Mexico competitive advantage in NAFTA: A case of social dumping?
A view from the Automotive Industry

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Abstract

In the midst of NAFTA renegotiation the Mexican Automotive Industry (MAI) draws more attention. Gaining a progressive share of markets, jobs and portfolio investments within the region and accounting for the entire U.S. trade deficit, the MAI is one of the most critical pieces in the way towards a new NAFTA. This and the fact that Trump has criticized it as an example of the wrongdoings of the old agreement calls for new contributions to better assess its sources of competitive advantage.

This paper builds on business cycle theories and socioeconomic perspectives of market embedded institutions to provide an additional window to study the MAI. It articulates theory and extensive primary and secondary evidence to demonstrate that the MAI position rests on social dumping policies underpinning illegitimate sources of competitive advantage. Then it discusses the issues at stake in the current NAFTA renegotiations rounds.

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Introduction

No industry as the automotive shows the nuances and outcomes of NAFTA's twenty-three years. Coming from a weak and outdated manufacturing base and without an internal market to spur its economy, over the NAFTA era the Mexican auto industry (MAI) has grown at a 7 percent yearly rate. At this rate, at the turn of this decade, Mexico will be manufacturing one-third of the North American output and be becoming the new automotive capital of the whole region (Forbes, 12/28/2014). Mexico is now an increasing manufacturing and export hub, while Canada has lost ground and the USA has sent South thousands of jobs. While other factors account for turning the country into the 7th producer and the 4th exporter worldwide, as well as the 1st one to the American market, NAFTA, cheap labor and a declining peso are the factors around which the rest cluster.

This paper makes the case that these last factors amount for social dumping policies to build an international advantage on nonsystematic competitive grounds, namely spurious competitiveness in ECLAC (2014) terms. Instead of a structured capacity building approach based on technology and innovations developments along the upgrading and remuneration of human capital, such competitive advantage breaks the rules of free and fair trade. The argument runs as follows:

At present, workers of the MAI make $2.3 per hour, less than 90 percent than their American counterparts. Such pay is 59 percent lower than the one they received a decade ago, so that labor costs has been descending five percent per year at average throughout the industry boom. None of the three most significant conditions socioeconomic theory recognizes as possible drives of a decreasing value of labor in a free market economy takes place in the MAI. That is:

- The trough or contraction stages of the business cycle. As noted, the MAI has experienced a steady high growth to such an extent that is now one of the hottest spots globally in the sector, and corporation representatives call it 'the China of Occident.' Therefore, in the MAI the traditional business cycle has been broken and wages behave as if the industry were in the cycle's contraction or trough stages. Neither the Keynesian cycle of growth nor the mainstream, Real or Austrian versions of it work in the MAI.[1]

- Declining levels of productivity. From 2007 to 2015 Mexican workers of the whole industry increased their productivity at a 9 percent average rate annually. Therefore, nor also the Schumpeterian cycle of innovation, productivity and development take place in the Mexican case.[2]
- Absent or lower levels for regulating the labor and management relationship and providing social protection. Mexican labor law provides higher levels of protection for workers than that of the U.S. and Canada in terms of individual and collective dismissals, and regulation on temporary employment. And Mexico has ratified seven out of eight fundamental ILO Conventions, while U.S. has just two. Therefore, from a Polanyian embeddedness perspective[3] the country has the factory laws, representation structures and social legislation needed to better tame the market forces as compared –say—with its mayor NAFTA partner. In practice, however, it is the other way around.

Therefore, it is not only that through cheap labor and the lowering of social standards Mexico has built an export subsidy (van Roozendaal, 2002). It is that the MAI conforms the strictest case of social dumping. That is, policies and practices "… undertaken by self-interested market participants of undermining or evading existing social regulations with the aim of gaining a competitive advantage" (Bernaciak, 2014:16). As the paper shows, the main problem of labor in Mexico is law enforcement, particularly in such critical conventions as the right to freely organize

[1] Cfr. Keynes, M. (1930) *The General Theory of Employment, Interest and Money*. Stellar Classics.

[2] Schumpeter, JA (1934); *The Theory of Economic Development: An Inquiry Into Profits, Capital, Credit, Interest, and the Business Cycle*. Transaction Publishers.

[3] Polanyi, Karl (1989), *The Great Transformation*. Madrid La Piqueta.

and engage in collective bargaining. In the end, Mexico offers a problematic functioning of the social institutions in which its market is embedded.

Labor costs are not a minor issue in the industry. A KPMG (2016) study demonstrates that they "represent the largest category of location-sensitive cost factors," ranging from 40 to 57 percent of location-sensitive costs for manufacturing.[4] Henceforth, the implications of Mexican cheap labor for the North American industry should be more fully assessed. This paper will contribute to such task.

On the other hand, during these years of MAI boom, the peso has kept descending against the dollar, following the more than 2,500 percent accumulated devaluation since the early 1970's. Given the fact that through a depreciated currency a country gets a cheaper domestic economy that increases demand for exports and its appeal for foreign investors (Herrera-Echeverry et al., 2016), there is no doubt that a successive depreciated peso has made less expensive manufacturing vehicles and parts (CAR, 2016). Thus, through a weak currency the country is piling up practices for getting an extra competitive advantage on illegitimate grounds in terms of free trade.

The paper is organized in five sections. Section one shows the development of the MAI over the NAFTA 23 years in the context of the North American market. It studies how while Mexico has built a dense network of free trade agreements to cement its stand as an export platform NAFTA is its masterpiece. Then it discusses why the auto industry is the most critical piece in NAFTA renegotiations.

