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Development and Economic Effect Analysis of Free Trade Area with Axle of Mexico

DEVELOPPEMENT ET ANALYSE DES EFFETS ECONOMIQUES DE LA ZONE DU LIBRE ECHANGE AVEC L' ESSIEU DU MEXIQUE

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Abstract

With the development of the economic globalization and regionalization, Mexico, as the developing country, conducts the marketization and liberalization reforms actively, and gains rapid development in the aspects of regional economic cooperation. In the recent several years, Mexico had entered into free trade agreement with multiple countries and regions, and formed the trade junction connecting Europe, Asia and America. This paper describes the developmental actuality of free trade area with the axle of Mexico, analyzes the developmental strategy of America, Asia and Europe with the axle center of Mexico, and discusses the economic influences of the overlapping free trade area on Mexico by applying the diagram, which mainly reflects in the following aspects. First, it pushes forward the vigorous growth of the value of import and export trade in Mexico and enhances the ability of attracting foreign capitals. Second, it reduces the dependence on the US market. Meanwhile, it also leads to the rising of the administrative cost.

Key words: Overlapping free trade area; Developmental strategy; Rules of origin

Résumé

Avec le développement de la mondialisation économique et de la régionalisation, le Mexique, alors que le pays en développement, mène la marchandisation et de réformes de libéralisation activement, et les gains de développement rapide dans les aspects de la coopération économique régionale. Dans les dernières années de plusieurs, le Mexique avaient conclu un accord de libre échange avec plusieurs pays et régions, et ont formé la jonction de commerce reliant l'Europe, en Asie et en Amérique. Ce document décrit la réalité de développement de la zone de libre-échange avec l'axe du Mexique, analyse la stratégie de développement de l'Amérique, en Asie et en Europe avec le centre de l'essieu du Mexique, et examine les influences économiques de la zone de libre-échange qui se chevauchent sur le Mexique en appliquant le schéma , qui reflète principalement dans les aspects suivants. Premièrement, elle pousse en avant la croissance vigoureuse de la valeur des importations et des exportations au Mexique et en améliore la capacité d'attirer des capitaux étrangers. Deuxièmement, il réduit la dépendance sur le marché américain. En attendant, il conduit également à la hausse des coûts administratifs.

Mots-clés: Chevauchement; Zone de libre-échange; Stratégie de développement; Règles d'origine

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After 1980s, Mexico conducts the marketization and liberalization actively, on the one hand, positively participating in the multilateral trade organization, on the other hand, starting to build free trade area with other countries. Mexico joined in GATT in 1986, entered into North American Free Trade Agreement with Canada and US at the end of 1992, and joined in APEC in 1993. North American Free Trade Area was formally established on January 1, 1994. Hereafter, Mexico has gained rapid development in the aspects of regional economic cooperation.

1. DEVELOPMENT ACTUALITY OF FREE TRADE AREA IN MEXICO

In 1992 the bilateral free trade agreement signed between Mexico and Chile began to come into effect. In 1995 Mexico built G3 with Venezuela and Columbia. In 2004 the free trade agreement signed between Mexico and Uruguay began to come into effect. As of 2008, Mexico had entered into free trade agreement with 39 countries and regions worldwide involving the largest economic entity as EU and Japan, which became the country with entering into the most free trade agreements all over the world. At present Mexico has formed the free trade area network involving in Europe, Asia and America in the world, which became the country of entering into free trade agreements with the largest number all over the world. According to the concept of overlapping free trade agreement, Mexico had entered into different free trade agreements with multiple countries and regions, which became the axle country. Thus, Mexico possessed the location strategic advantage in the global economic system. First, it became the business bridge between North America and Central America through entering into the trade agreement with the countries in America. Next, it became the economic connecting ligament between America and Europe through entering into the agreement with EU. Last, it accessed to the Asian market through entering into the trade agreement with Japan. Mexico became the axle country by this extensive free trade agreement and possessed the superiority of the axle country. Mexico was in the advantageous position in the world economy and gained larger profits in attracting investment and international trade through enjoying numerous preferential treatment of free trade agreement. Therefore, Mexico set up the trade bridge of America, Europe and Asia and became the important junction of world trade.

