Lorraine Eden and Maureen Appel Molot
Norman Paterson School of International Affairs
Carleton University

8

The View from the Spokes: Canada and Mexico Face the United States[1]

INTRODUCTION

The phrase "hub-and-spoke" has been used by economists to characterize the possibility of a series of bilateral free trade arrangements negotiated between the United States (the hub) and a number of its trading partners (the spokes).[2] Rather than anticipating a hub-and-spoke relationship as a potential negotiated outcome, it is the contention of this paper that a hub-and-spoke relationship already exists in North America between Canada and the United States, on the one hand, and between Mexico and the United States, on the other, reflecting the underlying structures of production, trade, and investment patterns among the three economies. The northern hub-and-spoke relationship has recently been institutionalized under the 1989 Canada-United States Free Trade Agreement (PTA). In 1990, Mexico and the United States began discussions on formalizing the southern hub-and-spoke link-discussions which Canada subsequently decided to join. Mexico, the United States, and Canada initiated formal

1 This paper is part of a wider project on the political economy of North American free trade being conducted under the sponsorship of the Centre for International Trade and Investment Policy Studies and the Centre for Trade Policy and Law at Carleton University. We also acknowledge the financial assistance of the Social Sciences and Humanities Research Council of Canada and of Carleton University on this project. Research assistance was provided by Jeremy Byatt and Susan Olsen. We would also like to thank Maxwell Cameron, Richard Lipsey, and Bruce Wilkinson for helpful comments.

2 Richard Lipsey, "Growth, Erosion and Restructuring of the Multilateral Trading System," (a paper delivered at the annual meetings of the American Economics Association, Atlanta, Georgia, December 1989). Ronald J. Wonnacott, *U.S. Hub and Spoke Bilaterals and the Multilateral Trading System,* Commentary No. 23 (Toronto: C.D. Howe Institute, October 1990).

talks in June 1991 to negotiate a North American Free Trade Agreement (NAFrA).

The purpose of this paper is to examine similarities and differences in the Canadian and Mexican approaches to free trade with the United States. Through an examination of existing intra-North American trade and investment linkages, the paper first documents why we believe a hub-and-spoke relationship is already present. The reasons why Canada opted for a Canada-United States FTA are discussed and contrasted with its reasons for participating in the NAFrA talks. The paper then focuses on the reasons why Mexico decided to embark on free trade negotiations, first with the United States, and then through NAFTA discussions. The last section of the paper addresses the view from the spokes as both contemplate the transformation of the existing dyadic relationships into a continental free trade bloc. The paper concludes that a *NAFTA* is likely to deepen prevailing trade and investment patterns.

DOCUMENTING THE HUB-AND-SPOKE RELATIONSHIPS

The Trade Hub and Spokes

Intraregional North American trade presently accounts for approximately thirty-six per cent of the combined total of the trade of the United States, Canada, and Mexico.[3] The trade linkages can be envisioned as a triangle in which the intensity of linkages among the three parties varies in strength. Table 1 shows these linkages, focusing on import penetration.

The triangular trade among the three North American countries is quite unbalanced. In 1987, the United States sold eighteen per cent of its total exports to Canada and six per cent to Mexico and obtained eighteen per cent of its total imports from Canada and five per cent from Mexico. Canada sold seventy-six per cent of its exports to the United States but negligible amounts to Mexico, and received sixty-six per cent of its imports from the United States with similar negligible imports from Mexico. Therefore the United States-Canada trade link is much more intense than either of the two other sides of the triangle. For both Canada and Mexico, the United States is the major trading partner, absorbing some seventy-five per cent of Canadian exports and sixty-seven per cent of Mexican exports in recent years. What is particularly noteworthy is the rapid growth in Mexican manufactured exports to the United States. Until the early 1980s, petroleum was the major Mexican export to the United States;

3 House of Commons, Standing Committee on External Affairs and International Trade (SCEAin, *Hearings on Canada-U.S.-Mexico Trade Negotiations*, 68 (1990), pp. 35-36.