Section two focuses on the role of cheap labor for building MAI competitiveness. It works with primary evidence from collective bargaining agreements signed by management and labor unions in the existing 18 automotive factories, as well as with qualitative data gathered from focal groups carried out with autoworkers. It demonstrates that in addition to keeping wages down labor costs are even more compressed through a lower *tax wedge*. Thus the section shows that in the MAI there is a race to the bottom involving all OEMs, regardless their nationality, brand position, age, and even car segment. Then it analyses how the lowering of labor standards renders one of the highest profits of the industry worldwide.

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[4] Other location-sensitive cost factors range as follows: Cost of capital, 11 to 25 percent; taxes, 10 to 18 percent; transportation, 6 to 21 percent; utilities, 2 to 7 percent; and facilities, 2 to 5 percent.

Section three heads to demonstrate that the MAI is being backed by social dumping policies. To this end, it deals with each of the three situations socio-economic theory identifies as responsible for declining wages and labor compensation under a free market economy. They are productivity and business cycle evolutions, and rules to govern the labor and management relationship. Then the analysis moves to identify how a policy of having a weak currency supplements the MAI approach to keep competitive advantage.

Section four study the mechanisms through which state and private agencies evade labor regulations to keep compensation costs down and undermine labor organization's initiatives other than the one they consent and control. It identifies how these features have remained unchanged –and even grown—within the NAFTA framework, creating a comfort zone for Mexican public and private representatives whose unique concern is keeping things unchanged and luring foreign investors.

Section five sums up conclusions and implications with a focus on the current NAFTA renegotiation.

I. Mexico competitiveness, free trade networks and NAFTA

Mexico is not competitive in infrastructure for communications, utilities and facilities costs, and just ranks moderately in taxes and cost of capital –i.e., the bulk of variables that factor to define the competitive advantage of a given jurisdiction (KPMG, 2016). While progressing as the workshop of the North America, the country's port, road, rail and air systems are under a growing stress and the programs to develop them keep lagging behind. The U.S.-Mexico 3,145 km continental border, 29 km Pacific Ocean and 19 km Gulf of Mexico borders partially compensates this. Still, the country's costs of transportation are 40 higher than in the U.S., as so they are on electricity and gas (CAR, 2016). Then it comes the crime and insecurity issues. Taking the 22th position among the most dangerous countries in the world according to the Global Peace Index 2016, in Mexico business costs have to pill up stronger externalities for insurance, safety, and losses.

Despite all these, Mexico ranks as one of the three leading markets for international business location, just next to China and India (KPMG, 2012-2016). How come? The first part of the answer hinges on NAFTA provisions that allow OEMs to manufacture in Mexico and penetrate the American market tariff free.

Shifting sides

Back in 1990 Mexico manufactured a tiny part of the North America auto output while the U.S. share was 78 and Canada 16 percent, respectively. NAFTA would change the history. By 2000 Mexico had more than doubled vehicle manufacturing. Still the greater transformation would take place after the 2008-2009 global financial crisis. From then onwards output of the Mexican auto industry (MAI) has grown at a 7 percent yearly rate. Such growth has led it to increase year after year its share in the region, whereas the USA and Canada shrink theirs. Last year these figures were 20, 67, and 13 percent, respectively.

Employment has closely followed this trajectory. Back in 1999, the U.S. had 1.1 million jobs in the sector, of which 380,000 were manufacturing vehicles. By 2009 they had been reduced to a half. And even when from then jobs have bound back backed by the recovery of the sector and by 2016 hit 945,000 (211,000 automakers and 734,000 part suppliers), over these two decades there has been a net job loss of 17 percent. It is important to note also that just 22 percent of that auto jobs are in motor vehicle factories, down from the 35 percent and more they used to reach in previous decades. By contrast, autoworkers in Mexico have increased 47 percent during this boom and now approach 700,000 jobs, out of which 10 percent are in motor vehicle factories.

Table 1 North America Cars & Commercial Vehicles
Vehicle production (Millions)

Year	Canada	USA	Mexico	North America
1990	2	9.8	.8	12.6
1997	2.3	12.1	1.4	15.8
2000	3	12.8	1.9	17.7
2007	2.6	10.8	2.1	15.5
2016	2.4	12.2	3.6	18.2

Source: Own elaboration with OICA’s data.

Trade balances

First and foremost NAFTA accelerated the flow of goods and services in the region, particularly between the U.S. and Mexico. From 1993 to 2016 trade between both nations multiply more than five times and thus the U.S. balance went from positive (at 1,6 billion) to a negative record (at 64.3 billion).

Table 2 U.S.-Mexico Trade
(Millions)

Year	Exports	Imports	Balance
1993	41,580	39,917	1,663
2016	229,701	294,055	-64,354

Source: Own elaboration with United Census Bureau's data.

As noted elsewhere, the automotive sector accounts entirely for this imbalance. From 1993 to the last year the U.S. deficit with Mexico in the sector have multiplied almost twenty times, with vehicles accounting for two thirds of these figures and auto parts making the remaining third. Likewise, the Canadian automotive deficit with Mexico has increased five-fold over these 23 years. These figures show how the Mexican auto industry benefited the most of NAFTA provisions and turned into the most dynamic activity of the unstable Mexican economy.

This is why the auto industry is the most critical piece in NAFTA renegotiations so that the Trump administration knows it that through closing the borders for the sector the U.S. deficit with Mexico would disappear.

