From NAFTA to USMCA: Power, Path Dependence, and Protectionism

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By

Ludovic Arnaud

Lincoln College, Oxford

Oxford Department of International Development

University of Oxford

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Abstract

The North American Free Trade Agreement (NAFTA) shaped the preferences and available choices of negotiators and stakeholders during its renegotiation in 2017-19, leading to the United States-Mexico-Canada Agreement (USMCA). This thesis first examines the reasons behind the US demand for institutional change. Drawing on structuralist economics, it develops a typology of US trade policies since WWII based on the global South's access to the US market and policy space. US trade policy evolved from 'magnanimous' (1944-70) to 'competitive' (1971-1990) to 'restraining' (1991-2016) as the US reacted to disruptions caused by import competition. Since 2017, US trade policy globally has shifted to 'power-based' as a reaction to the restraining policy, symbolised by the WTO and NAFTA, which encouraged offshoring by stabilising access to the US market and restricting trading partners' policy space. Paradoxically, USMCA largely preserved US restraining policy regionally, although uncertainty is institutionalised by the inclusion of review periods and a sunset clause.

To understand the continuity between NAFTA and USMCA despite the Trump administration's radical negotiating objectives, this thesis then analyses the process of institutional change, drawing on over one hundred interviews. Historical institutionalism is integrated into the two-level game framework to understand the role of increasing returns and veto power in a trade renegotiation. Those two path dependence mechanisms were the main reason for US policy continuity as labour unions and members of Congress historically opposed to NAFTA defended the agreement against President Trump's disruptive strategy, while business groups lobbied to preserve the status quo. In Mexico, path dependence also constrained Mexican President López Obrador to endorse USMCA, despite his long-standing criticism of NAFTA and efforts to regain policy space. He instead used USMCA to lock in his ambitious labour reforms, just as NAFTA was used in the 1990s to lock in trade liberalisation.

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List of Abbreviations

AD/CVD	Anti-dumping and countervailing duties
AFL-CIO	American Federation of Labour and Congress of Industrial Organizations
AMLO	Andrés-Manuel López Obrador (Mexican President)
ASEAN	Association of Southeast Asian Nations
ATIP	Activist trade and industrial policies
BATNA	Best Alternative to a Negotiated Agreement
CBP	(US) Customs and Border Protection
CPTPP	Comprehensive and Progressive Trans-Pacific Partnership
CSIS	Centre for Strategic and International Studies
CETA	Comprehensive Economic and Trade Agreement (Canada-EU)
CUSFTA	Canada-United States Free Trade Agreement
CWA	Communication Workers of America
DSM	Dispute Settlement Mechanism
EOI	Export-oriented industrialisation
EU	European Union
FTA	Free Trade Agreement
GATS	(WTO) General Agreement on Trade in Services
GPA	(WTO) Government Procurement Agreement
GSP	Generalised System of Preferences
IMF	International Monetary Fund
IP	Intellectual Property
IPEF	Indo-Pacific Economic Framework
ISDS	Investor-State Dispute Settlement
ISI	Import-substitution industrialisation
IUST	Inside US Trade
KORUS	South Korea – United States Free Trade Agreement
LVC	Labour Value Content
MFN	Most Favoured Nation

List of Abbreviations

MNC	Multinational corporation
NAALC	North American Agreement on Labour Cooperation
NAFTA	North American Free Trade Agreement
NGO	Non-governmental organisation
NLRB	National Labour Relations Board
NTB	Non-tariff barrier
OEM	Original Equipment Manufacturer
PIIE	Peterson Institute for International Economics
PM	Prime Minister
PNTR	Permanent Normal Trade Relations
PRI	Partido Revolucionario Institucional (Institutional Revolutionary Party)
PTA	Preferential Trade Agreement
RCEP	Regional Comprehensive Economic Partnership
ROO	Rule(s) of Origin
RRM	USMCA Rapid Response (Labour) Mechanism
RVC	Regional Value Content
SOE	State-owned enterprise
SPS	Sanitary and Phytosanitary Measures
TBT	Technical Barriers to Trade
TPA	Trade Promotion Authority
TPP	Trans-Pacific Partnership
TRIMS	(WTO Agreement on) Trade-related Investment Measures
TRIPS	(WTO Agreement on) Trade-related aspects of Intellectual Property Rights
UAW	United Auto Workers
US	United States
USMCA	US-Mexico-Canada Agreement
USTR	United States Trade Representative
USW	United Steelworkers
VER	Voluntary Export Restraint
WTO	World Trade Organisation