TABLE 1. INTRA-NORTH AMERICAN TRADE (1988)

	U.S.$ Billion[a]	Import Penetration[b]	Export Orientation[c]
Canada to U.S.A.	79.3	17.3	71.2
U.S.A. to Canada	69.9	62.3	22.2
Mexico to U.S.A.	23.3	5.0	n.a.
U.S.A. to Mexico	20.6	n.a.	6.5
Mexico to Canada	1.1	1.0	5.6
Canada to Mexico	0.4	2.0	0.4

a Excludes U.S.$2.1 billion added from *maqulladora* output.
b Per cent of total imports.
c Per cent of total exports.

since 1985, manufactured goods have constituted the largest export category, with eighty-five per cent of Mexico's manufactures now destined for the U.S. market! Nearly half of these manufactured goods are produced in the *maquiladoras-firms* located in export processing zones set up to attract foreign direct investment (FOi) and encourage local assembly by taking advantage of low Mexican wage rates and reduced taxes.

Canada and Mexico trade very little with each other. Two-way trade in 1989 amounted to some U.S.$2.3 billion, although transshipments through the United States probably understate these statistics.[5] Canada ranks sixth amongst Mexico's trading partners and Mexico ranks seventeenth among the states with which Canada trades. In recent years, Mexico has consistently had a trade surplus with Canada. Moreover, Mexico exports a higher percentage of fully manufactured goods to Canada (69 per cent of exports) than Canada does to Mexico (24 per cent). In 1990, the trade balance in Mexico's favour increased as Canadian exports to Mexico fell by 4.2 per cent.[6]

4 Sidney Weintraub, "The Impact of the Agreement on Mexico." In *Making Free Trade Work*, ed. Peter Morici (New York: Council on Foreign Relations, 1990), p.106.

5 Michael Hart, *A North American Free Trade Agreement: The Strategic Implications for Canada* (Halifax: Institute for Research on Public Policy, 1990), p. 7.

6 "Trade Imbalance with Mexico Grows," *Ottawa Citizen* (20 February 1991): p. E3.

TABLE 2. INTRA-NORTH AMERICAN INVr5TMENT (1984).
FLOW OF FOREIGN DIRECT INVF.STMENT

	U.S.$ Billion	Import Penetration[3]	Export Orientation[b]
Canada to U.S.A.	22.8	14.3	35.6
U.S.A. to Canada	49.5	77.2	21.8
Mexico to U.S.A.	0.3	0.002	n.a.
U.S.A. to Mexico	5.0	n.a.	2.2
Mexico to Canada	0.002	0.002	n.a.
Canada to Mexico	0.2	n.a.	0.6

a Per cent of total inward FDI.
b Per cent of total outward FDI.

A brief look at the relevant U.S. statistics reveals the differential intensity of its North American trading links. Canadian and Mexican exports to the United States account for eighteen per cent and five per cent, respectively, of U.S. imports. The United States sells approximately twenty-four per cent of its exports to Canada and six per cent to Mexico. In 1988, the growth of U.S. imports from both Canada and Mexico outpaced the growth rate of U.S. imports from other sources. Canada remains the United States' largest trading partner, while Mexico now ranks third, after Canada and Japan.

The Investment Hub and Spokes

Table 2 provides a picture of the triangular FDI patterns among the three economies using statistics which are from 1984 FDI flows. What is striking about Table 2 is its similarity to Table 1; while the dollar amounts are smaller, their relative size is the same. The importance of the United States as a foreign investor in both the Canadian and Mexican economies is obvious.7

7 Lorraine Eden, "Multinational Responses to Trade and Technology Changes: Implications for Canada." In *Foreign Investment, Technology and Economic Growth,* ed. Don Mcfetridge (Calgary: University of Calgary Press, 1991), pp. 133-72. Lorraine Eden and Maureen Appel Molot, "From Silent Integration to Strategic Alliance: The Political Economy of North American Free Trade," (a

The United States invested U.S.$49.5 billion in Canada in 1984, which represented 21.8 per cent of U.S. FOi outflows and 77.2 per cent of Canadian FDI inflows. U.S. levels of FOi in Canada as well as U.S. ownership of Canadian industry have declined in recent years, although Canada continues to have a higher percentage of its economy controlled by foreign investors than any other OECD country.[8] The U.S. share of the total FDI stock in Canada was 75.6 per cent in 1985, representing 20.5 per cent of U.S. outward FDI stock. This compared to a Canadian ownership of 9.3 per cent of U.S. inward FOi stock, or 71.2 per cent of Canadian outward FDI stock.[9]