Table 3

Trade Balances
North American Trade in Motor Vehicles and Parts: 1993 and 2016
(billions of $US dollars)

Bi-lateral Trade	1993	2016	Change	% Change
U.S. with Canada				
Vehicles	-$18.5	-$20.6	-$2.1	
Parts	$7.9	$12.4	$4.5	
Total	-$10.6	-$8.2	$2.4	23%
U.S. with Mexico				
Vehicles	-$3.5	-$45.1	-$41.6	
Parts	-$0.1	-$23.8	-$23.7	
Total	-$3.6	-$68.9	-$65.3	-1814%
Canada with Mexico				
Vehicles	-$0.7	-$4.8	-$4.1	
Parts	-$0.9	-$3.9	-$3.0	
Total	-$1.6	-$8.7	-$7.1	-444%

Sources: U.S. Congressional Research Service, The North American Free Trade Agreement, May 2017; Industry Canada Trade Date On-Line - Statistics Canada

(Taken from http://www.bilaterals.org/?unifor-uaw-statement-on-auto-and&lang=en).

From the lure of free trade to the appeal of the American market

Mexico has created a dense network of international trade arrangements that back its competitive advantage as an export platform. They include 10 free trade agreements encompassing 45 countries, 32 agreements for promoting and protecting investments, and 9 trade agreements within the Latin American Association for Integration (ALADI) framework (see (www.promexico.mx/es/mx/tratados-comerciales). These, along with Mexico membership at WTO, OCE, and APEC grant Mexican exports tariff-free access to countries accounting for most of the Gross Domestic Product worldwide (60 percent according to CAR, 2016).[5]

Still, OEMs come to Mexico at the first place looking for access to the American market based on the avenues opened by NAFTA. In this respect facts are overwhelming: 82.5 percent of Mexico auto output goes to international markets, from which the North American market takes 76 percent. And, as FCA CEO Sergio Marchionne put it talking about Trump announces to impose a tariff on Mexican exports or ends NAFTA,

"The reality is the Mexican automotive industry has for a number of years now been tooled-up to try and deal with the U.S. market. If the U.S. market were not to be there (or NAFTA by the same token), the reasons for its existence are on the line," (Reuters, online, http://www.reuters.com/article/us-usa-autoshow-fiat-chrysler/fiat-chrysler-may-end-mexico-output-if-trump-tariff-too-high-ceo-idUSKBN14T1UG, January 9, 2017).

Such logic extends to the more than 2,500 auto suppliers and logistic factories set up in Mexico, which perform more than fifty billion intra-firm trade annually to move back and forth parts and components that are critical to make vehicles across the North American borders. They stick to the geographical logic of automakers so that where assembly plants go, including engine and transmission plants, they move to build and increase a web of transactions across firms.

[5] For instance, CAR estimates automakers can save $2,500 per vehicle in tariffs when exporting from Mexico to the European Union, as compared with doing it from the U.S.

II. Using the low road for labor to build competitiveness

Cheap labor is the next variable of the MAI's equation for building competitiveness. Mexican officials like to say that autoworkers make 8 to 10 dollars hourly (for instance Inegi and AMIA). This may true when mixing together white and blue collars to get a factory overall compensation cost.[6] But when subtracting salary from the equation, numbers collapses and a raw reality emerges: Mexican autoworkers are poor people making poor wages. That is a 2.3 dollars at average right now for vehicle assemblers, a half less for workers of part suppliers tiers 1 and 2, and a half that for workers of part suppliers 3 and 4.[7] The author has carried out six focal groups with autoworkers of the Bajio and North regions over the last four years. Inquired on their subjective well-being, they are quick to answer: 'Our payment is not sufficient to provide us a decent standard of living' –i.e., the equivalent to the typical "no nos alcanza" of the median Mexican. Just a few of them (the twentieth percent that has been working for 15 or more years) say otherwise.

Adding 30 percent for statutory & fringe benefits to get total labor compensation, they obtain 2.99 dollars per hour.[8]

Table 4 shows daily wages of Mexican autoworkers plant by plant as set in the last labor contracts signed between management and unions. Several points are worth to underscore:

- The 2.3 dollars mean pay implies that Mexican autoworkers make not even a tenth of their U.S. counterparts –considering a mean hourly wage of 26.5 dollars in 2016, according to BLS (at https://www.bls.gov/oes/current/naics4_336100.htm). Likewise, their 2.9 dollars for total compensation is far less small when compared with the 47

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[6] INEGI, the federal government official statistic office, provides this data under the concept of "masa salarial," or "remuneraciones al trabajo." See for example, Inegi (2010-2015) *La Industria Automotriz en Mexico. Estadisticas Sectoriales.* En *Estadisticas a Proposito de la Industria Automotriz* (Inegi-AMIA, 2016), under the concept of "remuneraciones a los trabajadores" (a concept equivalent to labor cost –i.e., wages plus statutory/fringe benefits), they register 25,280 pesos per month. This figure is 2.5 times higher than the data we found in labor and management collective bargaining agreements.

[7] Data for workers of part suppliers are based on Covarrubias' (2014-2016) studies.

[8] I estimate this 30 percent based on the specifics contained in the same collective bargaining agreements. The Conference Board estimates at 29.7 percent of total compensation the cost for benefits in the whole Mexican manufacturing sector (*The Conference Board International Labor Comparisons*).

dollars made by American autoworkers (this data according to *The Conference Board International Labor Comparisons*, online, https://www.conference-board.org/ilcprogram/). Put it bluntly: Mexican workers make 94 percent less than American's.

