some areas – notably, the U.S. imposes limitations on Mexican trucks, vegetables, and sugar and duties on Canadian softwood lumber and wheat. Mexico restricts high-fructose corn syrup from the U.S. The principal problem with NAFTA, however, is not the lack of compliance but the lack of imagination or rather political will to address some difficult questions.

First, NAFTA was silent on the development gap separating Mexico from its two northern neighbours, and that gap has widened. Second, NAFTA did not plan for its success; as a result, inadequate roads and infrastructure cannot cope with the increased traffic. The resulting delays have raised the transaction costs of regional trade more than the elimination of tariffs has reduced them. Third, NAFTA did not address immigration, and the number of undocumented workers in the U.S. jumped. Fourth, NAFTA did not address energy issues, and eastern Canada and northeastern U.S. suffered a catastrophic power black-out in August 2003, even while Mexico imports natural gas from the U.S. Fifth, NAFTA made no attempt to coordinate macro-economic policy, leaving the region with no way to prevent market catastrophes such as the Mexican peso crisis. Finally, NAFTA was silent about security, and 9/11 threatens to cripple the North American integration process by placing new and formidable barriers in the path of trade and movement of people.

An Agenda for North America's Second Decade

The thread that connects many of these omissions is the lack of institutions. Meetings of the three leaders of North America are "photo opportunities" because there are no institutions to prepare a common North American agenda (Pastor 2004). North America is not a trilateral partnership; it is characterized by dual-bilateralism (U.S.-Mexico and U.S.-Canada). Even when the governments negotiated a so-called "smart" border strategy, they duplicated virtually the same agreements.

This failure to construct North American institutions was deliberate. Canada thinks it can get a better deal bilaterally, though there is substantial evidence to question that. The U.S. is not exactly in a multilateral mood during the administration of George W. Bush. Mexico has been pursuing this, but no one else is paying attention. The architects of NAFTA also seemed determined to make the opposite mistake to that of the EU -- which they viewed as being over-institutionalized, excessively bureaucratic, and interventionist -- by creating no institutions.

There are good reasons to avoid the European example, but there is little chance of this happening. The two models of integration are quite different. In contrast to Europe, North America's model has been more market-driven, resistant to bureaucratic answers, pragmatic, and deferential to national autonomy. Nonetheless, North America should learn from the EU's 50 years of experience not only what it should try to avoid but what it should try to adapt. It should avoid excessive bureaucracy and a common agricultural policy, but if the three countries of North America are to become genuine partners, and if illegal migration from Mexico is to be curtailed, there is no goal more important than reducing the development gap, and the European experience is valuable in this area.

During the last 15 years, the income gap between the poorest and the richest countries of Europe shrank substantially, and migration was reduced. From 1986-2002, the per capita GDP of the four poorest countries of the EU—Spain, Portugal, Ireland, and Greece-- rose from 65 per cent to 80 per cent of the EU average. The progress was due to free trade, foreign investment, and a huge transfer of aid at a level that ranged from 2 to 4 per cent of the recipient's GDP. Good policies by the recipients, and conditioning aid on these policies, also made a substantial difference, as one can see in comparing the spectacular success of Ireland with the mediocre progress of Greece.

Among the lessons to be learned are, first, that the number of institutions for providing aid should be limited and have a "sunset" provision. Second, the most effective projects were in infrastructure and post-secondary education (community colleges in rural areas). Third, funds should be concentrated in the poorer countries (half went to the poor regions of the richer EU countries). Fourth, macro-economic policy coordination and resources are essential to cushion the effects of volatility of the poorer countries. Finally, a community requires that all members assist each other because problems cannot be contained, and growth in one can help others.

There was a moment at the beginning of the Fox and Bush administrations when the two leaders appeared to accept these points. In February 2001, President Vicente Fox invited President George W. Bush to his home, and together they endorsed the "Guanajuato Proposal," which read: "After consultation with our Canadian partners, we will strive to consolidate a North American economic community whose benefits reach the lesser-developed areas of the region and extend to the most vulnerable social groups in our countries" (Gobierno de la Republica de Mexico 2001). Unfortunately, they never translated that sentiment into policy.