U.S. direct investments in Mexico in 1984 were U.S.$5 billion, representing 2.2 per cent of U.S. FOi outflows. U.S. investment in Mexico represents about 63 per cent of the total FOi in Mexico. The establishment of *maquiladoras* in 1965 marked the initial opening of the Mexican economy to FDI. U.S. tariff regulations Nos. 806 and 807 levied duties only on the difference between the value of goods imported from Mexico net of U.S. inputs. Thus, U.S. multinational enterprises (MNEs) were directly encouraged to set up offshore factories in Mexico and shift subassembly functions to these Mexican plants. Given increasing competition from European and Japanese MNEs, U.S. multinationals have made heavy use of *maquiladora* factories as a cost-driven method of responding to foreign competition.[10]

Compared to the level of U.S. investment in Mexico, historically, Canadian FOi in Mexico has been limited; it currently stands at about U.S.$400 million. This figure represents 1.4 per cent of total FOi in Mexico and places Canada seventeenth among countries with investments in Mexico. In 1989, there were 214 companies in Mexico in which Canadians had investments. Canadian investment in Mexico has been primarily in the extractive industries, but in the last few years there has been some FOi in manufacturing as Canadian firms have either established joint ventures with Mexican firms or moved production to Mexico. In contrast to the huge numbers of U.S.-owned *maquila* firms stands the less than a dozen such Canadian-owned companies, primarily in the auto parts in-

paper presented at the annual meetings of the International Studies Association, Vancouver, B.C., 22-24 March 1991).

8 Glen Williams, "Regions within Regions: Canada in the Continent." In *Canadian Politics in the 1990s,* 3d ed., ed. Michael Whittington and Glen Williams (Toronto: Nelson Canada, 1990).

9 Alan Rugman and Alain Verbeke, "Canadian Business in a Global Trading Environment," *Research in Global Business Management,* Vol. 1 (New York: JAi Press, 1990), pp. 3-25.

10 Weintraub, "The Impact of the Agreement."

dustry. Mexico has traditionally had far more stringent restrictions on FDI than Canada and many of these continue. However, during the 1980s, both countries reduced their foreign investment regulations.

The foregoing discussion illustrates our contention that a pair of hub-and-spoke relationships currently exist in North America, relationships that predate any negotiations for bilateral or trilateral free trade arrangements. The impetus for the close connections has been in large part market-driven, facilitated by state policies which have encouraged bilateral trade and investment between the United States and its two neighbours.

THE VIEW FROM THE NORTHERN SPOKE

Pressures for a Canada-United States Free Trade Agreement

Canada's decision to seek a free trade agreement with the United States prompted enormous domestic debate over the wisdom of establishing formal trade links with its major trading partner. The reasons for the choice lay in Canadian trade dependence on the United States and fears of mounting U.S. protectionism. Free trade would mean secure market access as well as enhanced export opportunities for Canadian producers. It was hoped that a negotiated agreement would also protect Canadian producers from the crossfire of U.S. policies designed to level the international playing field by raising non-tariff barriers against European and Japanese imports. Moreover, the so-called fresh winds of competition were expected to improve Canadian competitiveness. The formalization of the hub-and-spoke link would also create a trade diversionary impact against foreign firms, thereby attracting investment inflows to Canada from firms anxious to preserve and enlarge their North American market access.

Canadian business for the most part supported the Conservatives' initiative. The executives of Canada's 150 largest corporations, including prominent U.S. subsidiaries, pressed for free trade long before either government was committed to the idea.[11] Also strongly in favour of a Canada-United States FTA were the provinces of Alberta and Quebec. Once the federal government opted for free trade, the Canadian Manufacturers' Association, the representative association for smaller Canadian manufacturers which had historically opposed free trade, joined those in favour of an agreement. Manufacturers who opposed the Canada-United States FTA were those in industries dependent on protection-for exam-

11 Duncan Cameron, ed., *The Free Trade Papers* (Toronto: James Lorimer, 1986), p.xv.

pie, furniture, some textile and clothing, and food processing firms. Canadian labour strongly opposed the Canada-United States FfA on grounds of lost employment as a result of MNE rationalization and the threat that such an agreement posed for the security of Canadian social policies.