**Table 4 Blue Collar Workers
Assembly Plants Hourly Wages.**

OEM/Plant (Contract year)	Mexican Pesos	USD
Nissan Civac (2016)	60	3.2
Chrysler Toluca (2015)	59	3.2
Chrysler Coahuila (2015)	59	3.2
VW Puebla (2016)	54	2.9
GM Toluca (2016)	51	2.8
Audi SJCh Puebla (2017)	50	2.7
Ford Cuautitlan (2016)	46	2.5
Toyota Baja California (2016)	46	2.5
Kia Pesqueria (2015)	46	2.5
Ford Hermosillo (2016)	42	2.3
Nissan Aguas Calientes (2016)	40	2.2
Nissan Aguas Calientes II (2016)	40	2.2
GM Ramos Arizpe (2016)	36	1.9
Honda El Salto (2016)	35	1.9
GM San Luis Potosi (2016)*	33	1.8
Honda Guanajuato (2016)	31	1.7
BMW San Luis Potosi (2016)*	28	1.5
Mazda (2016)	19	1
Mean hourly wage	43	2.3

Source: Collective Bargaining Agreements (as registered in Labor Minister Office STPS as of February, 2017). In parenthesis the year labor and management signed the contract and registered at the STPS offices. 1 dollar= 18.5 Mexican pesos, March 2017 (Banco de Mexico: http://www.banxico.org.mx/portal-mercado-cambiario/).
* As known, Ford canceled its plans to build its San Luis Potosi factory at the beginning of 2017 at the wake of Trump pressures to impose a tariff on Mexican exports to the U.S.

- The wage dispersion across the industry is considerable. In the extreme, Nissan Civac pays more than three times what Mazda does.
- Labor compensation is set up at the plant level so that there is a not any bargaining pattern for labor in the Mexican auto industry other than racing to the bottom, even at the company and regional levels.
- Such racing to the bottom involves all OEMs, regardless their nationality, brand position, and even car segment. Take the case of BMW, a global leader in the Premium Segment whose home country holds one of the most structured

industrial relations systems providing the highest wages worldwide. It chose Mexico San Luis Potosi to manufacturing its next generation of 3 Series with one of the lowest wages.

- In general workers from old brown factories make more than workers from brand new plants or green fields worksites. Though this is not an iron law in the MAI. For instance, Audi San Jose Puebla and Kia Monterrey, which just start running, are paying more than Ford Hermosillo and GM Ramos Arizpe, which have been churning vehicles for more than three decades.

Mexico championing: Cheaper labor rendering some of the highest profits.

CAR estimates labor costs savings of $674 per car in Mexico at 8.24/hour compensation rate. It could be more than double that amount taking the one this paper finds. There are other variables making cheaper Mexican labor.

The OCDE' tax wedge, which shows the percent of labor costs that goes to income tax and social security contribution from both the employee and the employer, is a third lower in Mexico versus their North American partners. It is much lower when compared with the average of OCDE countries, namely 20.1 versus 36 percent, respectively (Table 5). Income tax and employee social contribution account for most of the difference. To a large extent, this reflects that in Mexico there are many tax-exempt low-income people. [9]

Table 5 OCDE Tax Wedges (2016) (as a percentage of labor costs).

Country Total Tax Wedge	Income Tax	Employee SSC	Employer SSC
CAN: 31.4	13.8	6.8	10.8
US:: 31.7	16.9	7.1	7.7
Mex: 20.1	8.5	1.2	10.4
OCDE: 36	13.4	14.4	14.4
Latin American countries: 21.7	0.3	7.7	14.3

Source: OECD (2017), *Taxing Wages 2017. Tax Policy Analysis*; OCDE/CIAT/BID (2016), *Impuestos sobre los Salarios en América Latina y el Caribe.*

[9] This is a common feature of Latin American countries (LACs). LACs average tax wedge of 21.7 percent can be explained on the same grounds of Mexico's.

KPMG's Guide to International Business Location Costs gathers information showing that in auto parts manufacturing Mexico offers after-tax profits more than four times higher than in U.S. and Germany; twice than in Canada, France, Italy, and Netherlands; and 13 times than in Australia; not to mention Japan's where they are negative. They are even higher than that of Russia and Brazil, and just next to India and China. Again, within the set of variables that determine these profits outcomes, labor costs are the discriminating factor in the case of Mexico (KPMG, 2012).

Wages in the MAI are not only low but have going down. Covarrubias (2014) study found that by 2013 autoworkers were receiving $3.6 per hour. Likewise, Stanford (2010) noted that by 2007 they made $3.95 per hour ($1.65 more than the current $2.3). Therefore, over these last ten years of sizeable growth of the MAI –i.e., an output yearly rate increase of 7 percent—autoworkers' wages have decreased by 42 percent. That is a yearly average decrease of 4 percent.

On the other hand, the reduction of wages means that the value they lose is going to the other side of the income equation, namely the income of corporations (assuming a fixed tax share). Available data shed some light on this: Within the added value structure of the MAI and under a fixed tax rate of less than 1 percent, while in 2007 labor compensation share was 22, six years later it decreased to 14 percent. By contrast, the share of capital remuneration (seen as gross operating surplus) went from 77 to 86 percent (data from INEGI, 2015).

III. Is Mexico a case of social dumping and spurious advantage?

The specialized literature recognized tree situations under which a decreasing value of labor could take place and be expected. They are the trough or contraction stages of the business cycle, lower levels of productivity, and absent or lower levels for regulating the labor and management relationship and providing social protection in a given jurisdiction. None of them fit the MAI so that the lower labor costs of the Mexican autoworkers come from social dumping policies.