A true partnership in North America is simply not possible while the people of one of the nations earn, on average, one-sixth of the income of people living next door. Actually, the gap is much wider because one-third of the people of Mexico live in deep poverty. Mexico's underdevelopment is not only a threat to its stability and, therefore, to its neighbours, but its growth offers its neighbours the most promising market.

In the absence of an explicit development strategy, 90 per cent of new foreign investment in Mexico went to just four states, three of them in the north, which grew roughly ten times faster than the south.[9] The border became a magnet for emigrants from the southern part of Mexico. Why do companies invest in the border area where labour is three times as expensive as in the south, labor turnover is 100 per cent after a year, and congestion and pollution is chronic? The answer: the roads to the south are poor, and infrastructure (roads, communications) is worse. The World Bank estimates that Mexico needs to spend $20 billion per year for at least ten years to meet the infrastructural deficit. This lack of infrastructure, combined with a Third World fiscal system, an energy sector that is inefficient and unreliable, and rigid labour laws, has resulted in a drop in Mexico's competitiveness, and a diversion of foreign investment to China.

Mexico needs to grow at 6 per cent per year for ten years in order to reduce the development gap with the U.S. by 20 per cent. A long journey would still be needed to close the gap, but just a consistent strategy that reduces it each year would alter the perceptions of Mexico and by Mexicans. A North American Investment Fund is needed to fill this infrastructural gap by investing $20 billion per year for ten years. The U.S. would provide $9 billion; Canada, $1 billion; and Mexico, $10 billion by gradually increasing its tax revenues from 11 per cent to 16 per cent of its GDP during the course of the decade. This is less than half of what the Europeans have been investing in the south of their continent. Fox, of course, tried unsuccessfully to persuade the Mexican Congress to approve fiscal reform, but if he had the leverage of a promise of $10 billion per year from the U.S. and Canada, the Mexican Congress might be more amenable. A new agency is not needed. The money could be managed by the World Bank. If roads were built, then investors would come to the centre and the south of the country, and immigration levels and disparities in income would decline.

The weakest link in North America is the lack of credible institutions, and the three governments should begin to fix that by establishing a North American Commission (NAC). Unlike the sprawling and intrusive European Commission, which manages and administers European policy, the NAC would be lean and advisory, consisting of just 15 distinguished individuals, five from each country. Its principal purpose would be to prepare an agenda on "North American issues" for the three leaders to consider at annual summits and then to monitor the implementation of the decisions and plans. The NAC would have an office that would gather statistics from the three governments, and it would commission studies of different sectors, like transportation, electricity, or technology. These studies would ask what could be done to facilitate economic integration in these sectors on a continental basis; it would submit these analyses with specific options to the prime minister and the two presidents. The NAC would encourage the three governments to respond to a continental vision. For example, in agriculture, farmers in a few areas cannot compete, and their representatives use all the legal and political channels possible to protect themselves. The three countries can continue aggravating each other, and subverting NAFTA, or they could negotiate a set of North American rules that modify their individual regulatory schemes.

A second institution would represent a merging of two bilateral legislative groups into a North American Parliamentary Group. The U.S. Congress is the most insular and clearly the most powerful and autonomous of the three legislatures. The approval in July 2001 of legislation to ban Mexican trucks from U.S. highways and a Congressional Resolution aimed at prying open Mexico's nationalized oil industry are just two examples of many that offend the U.S.'s neighbours. It is possible that a North American Parliamentary Group might become a mechanism for the three parliaments to deal with each other differently than they have in the past.

The third institution should be a Permanent Court on Trade and Investment. The dispute panels established under NAFTA are ad hoc, and it is proving difficult to recruit experts who do not have a conflict of interest. The hearings have finally been opened to the public. Some narrowing or clarification of the scope of Chapter 11 panels on foreign investment is also needed to prevent the erosion of environmental rules.

Canada and Mexico have long organized their governments to give priority to bilateral issues with the U.S., and Canada has recently established a Director-General for North American Affairs. Only the U.S. is poorly organized to address North American issues. In 1997, the Canada office was finally moved out of the Bureau of European Affairs and into the Bureau of Western Hemisphere Affairs in the Department of State, and in 2002, a Deputy Assistant Secretary was appointed to handle North American Affairs, but this official cannot negotiate on a par with domestic cabinet officers or congressional leaders. The U.S. needs to establish a White House Advisor to the President for North American Affairs. That person would need to bridge the National Security, Domestic Policy, and Homeland Security Councils and chair a cabinet-level Inter-Agency Task Force on North America. No president can have much of an effect on U.S. policy toward North America without such a wholesale reorganization.