Almost three years into the agreement (operative January 1989), there continues to be uncertainty about whether Canada has benefitted. Studies suggest different interpretations.[12] Labour points to more than 200,000 job losses since the agreement was signed, arguing that the Canada-United States FfA is responsible. The Royal Bank of Canada disputes this negative assessment, arguing that taxes, the recession, and interest rates, and not free trade, account for the loss of manufacturing jobs; in the Bank's view it is far too early to judge the impact of the Canada-United States FfA.[13] The Canadian government is more than satisfied with the Canada-United States FfA, maintaining that the recession would have been worse without it.[14] A U.S. customs report argues that two years of free trade have increased U.S. exports more than Canada's.[15] These differing interpretations partly account for the reluctance of government, the public, and business to contemplate a NAFfA.

Pressures for the NAFTA: The Canadian View

There are fewer societal and state pressures promoting Canadian participation in NAFfA talks than was the case in the Canada-United States negotiations. The government, which vacillated for some time before deciding to request a seat at the table, recognized that it had to be a party to discussions which will shape the trade and investment rules in North America. Given its trade dependence on the United States, Canada cannot risk diluting any of the advantages it has gained through the Canada-United States FfA.

Already in the midst of adjusting to the Canada-United States FfA, Canada will face a second round of adjustment with a new, low-cost Mexican partner. Although the two spokes did increase their formal economic contacts at the end of the 1980s, Canada neither wanted nor

---

12 Eden, "Multinational Responses to Trade."

13 "'No Clear Proof Yet' Free Trade Costs Jobs," *Globe and Mail* (6 February 1991): p. B13.

14 "Wilson Defends Free Trade Deal," *Globe and Mail* (19 August 1991): p. 5.

15 This statement was made in testimony to the Senate Finance Committee, 20 February 1991. The explanation offered by the official was that "U.S. merchandise generally [was) less expensive than similar Canadian goods," *Financial Post* (21 February 1991): p. 6.

encouraged Mexico to approach the United States to open trade talks. Canada's purpose at the table is more to protect its own interests in U.S. markets (i.e., defensive) than the more positive, engineering of competitive advantage. While a NA.FfA may improve Canadian competitiveness, this is not the major purpose behind Canadian interest in a NAFTA. Indeed, Canada may have misjudged the consonance of its desire for freer trade with those of the United States: Canada clearly focused solely on the Canada-United States FfA and appeared rather surprised by the quick U.S. move to consider other bilateral agreements. Recognition of the potential costs of a series of U.S. hub-and-spoke arrangements brought Canada to the NAFfA table.[16]

That Canadian business is more ambivalent about a NAFI'A is not surprising, given the limited character of Canada-Mexico trade and the pressures of adjustment to the Canada-United States FfA. There is considerable concern about competition with Mexican goods for the U.S. market. Nonetheless, Canadian multinationals, the Chamber of Commerce, the Canadian Manufacturers' Association, and the Automotive Parts Manufacturers' Association of Canada all believe that Canada cannot permit others to determine the North American trade regime; in their view, Canada must participate in the NAFTA negotiations.17 Firms and industries already finding adjustment to the Canada-United States FfA difficult, such as the furniture, shoe, and garment industries, are concerned about another trade agreement. Canadian labour cites job losses from the Canada-United States FfA and, like its U.S. counterpart,

16 For further material on this matter, see Lorraine Eden, "Multinational Responses to Trade"; Lorraine Eden and Maureen Appel Molot, "From Silent Integration to Strategic Alliance"; Maureen Molot, "Why We Need More Answers," *Policy Options* 12, No. 3 (April 1991); Ronald J. Wonnacott, *Canada and the U.S.-Mexico Free Trade Negotiations,* Commentary No. 21 (foronto: C.D. Howe Institute, September 1990); and Wonnacott, *U.S. Hub and Spoke Bilaterals.*

17 In testimony on Canada-United States trade negotiations before the House of Commons Standing Committee on External Affairs and International Trade (SCEAin, Laurent Thibault, then president of the Canadian Manufacturers' Association (CMA), noted, in comments on a survey done of CMA members' opinions on the NAFfA, that forty-six per cent viewed trade liberalization with Mexico as an opportunity and about twenty-nine per cent viewed it as a threat. Of the latter, which numbered ninety-five companies, seventy five still felt that Canada should participate in the trade talks. On the general question of whether Canada should participate in NAFfA talks to promote its trade and investment interest, eighty-eight per cent of CMA members favoured Canadian participation. Mr. Thibault also noted that the survey revealed a lack of Canadian familiarity with Mexico, a fact that is not surprising given the low level of economic ties between the two countries (SCEAIT 59 [1990], pp. 23-24).