When wages and productivity follow opposite directions and the braking of the business cycle

Could this wage evolution be explained by the productivity of Mexican autoworkers? This is an important question as lower productivity in developing countries settings often explains real-wage differentials (de la Dehesa, 2007), or, at least, is instrumental in justifying them. Table 6 data says that that is not the case in the MAI and quite the contrary they are extraordinary productive employees.

Table 6

Job, production value & labor productivity indexes*

Year/Index	Employment (1)	Production Value (2)	Labor Productivity 2/1
2007	100	100	100
2008	96	102	106
2009	77	89	115
2010	88	126	144
2011	103	149	145
2012	116	178	153
2013	127	191	150
2014	138	216	157
2015	147	258	176

Source: Own elaboration with data from Inegi: Encuesta Mensual de la Industria Manufacturera.
* Data for the whole transportation sector.

As shown, over the 2007-2015 period the Job Index increased 147 while the Value Production Index grown 254. As a result, Labor Productivity (the Job Productivity Index coming from VPI/JI) rose to 176. Put it differently, from 2007 to 2015 Mexican workers of the whole industry increased their productivity at a 9 percent average rate annually.

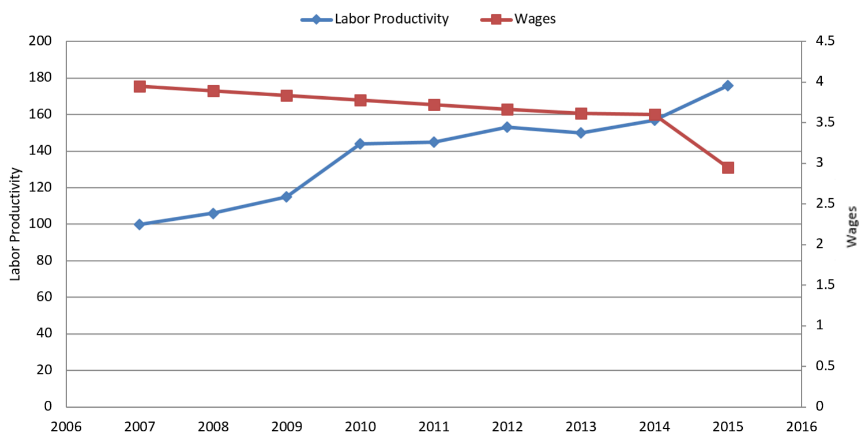
The productivity of Mexican autoworkers is a well-known asset between management. For many years Ford Hermosillo plant was the second most productive of the corporation worldwide. Nissan rates its Aguascalientes facility among the “company’s most productive and profitable.” European automakers have learned something similar (author’s interviews with plant managers of the eight OEMs in

Mexico from 2013 to 2016). Specialized consulting agencies' studies such as KPMG (2014) and Hi (2013) came to similar conclusions.

Therefore, in the MAI there is not only a growing wage-productivity gap, but wages and labor productivity follow opposite directions (Figure 1).

Figure 1

Labor productivity and wages. MAI 2007-2066



Source: Tables 4 and 5.

At the same time, these basic data show that in the MAI has been broken the relationship between investment, output, employment and wages. That is, in the MAI the traditional business cycle does not work. In terms of income, wages behave as if the industry were in the cycle's contraction or trough stages, no matter that the boom is here and investment and employment levels have steady been in the raise. Nor the Keynesian cycle of growth, employment and money nor the Schumpeterian one of innovation, productivity and development take place in the Mexican case, [10] as neither do the mainstream, Real or Austrian versions of it.

From protective labor provisions to subscribing basic labor standards

Mexican labor law provides higher levels of protection for workers than some OECD countries. Certainly they are much better than those of the U.S. and Canada in terms of

[10] Cfr. Keynes, M. (1930) *The General Theory of Employment, Interest and Money*. Stellar Classics; Schumpeter, JA (1934); *The Theory of Economic Development: An Inquiry Into Profits, Capital, Credit, Interest, and the Business Cycle*. Transaction Publishers.

protection of workers against individual and collective dismissals, as well as regulation on temporary forms of employment.

Table 7

The OECD indicators on Employment Protection Legislation
Scale from 0 (least restrictions) to 6 (most restrictions), last year available

	Protection of permanent workers against individual and collective dismissals	Protection of permanent workers against (individual) dismissal	Specific requirements for collective dismissal	Regulation on temporary forms of employment
Can	**1.51**	**.92**	**2.97**	**.21**
US	**1.17**	**.49**	**2.88**	**.33**
Mex	**2.62**	**1.91**	**4.38**	**2.29**

Source: OCDE, 2013, *Indicators of Employment Protection*, online, http://www.oecd.org/els/emp/oecdindicatorsofemploymentprotection.htm.

Table 8 Fundamental ILO Conventions. North American countries

Convention	*U.S.*	*Canada*	*Mexico*
C29-Forced labor		*X*	*X*
C087-Freedom of association and protection of the right to organize		*X*	*X*
C098-Rigth to organize and collective bargaining		*X*	
C100-Equla remuneration		*X*	*X*
C105-Abolition of forced labor	*X*	*X*	*X*
C111-Discrimination (employment and occupation)		*X*	*X*
C138-Minimum age		*X*	*X*
C182-Wors forms of child labor	*X*	*X*	*X*

Source: ILO, online, http://www.ilo.org/global/lang--en/index.htm

Likewise, Mexico subscribes most of the fundamentals ILO conventions. Canada leads the region in this respect as it has ratified all of them. The U.S. has subscribed just two, namely the 105 (abolition of forced labor) and the 182 (worst forms of child labor).