Table 1
Free Trade Agreement Signed by Mexico

Free Trade Agreement	Signing Date	Effective Date
North American Free Trade Agreement	August 1992	January 1, 1995
G3	September 1990	
Mexico—Bolivia	October 1994	January 1, 1995
Mexico—Chile	October 1998	January 1, 1995
Mexico--- Costa Rica	April 1994	August 1, 1999
Mexico—EFTA	November 2000	January 1, 1995 July 1, 2001
Mexico—EU	February 1995	October 1, 2001 (Iceland)
Mexico—Israel	April 2000	July 1, 2000
Mexico ---Nicaragua	August 1992	July 1, 2000
Mexico---Northem Triangle	June 2000	July 1, 1998 March 15, 2001 (Guatemala, Salvador) June 1, 2001 (Honduras)
Mexico—Uruguay	November 2003	July 15, 2004
Mexico ---Japan	September 2004	April 1, 2005

Source of Data: SICE-OAS Databas

2. DEVELOPMENTAL STRATEGY OF FREE TRADE AREA WITH AXLE OF MEXICO

2.1 Development of Regional Economic Integration for the Western Hemisphere in Mexico

Mexico built free trade area with US and Canada, which was an important step of promoting the economic integration in the Western Hemisphere as well as the primary strategy for Mexico to open to the outside world. Article I in *North American Free Trade Agreement* explicitly formulates that US, Mexico and Canada formally build a free trade area in accordance with the basic principle of General Agreement on Tariffs and Trade. The tenet is to cancel the trade barriers, create the conditions of fair competition, increase the investment chances, provide the appropriate protection for the intellectual property, and establish the effective procedures of executing the agreement and solving the dispute. The agreement mainly contains the following contents from 10 aspects, including market access, textile and clothes, automobile products, energy and basic petrochemicals, agricultural products, rules of origin, land transportation, investment, financial services and dispute settlement mechanism. Because Mexico is the developing country, the agreement stipulates for giving a certain privilege to Mexico. In order to promote the economic integration of Central America, Fox, the president of Mexico, firstly proposed the idea of Puebla-Panama Plan in March 2001, which propelled 98 investment and cooperation projects and drove the progress for the economic integration of Central America. In order to promote the economic integration of countries in South America, Mexico entered into free trade agreement with Chile in 1992, and built

G3 with Venezuela and Columbia in 1995. The free trade agreement of G3 mainly includes market access, rules of origin, investment, government procurement, service trade, intellectual property, and trade dispute solution etc. Firstly, in the aspect of market access, the three countries would reduce or even exempt the tariff within the period of 10 years to realize the free flow of the commodities in the free trade zone. Secondly, in order to coordinate the trade contradictions of the agricultural and chemical products and textile, the agreement stipulated that all the agricultural products with governmental subsidy were not included in the scope of the agreement, and the textile and petrochemicals would be also treated separatly. Finally, the tariff of the automobile products would reduce gradually two years after the agreement was signed, and it shall be reduced to zero within 10 years. But on 19th Nov, 2006, because Venezuela was not content with the free trade agreement signed between Colombia and America, Venezuela withdrew from the G3.

2.2 Development of the Mexican— European Free Trade Agreement

The origin for the European-Mexican Free Trade Agreement can be traced back to the mid 1990's. On 2nd May, 1995, both European Union and Mexico announced that in order to further develop the bilateral relations between the two counties, the two parties would promote political dialogue and pave the way for the establishment of the free trade zone. On 8th Dec, 1997, the two parties signed the *Economic Partners, Political Coordination and Cooperation Agreement* as well as the *Provisional Agreement on Trade and Trade Related Problems*. On the basis of these agreements, the free trade negotiation between European Union and Mexico officially began on 14th Jul, 1998. Through the negotiations of three rounds, the two parties finally reached an agreement on 24th Nov, 1999. On 23rd March, 2000 the signing ceremony for the European Union-Mexican Free Trade Agreement was held in Lisbon. And this agreement has two prominent characteristics: Firstly, Mexico is the only country in the world that has reached the free trade agreement with two developed economic areas as North America and European Union. Secondly, this is not only a free trade agreement reached by the European Union with other countries outside the Europe that possess the most widest market coverage, but also the first free trade agreement reached by the European Union with Latin American countries.