fears that a NAFTA, which would generate competition with lower-paid Mexican workers, will simply exacerbate this.18

These mixed views are reflected in a February 1991 opinion survey which found that forty-six per cent of Canadians supported a NAFTA, fifty per cent opposed it, and the remainder were unsure. Opposition is strongest in the province of Ontario were sixty per cent were against the initiative and thirty-six per cent were in favour.[19] Among provincial governments, the line-up is largely similar to what it was on the Canada-United States FTA: Quebec, Alberta, Saskatchewan, and the Atlantic provinces favour participation in the NAFTA talks; Ontario is strongly opposed to a trilateral arrangement; and Manitoba and British Columbia are undecided.

THE VIEW FROM THE SOUTHERN SPOKE

Pressures for a Mexico-United States Free Trade Agreement

In June 1990, Mexican President Carlos Salinas de Gortari and U.S. President George Bush began joint talks on a Mexico-United States Free Trade Agreement (MUSFTA). A MUSFTA would formalize the southern hub-and-spoke relationship which had been intensifying as the result of a series of policies adopted to promote economic growth in Mexico by liberalizing trade restrictions and opening the economy to international commerce. Among these policies were tariff reductions, Mexico's accession to the General Agreement on Tariffs and Trade (GATI) in 1986, the loosening of investment restrictions, and the sale of a number of state-owned enterprises. In less than a decade, Mexico has dramatically altered its economic philosophy from one based on import-substitution industrialization to one of economic openness through export-oriented growth.

There were several motives for Mexico's desire for a MUSFTA. First, a free trade agreement would continue and solidify these domestic reforms. Most large corporations, and many smaller ones, had already accommodated themselves to the more open trading environment that

18 In testimony before the House of Commons Standing Committee on External Affairs and International Trade (SCEAm, the Canadian Labour Congress listed some thirty-six companies, including General Motors, Ford, General Electric, Northern Telecom, Black and Decker, Campbell Soup, Motorola, and IBM, which have closed facilities in Canada. While, the representative argued, it is impossible to trace plant closures and layoffs in Canada to job creation in Mexico, all of the above-named firms have invested heavily in the *maquiladoras* (SCEAIT 59 [1990), p. 6).

19 *Ottawa Citizen* (26 February 1991): p. B3.

resulted from Mexico's GAIT membership; for them, a MUSFTA would ensure the continued outward-looking nature of the Mexican economy.

Second, a MUSFfA would secure and enhance access to the U.S. market. As trade dependence on the U.S. market deepened and Mexican firms became more competitive in sectors such as steel and textiles, the number of U.S. antidumping and countervailing actions increased. Between 1980 and 1986, Mexico was involved in twenty-six countervailing duty investigations, nineteen of which resulted in some kind of restrictive action.[20] Mexico believed that institutionalization of the hub-and-spoke relationship with a formalized dispute-settlement mechanism would help prevent U.S. aggressive unilateralism. In addition, Mexican firms would be protected from U.S. actions against Asian exporters that have caught Mexico in the crossfire, the same protection Canadian firms received under the Canada-United States FfA.

Third, the signing of the Canada-United States FfA meant that Mexican exporters (except *maquiladora* exports) would face a disadvantage relative to Canada in accessing the U.S. market once the agreement was completely phased in. Canada went into the Canada-United States *FTA* to protect its access to its largest market; however, in doing so, Canadian entry diverted trade from Mexico. This trade diversion effect exists in sectors where both Mexico and Canada export similar products to the United States and Mexico was the more efficient supplier.[21]

Fourth, a MUSFfA was expected to promote economic stability by attracting inflows of FOL Inflows of FOi would create badly needed jobs for Mexico, a country of 82 million, where one million new workers enter the labour force each year. Investment was expected to come both from U.S. multinationals, rationalizing production within North America, and from third-country firms (e.g., Japanese MNEs) anxious to use low-cost Mexican labour inputs and geographic proximity to access the U.S. market.