The Mexico shortcomings in this respect are twofold. First, in Mexico there is an extended problem of enforcement of labor rights. Second, the most critical problems of them revolve around the right to organize and collective bargaining. It is telling that its corresponding ILO Convention –i.e., the 098—is the one that Mexico has not yet ratified. We will go in deep to this below. Now its time to observe the other feature that makes the Mexican equation of unsystematic competitiveness, namely a weak peso.

From social dumping to spurious competitive advantage

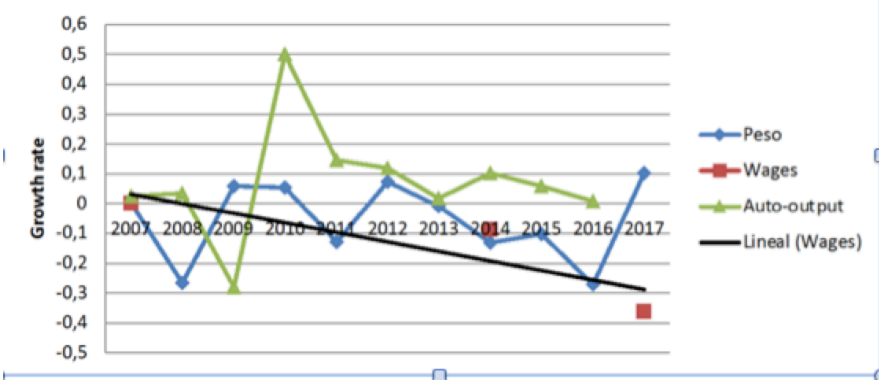
In the early 70's came to an end the Mexico more than two decades period of high economic growth, income and internal market development and steady exchange rate. Since then every government has aimed to turn the country into an attractive open economy from which international capitals can find many avenues towards global markets. A companion of this enterprise has been **a** weak and instable peso. In fact, government turned it into the third masterpiece to build its competitive position.

From 1970 to 2006 the peso devaluated 2,574 percent against the U.S. Dollar. During the last 10 years –i.e., over the current boom of the MAI—the peso has lost 34 percent of its value (62 percent if we take the rate of December 2007). Then it comes the lowering of labor. The minimum wage study conducted by Garavito (FES México, 2013) demonstrates that between 1976 —the point at which they reached their highest level— and 2013 workers' incomes lost 72.4 percent of their purchasing power.

There is debate as of if through a devalued currency a country intends to get competitiveness. Provoked or not, the fact is that through a depreciated currency a country gets a cheaper domestic economy that increases demand for exports and its appeal for foreign investors (Herrera-Echeverry et al., 2016). It represents what ECLAC (2008) terms spurious or unsystematic competitive advantage. There also is a debate as to the implications of keeping down wages to create artificial competitive advantage. And again, the fact is that through cheap labor and the lowering of social standards takes place an export subsidy that creates a social dumping (van Roozendaal, 2002).

Therefore, the tandem cheap peso/cheap labor makes Mexico matchless in terms of manufacturing costs. Figure 2 exhibits how a declining peso and decreasing wages have closely run over the boom of the MAI, making all attractive for international capital to land in Mexico.

Figure 2 Auto output, currency and wages. Growth rates



IV. Breaking the labor law

Mechanisms for spoiling the labor and management relationship

Having said all this, the MAI competitive advantage rests on social dumping policies as much as it does on NAFTA provisions and a weak peso. Such policies in turn lie in the violation of the mechanisms for regulating the labor and management relationship, particularly the right to freely organize and engage in collective bargaining. Lets start with the Kia and BMW labor contract agreements that subscribe the wages exhibited before at Table 4. Note that Kia had a labor agreement since 2015 and BMW since 2016, despite the fact that the former just begun running in 2016 and the latter will do so by 2019. How come?

The answer is that in the MAI (as in all Mexico) is possible to sign a labor contract before a factory is open and workers are hired. It is a flagrant violation of the labor law of course. Widely known as protection contracts ("contratos de protección"), it is a customary practice through which, at the very moment that a factory begins to be built, management and a labor union sign a contract. To do that, they had previously gotten the approval of state representatives, which means that it is a government led activity institutionalized through informal mechanisms. There also is a deal of corruption involved in such practices. Official union leaders receive a lump sum and a monthly pay from management for signing a labor contract committed to keep under control workers demands for better wages and working conditions.

In fact, these kind of mechanisms have allowed political officers to structure and drive a labor movement that serves a broad array of state-led objectives –i.e., from control work settings, to run political campaigns, to back economic policies, to attract investments, to bribe labor leaders, etc. (Cfr. Cook, 1996-2015; Bensusan and Middlebrook, 2013).

Prima face evidence of unions centrally structured and intervened by the government is CTM, CROM, CTS-CROC and the like. They lie behind all the labor situations that explain the downgrading of labor in Mexico and the MAI social dumping. They own 90 percent of the existent collective bargaining agreements in the sector and they are the ones that sign the so-called *contratos de protección* everywhere.[11]

Because of this, where there is a labor union other than the officials or state-control is more likely for workers to get better wages. Nissan and VW labor unions are good examples. Traditionally they have identified themselves as "independent" --drawing the line between them and state-dependent unions-- and been at the forefront of getting better wages and benefits. Though, it is not always the case. Especially when independent unions meet with stiff opposition from management who are supported all the way by state officials. In such a situation outcomes for labor could be counterproductive. Honda and Mazda have been cases in point lately. Over years their workers have been struggling to organize out of CTM-like unions at very high costs. There have been dismissals of union leaders and at the end management have imposed labor arrangements with some of the lowest wages and benefits of the whole sector (again, see Table 4).