Chapter 1. Introduction

> *There are a lot of provisions in USMCA that are precedent-setting and well outside the bounds of what has been agreed to in other trade agreements. The auto provisions as they are written now are much stricter than anything else that we've seen anywhere. The labour dispute settlement provisions are a lot more detailed, and the timelines are incredibly short, in a way that we haven't seen in a dispute settlement anywhere else.*
>
> John Melle, US chief negotiator, interview, 16 December 2020

> *It's important to understand the position that the US took from the beginning of the negotiation. It was clear that there would not be any deal and that the US would pull out of NAFTA unless there was a deal on autos. Why? Because the president was basically not interested in any of the other technical details of the agreement, he was interested in one thing in his mind: eliminating the trade deficit with Mexico.*
>
> Kenneth Smith Ramos, Mexican chief negotiator, Peña Nieto administration, interview, 16 October 2020

> *Our number one priority was to fix the dispute resolution system. It was the most important because Mexico has always had dispute problems with the United States and no mechanism to resolve it. We had to ask for favours. Well, the United States opposed that. Their response was that the fixing of the dispute settlement system was only acceptable on one condition: that we accepted a new clause that basically said that when a dispute is completed, any other government involved in the dispute has the right to veto the resolution. […] In the end, we created a proper dispute resolution system.*
>
> Jesús Seade, Mexican chief negotiator, López Obrador administration, interview, 15 October 2020

Thirty years ago, on 1 January 1994, the North American Free Trade Agreement (NAFTA) entered into force. In 2017, however, its future had become uncertain as US President Donald Trump threatened to withdraw the US from NAFTA unless Mexico and Canada accepted a renegotiated agreement containing his protectionist negotiating objectives. Trump blamed NAFTA for the US trade deficit with Mexico and the loss of US manufacturing jobs. His

campaign also focused on illegal immigration from Mexico, with inflammatory comments such as accusations that Mexican immigrants were criminals, and calls to build a wall between the two countries (Phillips 2017). Following his election in November 2016, Trump assumed the US Presidency on 20 January 2017. He immediately threatened to impose unilateral tariffs on Mexican imports and withdraw the US from NAFTA by executive decree.

On 18 May 2017, less than four months after his election, Trump formally notified the US Congress of his intention to renegotiate NAFTA, forcing the Mexican and Canadian governments to the negotiating table. The United States Trade Representative Office (USTR) published its negotiating objectives in July 2017, followed shortly by the Mexican and Canadian governments (USTR 2017a; Secretaría de Economía de Mexico 2017; Government of Canada 2017). While the Mexican and Canadian governments sought to modernise NAFTA and deepen trade liberalisation, USTR defied norms of trade agreement negotiations by proposing protectionist objectives including a five-year sunset (termination) clause, US-specific rules of origin for autos, and a sharp reduction in access to the US government procurement market. All three countries started negotiations on 16 August 2017. After Congressional hearings and the first rounds of negotiations, USTR published revised negotiating objectives in November 2017 (USTR 2017b). On 3 March 2018, the US began bilateral talks with Canada and Mexico.

In Mexico, the election of López Obrador as President in July 2018 also created trade uncertainty, as well as the need to coordinate negotiating positions with the outgoing Peña Nieto administration. López Obrador was the first left-wing Mexican President in over eighty years and had been historically critical of NAFTA and Mexico's repressive labour system. The Peña Nieto administration ensured that the incoming government was represented in the negotiations until the beginning of López Obrador's term in December 2018. On 27 August 2018, the US and Mexico reached a bilateral agreement (IUST 2018i). As Trump signalled his willingness to move forward without a deal with Canada, Canadian negotiators rushed back to the negotiating

table, culminating in a trilateral agreement on 30 September 2018. The first version of the US-Mexico-Canada Agreement (USMCA), known as Tratado Mexico-Estados-Unidos-Canada (T-MEC) in Mexico and the Canada-United States-Mexico Agreement (CUSMA), was signed on 30 November 2018.