The European-Mexican Free Trade Agreement almost referred to every aspect of the bilateral economic and trade relations. For example, this agreement was not only related to the general products and service industry trade, but also made certain stipulations in the aspects of investment, governmental purchase, intellectual property protection etc. Moreover, the agreement also established the mechanism to solve the disputes. And the ratio of the industrial products in the bilateral trade of the European and Mexico has reached 92.8%. According to this agreement, Mexico would provide the same treatment for the industrial products of the EU members which was enjoyed by America and Canada in the Mexican market. By 1st Jan, 2003, 52% of the industrial products exported from EU to Mexico would not be limited by tariff, and for the tariff of other parts, it would decrease from the 35% of that time to the maximum of no surpass 5%. For example, since the agreement has taken into effect on 1st Jul, 2000, the automobile tariff charged by Mexico to EU would decrease from 20% of that time to 3%, and in 2003 it shall be zero. By the year of 2007, the industrial products exported from EU to Mexico would enjoy the duty-free policy. While the export from Mexico to EU would enjoy the tax-free privilege in 2003. Wherein, the agricultural products had only taken about 7% in the bilateral trade between EU and Mexico. According to the Free Trade Agreement, 62% of the bilateral agricultural products trade will realize the liberalization. The concentrated orange juice, fresh flowers and avocados as well as other products can enter into the EU market freely, but to several comparative sensitive agricultural products in the EU member countries (such as meat, milk products and grain, there are beyond the stipulations of the Free Trade Agreement. According to the Agreement, EU and Mexico will gradually realize the free trade among the energy and finance, telecom, sales, travel, environment and other service industry departments within the period of the following ten years, but the sound and image products service industry, sea transportation and airport are not included. And the most conspicuous point is— the banks and insurance companies of the EU member countries will enjoy the same treatment as the America and Canada in the Mexico market.

Since Mexico has established the North- American Free Trade Zone with America and Canada, the economic mutual dependence degree among the three countries has constantly improved, and still Mexico has gained a lot of trade and investment interests from it. But, on the same time, there are frequent trade frictions between Mexico and America, thus it makes Mexico begin to realize that relying too much on the American market do harm to the multiple development of its economic relations with foreign countries. Thus, Mexico hopes that its free trade with the EU will reduce its dependence on the American market. In addition, the EU market with the population of 0.375 billion will play a more and more important role in the global economy, and Mexico, as the top ten export countries in the world cannot neglect the great potential of the EU market. More importantly, the EU is willing to reach an agreement with Mexico, partly because it wants to compete with America and Canada in Mexican market, partly because it hopes to use the "Springboard" function of Mexico to enter the American and Canadian large markets, and finally lay foundation for its possession on the American market. And more importantly, to promote the multiple development for the North–South cooperation under the background of economic globalization.

2.3 Free Trade Strategy of Mexico in Asia

Mexico signed a free trade agreement with Japan on March 12, 2004 which was the beginning of Asia strategy of Mexico. The signing of free trade agreement between Japan and Mexico is of great significance to both countries and beneficial to global economic development. Japan hopes that trade cooperation with Mexico will strengthen and restore competitiveness of Japanese enterprises in international market. Main export products of Japan to Mexico include electronic equipment and components, automobile and auto parts as well as steel products. According to the provisions of the agreement, over 300 kinds of agricultural products will receive preferential tariff treatment. Based on the preferential tariff treatment, Mexico will export 80 thousand tons of pork and 6500 tons of orange juice to Japan each year. Mexico Ministry of Economy expressed that within 10 years from the date of signing the free trade agreement, the annual investment of Japan to Mexico will reach 1.3 billion dollars. Japan will become important export market of Mexico agricultural products and invest a large sum of money in Mexico. Mexico is the second country that has signed free trade agreement with Japan after the free trade agreement signed between Singapore and Japan took effect in 2002 and it is the first time to sign comprehensive free trade agreement including agricultural products. After reaching free trade agreement, Japan and Mexico will mutually reduce import duties of a series of products including commercial vehicle. As a result, the export of Japanese automobile to Mexico will increase substantially. Japan Business Federation expressed that after signing free trade agreement, Japanese automobile manufacturers can be exempt from average 16% import duty on automobile and other manufactured goods, thus enhancing the competitiveness of Japanese manufacturing industry over counterparts in the United States and Europe. YoshihideMunekuni, Chairman of Japan Automobile Manufacturers Association, expressed that for Japanese automobile manufacturing industry, the free trade agreement to be reached between two countries was the chip of Japanese automobile for entering Mexican market. Japanese automobile manufacturers hope that the government can accelerate the free trade negotiation process with Thailand, Malaysia, Philippine and Korea. To further strengthen cooperation with Asia and fully occupy Asian market, Mexico has gradually focused on the emerging markets in developing countries and plans to build free trade area with China. On the one hand, it can cope with the situation that a large number of Chinese commodities are exported to the United States and Canada; on the other hand, it can enter Chinese market and expand export of commodities to Asia.

