Insight

Is NAFTA a Bad Deal?

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The North American Free Trade Agreement (NAFTA) has come under fire recently, with some labeling it “a disaster” and claiming that it is the driving force behind the relocation of American firms like Ford Motor Company to Mexico.

This raises the question: is NAFTA a bad deal for the U.S.?

NAFTA went into effect in 1994 to encourage trade and investment between the United States, Canada, and Mexico. It eliminated trade barriers between the countries by lifting all taxes on imports, protecting international property rights, and outlining dispute settlement provisions. The agreement also established the largest free trade area in the world, representing 26 percent of global Gross Domestic Product (GDP).

Although overall trends in global trade growth make it difficult to isolate the direct economic impacts of NAFTA, economists generally agree that the deal was successful in spurring commerce. For instance, total trade between NAFTA partners has quadrupled since 1993 and over one third of all U.S. exports are sold to Canada and Mexico. Exports to our NAFTA partners have also grown at a much faster rate than exports to the rest of the world. In fact, current U.S. trade with our NAFTA partners is roughly equal to U.S. trade with Brazil, Russia, India, China , and South Africa (the BRICS nations), Japan, and Korea combined.

Critics argue that free trade agreements, like NAFTA, harm U.S. companies and workers by making cheaper, foreign-made products more appealing than American-made goods. They cite the trade deficit as evidence that American companies are suffering because U.S. imports from Canada and Mexico exceed exports by $89 trillion . However, the Congressional Research Service found that eliminating tariffs between NAFTA partners has enabled U.S. firms to take a more active role in the production of imported goods. American manufacturers now create approximately 40 percent of the content of Mexican imports and 25 percent of the content of Canadian imports. In addition, trade between the U.S., Canada, and Mexico supports nearly 14 million American jobs, with 5 million created as a direct result of the increased trade generated by NAFTA.

The chart below provides additional evidence that the U.S. has benefited from NAFTA by detailing the trend in U.S. exports to Mexico since the agreement was signed. Apart from recessions, the value of U.S. exports to Mexico has steadily increased since 1994. Even more telling is the rise of U.S. exports to Mexico as a percentage of total U.S. exports. Before NAFTA went into effect, only about 9 percent of U.S. exports went to Mexico. That figure has risen to almost 15 percent showing that concerns over NAFTA’s disproportionate benefits to Mexico, and consequent damage to the U.S., may be misguided.

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The last 20 years of NAFTA have proven to be of great benefit to the U.S. Investment has grown, American business has gained, and trade has increased for all parties involved. While some critics may denounce NAFTA as a handout to Mexico, the evidence here tells a much different story.