Among the sectors uncertain about United States-Mexico free trade were the chemical industry, the textile sector, and some small- and medium-sized businesses. Also hesitant were those that have traditionally been under state control, such as oil, railways, and electricity.[22] Finally, there was concern among agricultural interests that more efficient Midwest U.S. grain producers would swamp their less efficient Mexican

---

20 Hart, *A North American Free Trade Agreement*, p. 38.

21 Weintraub, 'The Impact of the Agreement," p. 111.

22 SCEAIT 66 (1990), p. 12.

counterparts, thereby reinforcing Mexican dependence on U.S. com, wheat, and beans.[23]

Many Mexican analysts, like their Canadian counterparts in the late 1980s, worried about a more formal relationship with an economy as strong as the United States. Some felt that the free trade discussions were being rushed and questioned the long-term implications of an agreement on Mexican political reform and sovereignty.[24] Given the economic asymmetries between Mexico and the United States, a free trade agreement might well simply perpetuate dependency.[25] These economic and political concerns notwithstanding, the Mexican government wanted the MUSFfA negotiations completed as quickly as possible.

Pressures for a NAFTA

Although Mexico's first preference was for a MUSFTA, it agreed to trilateral trade talks in early 1991. Mexico perceived several disadvantages in expanding the negotiations. Among them were the greater complexity of the agenda, implying higher possibility of failure; the fear that Canada and the United States might insist on the discussion of items in which Mexico had little interest or did not want on the table; fear that the two rich northern countries might demand concessions from the smallest and poorest partner; and uncertainty about the depth of Canada's commitment to a NAFTA. In addition, the limited trade and investment linkages between the two spokes suggest that potential gains from trilateral trade would be limited for Mexico.

On the positive side, Mexico welcomes the potential market opening that Canada might provide, as well as the possibility of increased Canadian FOi. Canadian companies have expertise relevant to Mexican economic development, for example, telecommunications, public transport, and environmental and resource-based technologies. Similar to the market completion initiatives in Europe, a NAFTA would strengthen the competitiveness of North American firms. The common experiences of Mexico and Canada in dealing with the United States and the expertise developed by Canadian negotiators in the Canada-United States FTA are also seen as means of improving the bargaining leverage of Mexico in its negotiations with the United States.

23 "Mexico: The Salad Bowl of North America?" ***Business Week*** (25 February 1991): p. 71.

24 Cuauhtemoc Cardenas, "Misunderstanding Mexico," ***Foreign Policy*** **78** (Spring 1990); pp. 112-30.

25 Sidney Weintraub, "The North American Free Trade Debate," ***Washington Quarterly*** 13, No. 4 (Autumn 1990): pp. 119-30.

THE SPOKES Vmw EACH OTHER

There are a number of similarities in the ways in which Mexico and Canada have approached free trade with the United States. Both countries are highly trade dependent; trade was twenty per cent of Mexico's gross national product (GNP) in 1985 and almost thirty per cent for Canada.[26] Like Canada, Mexico had long been wary of closer links with its larger neighbour. Mexico, too, considered alternatives such as sectoral free trade before opting for bilateral free trade. In the end, the attraction of formal trade links with the United States paralleled that of Canada, in terms of the importance of unrestricted access to its largest market and the avoidance of U.S. protectionism. Also significant were the effect of the Canada-United States FfA and the concern about the potential for trade diversion detrimental to the Mexican economy.[27]

While Mexico and Canada both expect increased economic gains from a trilateral agreement, the burden of adjustment falls mainly on them as the smaller partners. Mexico, in particular, faces considerable adjustment costs given its less efficient manufacturing and protected, agricultural sectors.

While each spoke is interested in deepening its links with the U.S. hub, neither is strongly committed to a trilateral arrangement. This is due to the historical lack of economic and political ties, simple geographic distance, and differences in income levels. High Mexican tariff and non-tariff barriers have historically discouraged Canadian exporters; and, while Mexico has enjoyed tariff preferences under the Canadian Generalized System of Preferences (GSP) for developing countries, its direct exports to Canada have been limited.

Over the past year and a half, Mexico and Canada have made a concerted effort to improve their bilateral relations. In January 1990, a delegation of seven Mexican cabinet secretaries came to Ottawa to discuss trade and investment issues.[28] In March 1990, Prime Minister Mulroney visited Mexico, followed by John Crosbie, minister of international trade in April 1990. During these visits, a number of agreements were signed and trade development linkages established. Mexican Commerce Secretary Jaime Serra Puche has come to Canada twice (in June 1990 and April 1991) and President Salinas spent three days in Ottawa in April 1991. Canada has also joined the Organization of American States as a way of demonstrating its growing sensitivity to Latin America.