This explains why governments have been reluctant to ratify ILO 98 Convention despite the fact Mexico labor law grants workers the right to organize and engage in

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[11] Bouzas et al (2007) and Covarrubias and Bouzas (2016) estimate that out of the total of collective bargaining agreements existing in Mexico across all economic activities around two thirds are protection contracts.

collective bargaining. In brief, state representatives do no want ILO to supervise the way things go in these crucial features of the labor and management relationship. Furthermore, private business representatives are the first allies of government on such stand that advocates protecting the national sovereignty to conduct labor without “international intervention.”

The violations of basic labor rights in Mexico and the existence of protection contracts has been denounced in national and international forums. ILO supervisory bodies, Committee of Experts, and the Conference Committee on the Application of Standards, among others, have received many allegations relating such violations and cases of violence and arrests against independent union leaders. International Labor Confederations like ITUC and IndustriAll have been presenting the cases. Still, there have been just limited results. They do not go beyond the standard ILO recommendations and Mexican public representatives’ promises to study the problems and take corrective actions. (Bensusan and Middlebrook, 2013; Bensusán and Covarrubias, 2016).

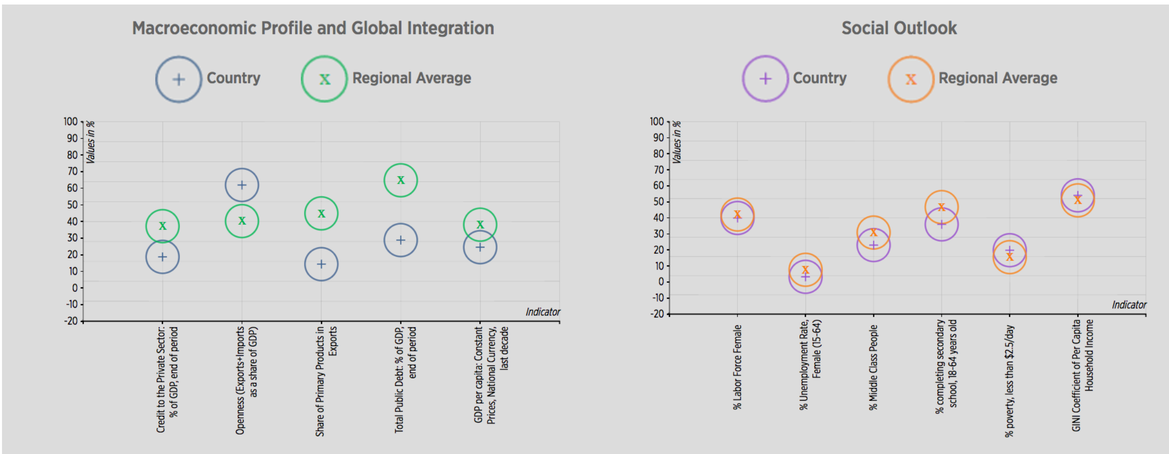
Something similar has happened inside the negotiations of NAFTA. Since its inception Mexican representatives opposed to include labor as a part of the agreement so that a side body came into being, the North American Agreement on Labor Cooperation (NAALC), with truly limited mechanisms to oversight and advance labor rights (Compa, 2001; Compa and Brooks, 2015).

From a falling economy to opposing change, to keeping NAFTA unaltered

During the NAFTA era Mexico has failed in terms of socio-economic development, growth and income distribution. Mexico led the Latin America region in terms of openness and global integration, but lags behind in GDP growth and GDP per capita, credit and public debt. Its social indicators have fared even worst in scope of poverty, inequality (GINI coefficient), education attainment, and middle class progress (Figure

3). In fact, after two decades of NAFTA Mexico reached the lowest rate of GDP per capita among the 20 Latin America countries, only up of Venezuela and Guatemala.[12]

Figure 3



IDB: Countries at a glance, online,https://data.iadb.org/IADBOpenDataVisuals/en/country-at-a-glance.html?country=MEX

As a result, the MAI is for Mexico its NAFTA' flagship. By 2013 Mexico received more flows of foreign investment in the auto sector than China and India, not to mention the rest of countries competing for attracting auto corporations (FDI Markets. Emerging Markets; James Kynge, April 21-2015). Since the beginning of the MAI boom annual announcements of new capital investment have averaged 4.3 billion and since 2011 nine of the eleven new factories for the continent have landed in Mexico (CAR, 2016). Then the MAI have kept growing and consolidating its position as a tractor sector of the unsteady Mexican economy. In the last 16 years it has multiplied four times the growth of the GDP and five times that of the industry as a whole.

Whit these amounts of money pouring into the country, state and private representatives see no incentive to change so that they are attending NAFTA renegotiations called for the Trump Administration with a single goal at hand: Resist

[12] Mexico GDP per capita averaged 0.9 annually over these decades, while the Latin America region averaged 1.6. (Feenstra and Timmer, IMF, 2013).

and avoid that a single coma of the agreement change, despite American and Canadian's struggle to do otherwise.

V. Conclusions and implications

The paper provides an additional window to assess how the MAI has built is renowned international competitive advantage inside NAFTA. The country has done so, it argues, through lowering labor standards, depressing wages and keeping a weak currency, and using NAFTA provisions to access the region tariff-free. While other studies have underscored the role of one or other of these factors to explain the boom of the MAI, I show that they cluster together to shape the core of its competitiveness to such an extent that they offset the shortcomings of other factors. That is transportation, infrastructure for communications, taxes, and utilities, facilities and capital costs.