After regaining control of the US House of Representatives during the December 2018 mid-term elections, however, Democrats conditioned passage of USMCA on progressive amendments, which led to the reopening of negotiations until a deal was reached on 10 December 2019. The Mexican government ratified the agreement two days later, followed by the US Congress on 16 January 2020 and the Canadian government on 13 March 2020 (Duchesne 2021: 20-26). Following ratification, the countries negotiated the implementation of the rules, including the interpretation of the new automotive rules of origin. The agreement entered into force on 1 July 2020. Despite Trump's protectionist agenda, USMCA largely preserved NAFTA provisions and strengthened North American economic integration.

Based on one hundred and eight interviews with negotiators and stakeholders, this thesis seeks to understand **how NAFTA shaped actors' preferences and power during the renegotiation process.** To explain the demand for institutional change, it builds a development-oriented typology of US trade policies since World War II (WWII) based on structuralist economic theory. To analyse the process of institutional change, it integrates historical institutionalism into the two-level game theoretical framework. This chapter first highlights the relevance of USMCA to future trade negotiations and details the puzzles which motivated this research. It then presents the theoretical framework and methodology and concludes with the thesis outline.

1.1. Why study USMCA?

1.1.1. Policy Relevance

Entering into force in 1994, NAFTA was the first North-South free trade agreement. It pioneered the logic of trade agreements through which countries in the global South relinquish space for industrial policy in exchange for stable and preferential access to markets in the global North (Shadlen 2008: 2). NAFTA had lasting implications for the regulation of world trade by setting a precedent for the rules of the World Trade Organisation (WTO), founded in 1995, and acting as a template for the numerous bilateral and regional trade and investment agreements that followed (Ibid.).

Similarly, USMCA will inform future trade negotiations across the world, although some of its provisions are likely to be replicated only in trade agreements involving the US (Gagné and Rioux 2022: 272). USMCA's unprecedented Rapid Response Labour Mechanism, aimed at addressing violations of collective bargaining and freedom of association in specific factories, inspired similar provisions in the Indo-Pacific Economic Framework (IPEF) (US Department of Commerce 2023). USMCA's provisions on currency manipulation, also unprecedented, were replicated in the US-China Phase One Agreement (2020). USMCA contains state-of-the-art chapters on digital trade, anti-corruption, and small and medium enterprises, among others, which have been used as templates by the US in its negotiations with other countries (Lighthizer 2023). Some provisions, such as the USMCA sunset clause and measures to prevent trading partners from signing a PTA with 'non-market' economies, are unlikely to be reproduced in PTAs not involving the US.

USMCA provisions reflect broader shifts in US trade policy rather than the will of the Trump administration alone. Democrats in Congress supported stricter auto rules of origin, the elimination of Investor-State Dispute Settlement (ISDS) between the US and Canada and its weakening between the US and Mexico, and blocked the extension of certain intellectual property rights. USMCA passed Congress with overwhelming support, reflecting bipartisan consensus over this new model (Gerstle 2022; Klein and Pettis 2020: 222). Within the US, the

consensus on trade policy shifted in 2017 from liberal to protectionist and has remained so under the Biden administration as Trump's approach echoed concerns raised historically by the left-wing of the US Democratic Party (Hillman and Tippett 2021; Hopewell 2021). Even within the Republican Party, which favoured free trade, Trump's protectionist policies have been mainstreamed given the overwhelming support for Trump in the Republican primaries for the 2024 presidential election (The Economist 2023).

Understanding the political economy of the NAFTA renegotiation enables a better analysis of the stakes in USMCA review periods, which will occur every six years from 2020, as well as the future of US trade policy. As the first trade agreement with a review and sunset clause, USMCA weakens the market access certainty historically provided by preferential trade agreements (PTAs). Other USMCA provisions also create uncertainty over Mexico and Canada's duty-free access to the US market, such as the stringent auto rules of origin which include, among others, the unprecedented requirement that at least 40-45 per cent of the value of a vehicle has to made by workers earning on average at least 16 dollars per hour. The competitiveness of the North American auto industry will be impacted by USMCA, which increases costs but also enables Mexico and Canada to benefit from US industrial policy, such as by receiving subsidies for electric vehicles financed by the Inflation Reduction Act of 2022. Beyond North American trade, USMCA will also impact trade outside the region, such as through its provisions dissuading PTAs with 'non-market economies' and its unprecedented labour provisions, including the ban on all imports produced by forced labour.