Institutions are key to structuring the way governments function and address issues on a routine basis, but what would a North American policy look like? The first set of issues that the NAC should consider relates to transportation. "Crossing the border," concludes a May 2000 report by a Canadian Member of Parliament, "has actually gotten more difficult over the past five years." The causes are twofold: "While continental trade has skyrocketed, the physical infrastructure enabling the movement of these goods has not." And second, the bureaucratic barriers that confront cross-border business make the infrastructural problems seem "minor in comparison"(Pastor 2001: 104). While some people have been critical of the U.S. for imposing U.S. safety standards on Mexican trucks, the true problem is that there are 64 different sets of safety regulations in North America, 51 of which are in the U.S. A NAFTA subcommittee struggled to propose a uniform standard and concluded that *"there is no prospect"* of accomplishing that (Pastor 2001: 104; emphasis added). The elected leaders of the three countries should have been embarrassed and would have been, if anyone had been paying attention.

The North American Commission should review this issue and develop an integrated continental plan for transportation and infrastructure. The first step is for the U.S. and Canada each to develop national standards on weight, safety, and configuration of trucking and then negotiate with Mexico on a single set of standards. Second, the governments should eliminate feather-bedding schemes that increase the cost of transporting goods across the borders. Third, the governments should plan and finance new highway corridors on the Pacific Coast and into Mexico. Fourth, the regulatory agencies should negotiate a plan that would permit mergers of the railroads and development of high-speed rail corridors between Canada and the U.S.

The establishment of the U.S. Department of Homeland Security represents as great a threat to North American integration as does the terrorism it is designed to confront. In the immediate aftermath of 9/11, the U.S. responded by virtually shutting down the border. Within hours, trucks on the Canadian side were backed up as far as 25 miles. Companies that relied on "just-in-time" production began to shut their plants. Canada responded first, by negotiating a 30-point "smart border" agreement with the U.S. The essence of the strategy, which had been developing before 9/11, is to separate low-risk goods and people; expedite their transit with transponders, sealed containers, pre-clearance, and other techniques; and concentrate inspection resources on the high-risk traffic. Mexico followed a few months later with a similar agreement with the U.S.

This strategy is too narrow to be a serious or enduring solution to what is fundamentally the same integration dilemma: how to facilitate the legitimate flows of people while protecting ourselves from terrorists and smugglers. What is needed is a broader approach to continental integration, first, by negotiating a customs union with a Common External Tariff (CET). This would significantly reduce inspections at the border and would eliminate the cumbersome rules-of-origin provisions. Mexico will have the most difficulty because its tariffs are the highest, but, fortunately, President Fox, the most visionary of North America's leaders, proposed a customs union and more. The negotiations would be very difficult, but not beyond the reach of the three countries, and it would accelerate integration.

The problem of transaction costs reaches beyond the issue of trucks and transportation. As the three countries deepen their integration, their three regulatory regimes have raised additional impediments, which are evident in the divergent approaches to trade in pharmaceuticals, mad cow disease, and softwood lumber. Part of the problem stems from the many regulations that customs officials need to administer on the border. The Canadians, for example, have to enforce 96 statutory regulations on the border, while U.S. customs inspectors are responsible for 400 separate statutory requirements. Regulatory standards – from product safety to pollution to business competition – all affect the flow of goods. New approaches are needed to reduce the protectionist dimension while assuring health, safety, and security. These might involve new North American regulatory agencies or coordinated subcommittees of existing national agencies. The second decade of NAFTA will need to address the emerging regulatory agenda.

The U.S. and Canada should also negotiate a convergence of their immigration and refugee policies. It will not be possible to expand this to include Mexico until the development gap is reduced, but in the meantime, all three governments could negotiate a "North American Passport," which could be extended to a wider group of citizens of the three countries each year.

For security reasons, all three governments need to focus more on the continental perimeter, and one way to do that, while at the same time eliminating the duplication of documents that comes with crossing the border, would be to establish a single "North American Customs and Immigration Force." This force would be composed of officials from the three governments and trained together in a North American professional school. Most important, if the Department of Homeland Security is not to become a fortress and insult to its neighbours, Mexican and Canadian perspectives and personnel need to be incorporated in some way.