More importantly, the paper contributes a theoretical lens to qualify the Mexican as a social dumping/spurious competitive advantage building approach and gathers evidence to support it. From a business cycle perspective the MAI approach to labor makes wages behave as if the industry were in the cycle's contraction or trough stages. It follows that the Keynesian cycle of growth dos not work in the MAI context. Then it comes the labor productivity issue. In the MAI there is not only a gap between productivity and wages but also a manifest contradiction between two variables following opposite directions (with the former going up and the latter down) when they are meant to run together. From an Schumpeterian perspective such a gap represents the breaking up with the cycle of innovation, productivity and development.

At the end Mexico offers a problematic functioning of its social institutions. From a Polanyian perspective the country has the factory laws, representation structures and social legislation needed to better tame the market forces as compared –say—with its mayor NAFTA partner. Thought, none of these seems to apply in the MAI as its economy appeared dis-embedded of its social institutions. Thus, the MAI fills the strictest case of social dumping as supports untamed market participants that are able to undermine labor regulations with little o no restriction.

The competitive advantage of the MAI coming from the lowering labor and exports costs thanks to the dyad cheap wages/weak peso has had no parallel and corporations can increase profits as in no other jurisdiction. In an industry where competition is always getting thicker and whose location-sensitivity is cost dependent, a jurisdiction premising such a dyad while granting quality and market access makes all the difference. The MAI has grown under these premises and promises throughout the NAFTA era, making the most of deploying social dumping policies. Data are overwhelming. Auto corporations have picked up Mexico as the premier location to land new investments and portfolio projects in the NAFTA region at the expense of the U.S. and Canada. Likewise, while jobs decrease or freeze in the U.S. and Canada, they grow in the MAI.

Given the fact that most of these projects target the American market taking advantage of NAFTA provisions, U.S. trade imbalances have skyrocketed. It is not by chance that the MAI accounts entirely for the U.S. deficit with Mexico.

All this is on the negotiation table now that NAFTA has been opened at a Trump administration request, where the automotive industry takes center stage. The priorities of each part are crystal clear The U.S. wants to eliminate its trade imbalance and stop the bleeding of investments and jobs towards Mexico. The first page of the Summary of Objectives for the NAFTA Renegotiation (Office of the United States Trade Representative; July, 17 2017) registers it:

“The new NAFTA will be modernized to reflect 21st century standards and will reflect a fairer deal, addressing America’s persistent trade imbalances in North America.“

Still at the same time the U.S. is also putting forward labor provisions to “bring (them) into the core of the Agreement rather than in a side agreement.” It also calls to adopt and maintain ILO core labor standards, including Convention 98.

Interestingly, it proposes two additional measures that could purge Mexico´s sources of competitive advantage. They are currency mechanisms to “ensure that the NAFTA countries avoid manipulating exchange rates in order to prevent effective balance of payments adjustment or to gain an unfair competitive advantage.” And provisions “to criminalize government corruption.”

Canada's Foreign Affairs Minister Chrystia Freeland disclosed the country core objectives in terms of seeking a "progressive fairer trade regime." It includes:

"Labor standards: Commitments with respect to labor standards should be brought into the core of the agreement (…)."What is different is that Canada proposes to use the Trans-Pacific Partnership (TPP)' chapter on labor as a model.

Like the U.S. Canada wants to bring environmental standards within the core of the agreement, and put forward a set of issues to color its idea of a progressive agreement such as gender and indigenous rights, and transfer of professionals "so as to make the movement of professionals and business persons easier, to reflect the needs of cross-border trade and businesses."

Canada handles objectives as a response to TRUMP attempt to put "America first," which will be contemptuous and can lead to a dead-end road. Among others, they are government procurement (based on Canada-EU Comprehensive Economic and Trade Agreement) vs. U.S. "Buy America" provisions; investors state dispute settlement; and "non-negotiable" priorities including a firm opposition to U.S. attempt to remove Chapter 19 related to dispute settlement mechanisms to "preserve the ability of the United states to enforce rigorously its trade laws, including the antidumping, countervailing duty, and safeguards laws."[13]

There are other issues that can complicate negotiations as rules of origin, procurement, agricultural, services, etc. It is beyond the scope of this paper to assess them. What it is necessary to underline here is the Mexican position. Contrary to the above, Mexican representatives stick to the plan of resisting and avoiding that a single coma of the agreement change, and, as twenty-five years ago, they are upfront to fiercely oppose any attempt to include labor as a part of a new deal.

Nobody knows what is going to be the final results of NAFTA renegotiations. Still a new agreement with no core provisions related to labor standards, corruption practices, and international currency manipulation, as well as due mechanisms to enforce them, will be a lost opportunity to make things right in the NAFTA region. In

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[13] Osler, Riyas Datu et al., (August 15, 2017): "Canada unveils its top priorities for NAFTA renegotiations," online, https://www.osler.com/en/resources/cross-border/2017/canada-unveils-its-top-priorities-for-nafta-renego.

such scenery, Mexican state and private decisions makers will keep living in their comfort zone of a country rated as the workshop of the hemisphere. A jurisdiction supplied of needed investments and jobs by international capitals looking for further opportunities to remain competitive and penetrate American markets at the lowest cost. No matter what the consequences for development could be. For instance, the host country will be further falling under growing layers of inequality, poverty, and crime, while international investors' homelands witness the spoiling of their job prospects, earnings, and living standards.

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