There is so far no overarching account of the NAFTA renegotiation process drawing on interviews with its actors and stakeholders. The literature has identified some of Trump's efforts to reduce market access for Mexico (Ciuriak 2019), detailed the new USMCA provisions (Gantz 2020; Gagné and Rioux 2022), and assessed the potential causes and impact of the renegotiation (Alvarez Medina 2021; Bersin and Long 2022; Blecker 2021; Bown and Claussen

2023; Burfisher, Lambert, and Matheson 2019; Ciuriak and Fay 2021; Gagné and Rioux 2022; Gantz 2020; Hershberg and Long 2023; Lilly 2023; Macdonald 2023; Manak 2022; Polaski 2023).[1] Bensusán and Middlebrook (2020) and Middlebrook (2024) draw on interviews focused exclusively on the renegotiation of NAFTA labour provisions but do not include accounts from the López Obrador administration, which accepted significant amendments to USMCA including the creation of the Rapid Response Labour Mechanism. The first research contribution of this thesis is to provide an analysis of the renegotiation process based on first-hand accounts. The theoretical contributions are now discussed.

1.1.2. Research Puzzles

Beyond the relevance of USMCA for policymakers, the renegotiation of NAFTA raised important questions for development studies and international political economy scholars. First, although countries in the global South should value policy space according to structuralist economic theory (to conduct activist industrial policies), the Mexican government favoured further policy space restrictions during the NAFTA renegotiation. President Peña Nieto (2012-2018) not only accepted new policy space restrictions but also proposed new ones. Following his victory in the 2018 elections, President López Obrador, who had campaigned for two decades against NAFTA (Watts 2019), decided to support all USMCA provisions except in the energy sector (although those were maintained in USMCA nevertheless), despite his objective of implementing activist industrial policies using Mexico's state-owned enterprises.

Second, despite the power asymmetry between the US and Mexico (but also Canada), the Trump administration was not able to impose its radical negotiating objectives. The Mexican

[1] For brevity, not all studies are listed. Think tanks and institutes published reports on the implementation of USMCA, including Brookings (2022, 2023), the Wilson Center (Bersin and Long 2022) and the Centro de Estudios Internacionales Gilberto Bosques (Chelminsky 2021).

economy has become much more dependent on trade since NAFTA: between 1993 and 2019, the share of total trade in Mexican GDP increased from 28 to 78 per cent (of which 80 per cent is with the US), whereas the share of trade in US GDP increased from 20 to 26 per cent during the same period (World Bank 2021b). In 2019, while approximately 80 per cent of Mexico's exports were destined for the US, 16 per cent of US exports were sent to Mexico. Despite this asymmetry, the Trump administration did not act on its threat to withdraw from NAFTA to gain concessions during the negotiations, even though it did not obtain any of its initial negotiating objectives such as a 50 per cent US-specific auto rule of origin, a five-year sunset clause, voluntary export restraints, 'dollar-for-dollar' government procurement, the elimination of all dispute settlement mechanisms, and the facilitation of trade remedies on agricultural imports.

Third, whereas most US labour unions and Congressional Democrats were opposed to NAFTA in 1992, they opposed a US withdrawal from NAFTA in 2016. In Congress, Democrats joined Republicans and the business sector in demanding that the Trump administration 'do no harm' to NAFTA. Many US labour union leaders, while sympathetic to Trump's objective of renegotiating the agreement to re-shore production to the US, did not want a US withdrawal from NAFTA. Although the President of the AFL-CIO, the largest US union, argued in 2019 that a US withdrawal from NAFTA would be helpful, he did so only at the end of the negotiations in the hope that the threat of a withdrawal would force the Mexican government to make further concessions on labour standards (Byrd 2019).