Finally, our three governments could learn from the EU's project to fund five EU Centres in the U.S to stimulate research and awareness in the U.S. of the EU. The three governments of North America should sponsor Centres for North American Studies in each of the countries to help all understand the problems and the potential of North America and view each other as both nationals of each country and also as North Americans.

Is any of this feasible? Since NAFTA came into effect, the opposition to free trade agreements has grown. Some people fear that they could lose their jobs to countries with low wages. Others fear that global development will have an adverse effect on the environment. Still others fear that a free trading system will be dominated by U.S.-based multinational corporations. Efforts to deepen North American integration will undoubtedly provoke the same groups plus others in Canada and Mexico who worry that steps toward a community could diminish each country's identity or accentuate their vulnerability. The chapters in this book by Janine Brodie (Chapter 20) and Cristina Gabriel and Laura Macdonald (Chapter 16) capture and articulate such fears.

Are these concerns legitimate? Some stem from a fear of globalization. Certainly, as global competition increases, wealthier countries will lose unskilled or manufacturing jobs to China, India, and other middle-income countries. To the extent that workers cannot move up the value ladder, they will lose out as "producers," even while they benefit as consumers. Of course, the essence of globalization in the modern world is that there is nowhere to hide. Canada and the U.S. did not lose many jobs to Mexico though they gained some higher value jobs. At the same time, all three countries have probably lost more jobs to China. The fear of cultural domination that one hears in Canada has a similar ring, though in this case, the workers want to be free to consume products from around the world, and a part of the intellectual elite, supported by those magazine and movie producers that seek protection for old-fashioned economic reasons, resist freer trade.

In an age of increasing integration, national governments should make sure that the gains of trade are redistributed to those who lose the competition and that regulations protect their people. Not all do that. Still, the premise of the "North American idea" is that the public of all three countries would be far better off forging rules to deepen integration than to rebuild barriers to trade.

Are the three governments prepared to give up their sovereignty for a wider community? The term "sovereignty" is one of the most widely used, abused, and least understood in the diplomatic lexicon. "Sovereignty" is not a fixed or immutable concept. Three decades ago, Canada interpreted sovereignty to restrict U.S. oil companies from investing in Canada. Mexico used it to ban international election monitors, and the U.S. used it to insist on "states rights" rather than human rights. In each case, sovereignty was used to defend bad policies, and yet changing these policies enhanced the prestige and prosperity of the country. Sovereignty, in brief, is a misleading if not a mistaken defence against an increasingly open and integrated world.

The question is whether the people of the three countries are ready for a different relationship, and public opinion surveys suggest that the answer is affirmative and, indeed, that the people are way ahead of their leaders. A survey of the attitudes of people in the three countries during the past 20 years demonstrates an extraordinary convergence of values – on personal and family issues as well as public policy. Each nation has very positive feelings about their neighbours (although this has changed somewhat since the war in Iraq). In all three countries, the public's views on NAFTA shifted in the 1990s. There is now modest net support, but a neat consensus: each nation agrees that the others benefited more than they have!

The most interesting surveys, however, show that a majority of the public in all three countries is prepared to join a larger North American country if they thought it would improve their standard of living and environment and not threaten their culture. Mexicans and Canadians do not want to be incorporated into the U.S., and they are ambivalent about adopting the U.S. dollar, but they are more willing to become part of a single country of North America and of a unified currency, like the "Amero," proposed by Herbert Grubel (Grubel 1999).[10] The "Amero" would be equivalent of the U.S. dollar, and the two other currencies would be exchanged at the rate in which they are then traded for the U.S. dollar. In other words, at the outset, the wealth of all three countries would be unchanged, and the power to manage the currency would be roughly proportional to the existing wealth. The three governments remain zealous defenders of an aging conception of sovereignty whereas the people seem ready to entertain new approaches.