---

26 Robert A. Pastor and Jorge G. Castaneda, *Limits to Friendship: The United States and Mexico* (New York: Vintage Books, 1989), p. 218.

27 Weintraub, 'The Impact of the Agreement."

28 Hart, *A North American Free Trade Agreement*, p. 68.

Most Canada-Mexico economic involvement has been mediated through the U.S. market by U.S. multinationals, e.g., in the auto sector. The rationalization of production in North America has already begun, and there is some evidence that regionalization of markets is occurring-Canada with the northern U.S. states, and Mexico with the southern ones.[29] A NAFI'A is likely to encourage this regionalization, particularly for low-value, high-weight products, due the geographic distance between these two spokes. While the promise of a growing Mexican market is attractive to Canadian exporters, given the disparities in income levels, it will be some time before they realize significant benefits.

Since June 1991, working groups from the three countries have been addressing a number of issues, including market access, rules of origin, non-tariff barriers, services, intellectual property, dispute settlement, petrochemicals, and agriculture. While neither spoke has yet formally articulated its positions, there are likely to be some differences of objectives in key areas. For example, Mexico may push for a long phase-in of tariff reductions and other market-opening policies on the grounds of its Less Developed Country (LDC) status, whereas Canada and the United States may be less receptive to these demands. Other contentious areas may be rules of origin dictating the amount of North American content in manufactured goods to avoid tariffs and the regional rules on the manufacturing of automobiles.[30] Since the Canada-United States FI'A is likely to be the starting point for NAFI'A discussions, Canada is concerned that the United States may use the trilateral talks to re-open the Canada-United States FI'A and alter current provisions such as the auto chapter, cultural issues, and patent protection for pharmaceuticals.[31] Some issues that are sensitive in United States-Mexican relations, most notably illegal immigration, may not be important to Canada, and vice versa, and these differing agendas may influence the ability of the two spokes to bargain with the hub.

CONCLUSION

According to both Lipsey and Wonnacott, two separate bilateral trade agreements, one United States-Mexico and the other United States-Canada, would create a hub-and-spoke trading arrangement in North

29 Canada, ***Canada and a Mexico-Unitea States Trade Agreement.*** Working paper (Department of Finance, July 1990), p. 15.

30 'Trade Deal Could be Signed Early," ***Financial Post*** (15 October 1991): p. 1.

31 Gordon Ritchie, "A Canada-Mexico-U.S. Free Trade Agreement: Watch Out!" ***Business Quarterly*** 55, No. 3 (Winter 1991): pp. 18-26.

America.[32] These economists argue that two bilateral FfAs would give U.S. firms preferential access to both Canada and Mexico, while restricting the two spokes to preferential access only to the hub. A separate United States-Mexico agreement would therefore adversely affect Canadian preferences negotiated under the Canada-United States FfA.

As this paper has argued, an informal hub-and-spoke relationship already exists in North America. While two bilateral F fAs would exacerbate this trend, a full triangular arrangement, with all three countries as equal partners, will be difficult to negotiate given the substantially lower level of economic development and wages, the much more rural and agricultural nature of the Mexican economy, and traditional Mexican suspicion of U.S. multinationals.[33] Once negotiated and implemented (probably over a ten-year period), a NAFfA should provide both opportunity and motivation for substantial rationalization of production by U.S. MNEs on a continent-wide basis. Therefore, foreign investment patterns are likely to further integrate the spokes with the hub. We conclude that the hub-and-spoke relationship is likely to persist as a result of growing, cross-border regionalization of markets, though its intensity may be moderated by the choice of a NAFfA over two bilateral agreements.

32 For more information, see Richard Lipsey, ***Canada at the U.S.-Mexico Trade Dance: Wallflower or Partner?*** Commentary No. 20 (Toronto: C.D. Howe Institute, August 1990); Lipsey, "Growth, Erosion and Restructuring"; Wonnacott, ***U.S. Hub and Spoke Bilaterals;*** and Wonnacott, ***Canada and the U.S.-Mexico Free Trade Negotiations.***

33 Hart, ***A North American Free Trade Agreement.***