Fourth, whereas the Mexican government was opposed to including labour standards in NAFTA in the 1990s, it embraced enforceable labour standards in USMCA. The Mexican and Canadian governments supported the creation of an enforceable USMCA labour chapter, by contrast to the reticence of the Trump administration to accept dispute settlement mechanisms. Following the 2018 Mexican presidential election, the incoming López Obrador administration worked alongside the Trump administration on an annex to the labour chapter outlining

Mexico's domestic labour reforms, obtained improvements to the state-to-state dispute settlement mechanism to ensure enforceability, and accepted a Rapid Response Mechanism to incentivise compliance with rights to freedom of association and collective bargaining.

The four puzzles introduced above have a common theme: the preferences and power of actors opposed to NAFTA changed since the 1990s. This raises the overarching research question addressed by this thesis: **How did NAFTA shape actors' preferences and power during the renegotiation process?** This research question can be generalised to other PTA renegotiations. In the case of NAFTA, it can be subdivided into four sub-research questions focused on the four empirical puzzles:

1) Why did the Mexican government favour further constraints on its policy space during the NAFTA renegotiation?
2) Why was the Trump administration unable to implement its initial negotiating objectives despite US power asymmetry with Canada and Mexico?
3) Why were US labour unions and Democrats opposed to a withdrawal from NAFTA in 2017, in contrast to their position in 1992?
4) Why did the Mexican government support unprecedented labour provisions in USMCA?

To answer those questions, the thesis integrates historical institutionalism into the two-level game theoretical framework. The research also contributes to debates in the international political economy and development studies literature. The first sub-research question engages with the literature on the trade-off between policy space and market access in North-South trade agreements, whereby countries in the global South relinquish space for industrial policy in exchange for preferential and stable access to markets in the global North (Chang 2002; Shadlen 2005; Thrasher and Gallagher 2008). Throughout this thesis, the term 'structuralist economics' is used to encompass the different theories advocating for the global South's insertion into the

global economy using infant industry protection, including historical, global value chain and political economy approaches (Ibid.; Gerschenkron 1962; Hirschman 1958; Lin 2014; Prebisch 1949; Schneider 2013; cf. section 2.3). Although some of the scholars cited may not consider themselves 'structuralist economists', the term 'structural' is helpful to illustrate differences with the neoclassical school (cf. Chapter Two).

The second and third research questions speak to the literature explaining power paradoxes in international negotiations and the role of domestic politics in shaping international bargaining outcomes (Putnam 1988; Milner and Tingley 2015; Narlikar 2020; Jones 2013; Jones, Deere-Birkbeck, and Woods 2010). The fourth research question contributes to the debate over the protectionist vs developmental role of labour standards in PTAs, which USMCA labour standards render more salient given their unprecedented potential for both protectionist and developmental uses (Bhagwati 1995; Compa 2022; Polaski 2022). The conclusion reflects on the extent to which the theoretical framework can be generalised to other trade renegotiations.

1.2. Theoretical Framework

NAFTA was the first free trade agreement (FTA) to be renegotiated. Since the signing of USMCA in 2018, other FTAs have been renegotiated, such as the EU-Mexico and EU-Chile FTAs in 2020 and 2022. The NAFTA renegotiation was atypical, however, in that the Trump administration sought to reduce trade liberalisation. So far, the only other instance of efforts to increase protectionism during FTA renegotiations is EU-UK negotiations over Brexit, which led to the signing of the EU-UK Trade and Cooperation Agreement in 2020. This renegotiation differed from NAFTA, however, in that the UK government did not seek to undermine free trade with the EU, but rather to reverse deeper economic and political integration, such as freedom of movement, a customs union, and the role of the EU Court of Justice. The UK sought

to secure an FTA with the EU maintaining zero tariffs, which it obtained (although services are not fully liberalised due to the EU's refusal) (Institute for Government 2020). Theorising how a trade renegotiation differs from a trade negotiation is essential as an increasing number of countries are renegotiating their FTAs. This thesis does so by integrating historical institutionalism into the two-level game framework typically used in analyses of international negotiations.