Up to the present, Mexico has established extensive free trade agreement all over the world and extended to Europe, America, Asia etc.. Mexico Free Trade Agreement is typical overlapping free trade agreement. Mexico is typical overlapped free trade agreement. Mexico is hub country and other countries are spoke countries. According to changes in volume of import and export trade, Mexico has gained many benefits from such regional agreement, but in 2003, Mexican president expressed that Mexico had signed too many regional agreements and its export capability cannot take full advantage of preferential treatment given by free trade area; on the contrary, import volume of partners increased substantially, thus greatly increasing trade deficit of Mexico and seriously unbalancing international trade.

3. ECONOMIC IMPACT OF MEXICO FREE TRADE AREA ON MEXICO

3.1 Volume of Import and Export Trade of Mexico is Growing Rapidly

Relying on advantageous position of hub country, spoke countries will firstly enter markets of other spoke countries through Mexico and then enjoy regional preferential treatment. Moreover, hub country has demonstration effect. Many countries that haven't established free trade agreement with Mexico often choose to sign free trade agreement with hub country to reduce negotiation cost for signing free trade agreement with foreign parties and enjoy preferential market of larger field at the same time. This is also an important reason for rapid growth of volume of import and export trade of Mexico. For example, in 1999, Mexico hadn't signed free trade agreement with European Union. The average tariff for importing products from the European Union was 8.9% which was only 1.8% for importing products from the United States. Therefore, between 1990 and 1997, the export of the European Union to Mexico was reduced from 13.3% to 3.6% and the import from Mexico was reduced from 17.4% to 9%. Correspondingly, the export of the United States to Mexico was increased from 69.3% to 85.6% and the import was also increased from 66.1% to 74% (LI, GUO, 2007). In order to grasp Mexican market, the European Union signed free trade agreement with Mexico. So does Japan. Before signing free trade agreement with Mexico, 16% tariff should be levied for entering Mexican market and after signing free trade agreement, Japanese enterprises can save over 400 billion yen cost each year.

In addition, according to Mexican Economist Newspaper on March 31, 2010, recently, Minister of Economic Affairs of Mexico-Ruiz announced that the favorable balance of trade between Mexico and its free trade partners was 49 billion dollars in 2009. But, the unfavorable balance between Mexico and the non free trade partners reached 54 billion dollars in the corresponding period. In the first half of 2010, the total import & export trade volume was 286.6 billion dollars, which ranked No. 15 in the world and increased by 35% comparing with the same period of 2009. And the export proportion was 49.3%.[2] Visibly, the rapidly-increasing import & export of Mexico was benefit from the position of axle countries. In recent years, the total import & export volume of Mexico to the world has shown that its trade is rapidly growing.

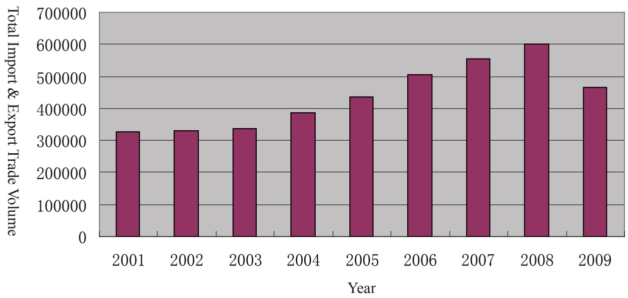

Figure 1
Data Source: Discriminatory Trade Report of Ministry of Commerce of the People's Republic of China, http://www.mofcom.gov.cn/

3.2 The Ability to Attract Foreign Investments of Mexico is Substantially Improving

After Mexico establishing the free trade area in the United States and Canada, its investment environment is greatly improved, as well as the marketization. In addition, Mexico has lower factor cost and many advantages & conveniences of entering into the axle countries. In order to bypass the restriction of strict origin rules of North American Free Trade Area, outside countries and areas invest to and establish factories in Mexico in succession. Therefore, Mexico not only attracts the investment of the United States and Canada, but also a large number of foreign investments. It should be said that the overlapping free trade area improves the ability to attract foreign investments of Mexico and provides a greater power for the development of Mexico.