Other surveys by Ekos of Canada suggest that people in all three countries have begun to think of themselves as part of a larger community. In Europe, instead of renouncing nationhood, Frenchmen and Germans also think of themselves as Europeans. Similarly, 58 per cent of Canadians and 69 per cent of the U.S. public feel a "strong" attachment to North America, and, most surprising, 34 per cent of Mexicans consider themselves "North American," though that term in Spanish has referred to the U.S. alone. The surveys also outline a "North American model" that is quite different from that of the EU. For example, in considering 12 values, people in all three countries gave the highest priority to "freedom" and the lowest to government size and "redistribution of wealth" (Public Policy Forum and EKOS 2002).

The October 2003 survey by Ekos found that a clear majority (56-62 per cent) believe that a North American Economic Union is likely to be established in the next ten years. An overwhelming majority of the public in all three countries favoured more integrated North American – rather than separate – policies on the environment, transportation, and defence, with more modest majorities in favour of common policies on energy and banking. And on the issue of whether to develop a common security perimeter for North America, both Americans and Canadians favoured it by 3:1 and Mexicans by 2:1.

Despite this convergence and a popular desire to experiment, the three governments have devoted so much effort to defining differences that they have not found the time or energy to expand what they have in common. The market has advanced integration; it is time for the political leaders to address its externalities – including currency crises, development gaps, environmental degradation, terrorist threats, and infrastructural impediments. That is the challenge of the North American Commission -- to sketch an alternative future for the entire continent that the people will embrace and the politicians will feel obligated to accept.

NAFTA built an economic foundation under a formidable regional entity. North America needs leaders who can articulate and pursue a broader vision. North America's second decade poses three distinct challenges – one for each country to take the lead. The first is for Canada to take the lead in replacing the dual-bilateralism of the past with rule-based North American institutions. If Canada leads, Mexico will support it, and the U.S. will accept it. The second challenge is for Mexico to demonstrate how it would contribute to and use a North American Investment Fund to double its growth rate and lift its economy. If Mexico and North America succeed, then Latin America would have reason to ride the train toward a Free Trade Area of the Americas, but if we cannot narrow the development gap in North America, then the prospects are bleak for other middle-income countries. The third challenge is for the U.S. to redefine its leadership in the twenty-first century to inspire support rather than resentment, fear, or unease. If the U.S. can adjust its interests to those of its neighbours, the world will look to the U.S. in more positive ways than it has since the invasion of Iraq.

These three challenges constitute an agenda of the greatest consequence for North America in its second decade. Success will not only energize the continent, it will infuse hope throughout the world.

Notes

[1] I wish to express my gratitude to Vassia Gueorguieva for research assistance on this paper.
[2] For two analyses of the issues and the agreement, see Wonnacott 1987 and Schott and Smith 1988. Both were published by the Institute for International Economics in Washington, DC.
[3] This summary of Carlos Salinas's views on trade is derived from numerous interviews that the author had with Salinas from 1979 through 1994 and particularly during the period 1989-92, when his views on NAFTA took shape.
[4] For a description and preliminary analysis of NAFTA, see Pastor 1993; see also Hufbauer and Schott 1993.
[5] For a review of that literature, see Pastor 2001: Chapter 4. For an excellent assessment of the original agreement, see Hufbauer and Schott 1993, Grayson 1995, and Orme 1996.
[6] For a detailed analysis of the electoral systems in the three countries and the ways in which each has and can learn from each other, see Pastor 2004.
[7] For the submissions, see http://www.dol.gov/dol/ilab/public/programmes/nao; also see http://www.naalc.org.
[8] For the more recent estimate, see Ferriss 2001.
[9] The estimates on the gap between northern and southern Mexico vary. Luis Ernesto Derbez, a World Bank economist, who became Mexico's minister of the economy and then of foreign relations, estimated that during the 1990s the export-oriented North grew at annual rates of 5.9 per cent, while the South barely grew at .4 per cent -- more than 10 times faster (cited in Tricks 2001). Tamayo-Flores also concluded that the gap in income between northern and southern Mexico had widened significantly since NAFTA even while the population in the poorer part of Mexico declined *vis-à-vis* the North (2001: 405-07). Based on data from INEGI and CONAPO, the North American Development Bank estimated that the northern part of Mexico was growing more than twice as fast as the south or centre.
[10] An October 2001 survey in Canada found that 55 per cent favoured the same currency as the U.S., but 59 per cent opposed adopting the U.S. dollar (see Dunfield 2001).

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