1.2.1. Two-level Game

Negotiators of international treaties must find agreement both at the international level with their negotiating counterparts (Level I) and at the domestic level with the actors capable of vetoing the treaty (Level II). This was first formally theorised by Putnam (1988) in the two-level game framework. In addition to *negotiators' strategies* (Level I), two domestic factors (Level II) affect the size of 'win-sets' (number of agreements that can be ratified at Level II) and thereby negotiators' bargaining power: *political institutions* and *preferences of domestic groups* (Ibid.: 440-2; Conceição-Heldt and Mello 2018; Evans, Jacobson, and Putnam 1993; Milner 1997; Milner and Rosendorff 1997).

Following North (1990: 3), institutions are 'the rules of the game in society, or, more formally, are the humanly devised constraints that shape human interaction'. Political institutions such as ratification procedures influence negotiators' bargaining strength (Putnam 1988: 448-9; Mansfield, Milner, and Pevehouse 2008). Negotiators facing a complex ratification process can more credibly claim that they need concessions for the agreement to be ratified (P.B. Evans, Jacobson, and Putnam 1993: 409, 450). In 1992 just as in 2018, following the Democrats' victory in the midterm elections, US negotiators were able to extract concessions by claiming that such changes were necessary for the agreement to pass Congress (Mayer 1998; Cameron and Tomlin 2000). In both cases, the veto power of Congress improved US negotiators'

bargaining power. Veto players are 'individual or collective actors whose agreement is necessary for a change of the status quo' (Tsebelis 2002: 19).

The application of the veto-power literature to the two-level game framework has neglected two important scenarios. First, veto players in a negotiation can be only semi-veto players in a renegotiation: the power to approve or veto an international agreement does not guarantee the authority to veto the withdrawal from that same international agreement (Janusch 2018: 235). For instance, it is legally unclear whether a US President can withdraw from a trade agreement without authorisation from Congress. Second, although the two-level game literature often hypothesises that domestic veto players strengthen the bargaining power of their negotiators, they can also undermine negotiators' bargaining power if their interests are closer to the demands of negotiators from the other country (Tsebelis 2002: 308-11; Oppermann and Brummer 2018).

This leads to the second domestic factor identified by Putnam (1988) as influencing the bargaining power of negotiators: the preferences of domestic groups. Preferences are defined as the interests of an actor that determine how that actor ranks different outcomes (Frieden 1999: 42). Preferences of domestic groups can be homogenous or heterogeneous. In the latter case, the weaker country can find allies in the powerful country, which can lead to power paradoxes (Ibid.: 442-8). Economic integration increases the likelihood of transnational alliances between a weak state and interest groups in a strong state, such as US multinationals with operations in Mexico allying with the Mexican government to lobby the US government to maintain duty-free access to Mexican products. The power and commitment of domestic groups also matter. Large businesses with vital interests in a trade agreement invest more resources in lobbying and have more influence than small and depoliticised interest groups.

Similarly to the veto power literature, the literature on domestic preferences is better equipped to explain a trade negotiation than a trade renegotiation. Indeed, the three prevailing theories of

the impact of trade on preferences do not explain the second puzzle (RQ2) outlined above, namely that nearly all US business groups and labour unions (including those representing import-competing sectors and workers without tertiary education) opposed a US withdrawal from NAFTA during the renegotiation. The Heckscher-Ohlin model, which assumes perfect factor mobility, predicts that owners of the scarce factor in a country (labour in the US) should have supported a US withdrawal from NAFTA (Rogowski 1987; cf. Stolper-Samuelson theorem). The Ricardo-Viner model, which assumes that only labour is perfectly mobile, predicts that import-competing industries should have supported a US withdrawal from NAFTA (Krugman 2018). The Melitz model, which moves from factor analysis to the firm level, can explain US business groups' support for NAFTA through the lobbying power of large exporting firms in import-competing industries (Melitz 2003; Osgood 2017), but fails to explain US labour unions' reluctance to support a US withdrawal from NAFTA and many of Trump's protectionist proposals, by contrast to their opposition to NAFTA in the 1990s.