In the 1970s, FDI average introduction of Mexico was 0.8%. Especially, entered into NAFT in 1994, the proportion of FDI absorption inflow absorbed by Mexico had always maintained over 5% among the developing countries, which maximally reached 12.1% in 2001. In the corresponding period, the proportion of FDI absorption inflow absorbed by Mexico also kept over 2% among the world FDI absorption inflow, which reached 3.4% in 2001(HE, 2009). The table below is the amount of introducing foreign investment of Mexico in the past ten years.

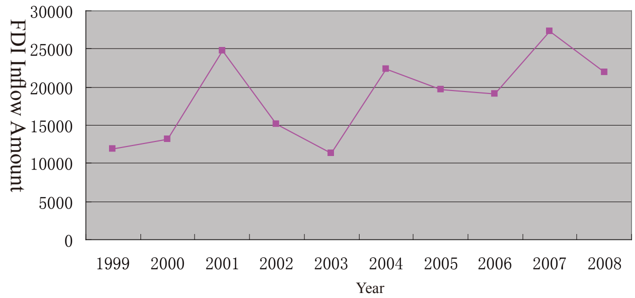

Figure 2
Data Source: UNCTAD FDI Database

3.3 The Overlapping Free Trade Agreement Decreases the Dependence of Mexican Economy on the United States

Mexican economy has tied very closely with the Unites States. Especially, after the establishment of North American Free Trade Agreement, most of trades are taken within the area almost. In 1999, Mexican export volume to the United State occupied 88.2% among the total export volume, which was increased by 31.2% comparing with the export volume of the second country-Bahamas among Latin American Countries exported to the United States, and was twice as the average proportion of Latin America exported to the United States that year. The United States is the largest FDI source of Mexico. Basically, 2/3 FDI comes from the United States; 90% Mexican commodities are exported to the United States, and 60% import commodities comes from the United States. But, in recent years, because Mexico has signed the free trade agreement with many countries, the dependence of Mexico on the United States market has became weaker gradually.

Table 2
Bilateral Trade Volume Between Mexico and the United States (Unit: Million Dollars)

Time (Year)	Total Export Volume of Mexico	Export Volume to the United States	Export Volume to the United States/Mexico Total Export Volume
2005	214233	170198	0.79
2006	249997	198259	0.793
2007	271958	210714	0.774
2008	292666	215915	0.737

Data Source: The data of total export volume, export volume to the United States and the export volume to the United States / Mexico export volume come from Discriminatory Trade Report of Ministry of Commerce of the People's Republic of China, http://www.mofcom.gov.cn/.

According to the calculated data of Export Volume to the Unites States / Mexican Export Volume from 2005 to 2008 in the above table, the proportion of the United States Export ranking Mexican Total Export Volume is diminishing. Although the changes are not large, the change trend is gradually reducing, which shows that the dependence of Mexico on the United Sates market is decreasing.

3.4 The Origin Rules Cause the Management Cost Rising of Mexico Overlapping Free Trade Agreement

The overlapping trade agreement can bring privileges to the member countries. Meanwhile, it can cause the changes of origin rules that the trade protective function is increased from the determination of origin rules. The overlapping free trade area signed by Mexico makes the origin rules have the function of protecting area economic interests. And it follows the origin rules of North American Free Trade Area basically, with the relatively-high restriction. How many free trade agreements signed by Mexico? There are how many sets of origin rules, which cause that the customs increases the management cost of origin rules.

The multiple free trade agreements signed by Mexico make the domestic products confront with many preferential markets. If the commodities are exported to this market, it will diversify the export of Mexico. With the diversified strategy of export market, the management cost will increase correspondingly, which will counteract the benefits brought by the free trade agreement tariff preference. And the export market diversification also can cause the decentralization of exported products of Mexico. For example, the exported agriculture raw material of Mexico took up 0.4%, 15.7% of foods, 2.7% of minerals and 71.7% of finished-products in 2007. Comparing to the past years, the proportion of raw material and primary commodities is less and less, while the proportion of finished-products is higher and higher.

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