The literature on two-level games has vastly grown since Putnam (1988) to develop testable hypotheses, contrast rational choice and constructivist approaches, and identify other factors shaping bargaining outcomes, such as electoral uncertainty (P.B. Evans, Jacobson, and Putnam 1993; Milner and Rosendorff 1997; Milner 1997; Frieden 1999; Drezner 2002; Milner and Tingley 2015; Conceição-Heldt and Mello 2018). Milner (1997) and Milner and Rosendorff (1997) develop Putnam's framework into a fully-fledged theory with testable hypotheses. Yet their prediction that 'when the executive is the most hawkish, domestic politics has *no effect* on the international negotiations […] (and) the legislature cannot exercise any constraint on the executive' does not apply to a trade renegotiation (Milner 1997: 79). Mansfield, Milner, and Pevehouse (2007) incorporate veto player concepts into the two-level game framework. Drawing on a large dataset, they demonstrate that an increase in the number of domestic veto players reduces the likelihood of a preferential trade agreement (PTA) being signed. Although

this framework helps explain the legislative constraint faced by the Trump administration, its explanatory power is limited given that the preferences of veto players are treated as exogenous.

In their review of the literature, Conceição-Heldt and Mello (2018: 16) argue that 'two-level-games applications could profit from adding a temporal dimension to replace static analyses with historical, process-oriented perspectives'. Static analyses of institutions and preferences are especially problematic here as a renegotiation does not occur within the same political institutions as a negotiation. During the original NAFTA negotiation, Congress threatened to veto the passage of the agreement. In the NAFTA renegotiation, it threatened to veto an attempt by the executive to withdraw from NAFTA unilaterally. The preferences and strengths of domestic actors also changed since the original agreement. In Mexico, NAFTA led to a dramatic shift in economic structure towards exports and integration in global supply chains, which weakened the power of import-competing firms, such as in the pharmaceutical industry (Shadlen 2017: 231-32). To understand these changes, the two-level game framework needs to be complemented with an analysis of how NAFTA affected political institutions and actors' preferences. Historical institutionalism provides this analytical framework.

1.2.2. Historical Institutionalism

Historical institutionalism emphasises temporality: how past events and their consequences shape political processes (Fioretos 2011: 371). By contrast to rational choice traditions, which argue that actor preferences are determined by maximising long-term utility, historical institutionalists emphasise the immediate costs of breaking with past institutions, which can lead actors to favour continuity or incremental reform over radical change (Mahoney and Thelen 2010). This difficulty in reversing course is defined as path dependence (Fioretos, Falleti, and Sheingate 2016; Pierson 2000; Rixen and Viola 2016). Historical institutionalism

is compatible with more nuanced rational choice traditions, such as those emphasising bounded rationality (Jupille, Mattli, and Snidal 2013: 7, 35). By contrast to rational actors, boundedly rational actors search for satisfactory institutions rather than optimal ones. Given the costs and uncertainty of changing institutions, they support the status quo as long as it generates results above a minimum threshold (Ibid.: 35).

In their analysis of temporality, historical institutionalists traditionally focus on critical junctures, defined as 'events and developments in the distant past, generally concentrated in a relatively short period, that have a crucial outcome later in time' (Capoccia 2016: 89). Compared with domestic politics, international politics provides the advantage of more clearly identifiable critical junctures, such as the negotiation of international treaties (Zürn 2016: 217). The difficult passage of NAFTA through the US Congress in 1993 can be conceived as a critical juncture: although highly uncertain at the time, the entry into force of NAFTA changed the course of North American history by creating institutions and interests which would be difficult to reverse in 2017. A trade agreement is foremost an international treaty which binds countries' institutions through norms of compliance and domestic reforms. A trade agreement also affects domestic preferences by increasing trade and investment between members, thus magnifying disruption costs.

To avoid fuzziness and historical determinism, explanations based on critical junctures need to specify the stabilising mechanisms which created path dependence (Beyer 2010; Thelen 2004). Two stabilising mechanisms are retained here: *increasing returns* and *veto power*. In addition to economies of scale (Arthur 1989; David 1985), increasing returns is also used by political scientists to refer to situations where 'the costs of switching from one alternative to another will increase markedly over time' (Pierson 2000: 251). Political science has come to equate increasing returns to institutions: the more institutions are used, the more they are valuable in terms of providing reliability and predictability (Ibid.; North 1990; Beyer 2010). As to veto

power, it can cause path dependence by preventing change. Policy stability increases with the number of veto players, in particular when their preferences are heterogeneous and they are able and willing to use their veto power (Tsebelis 2002: 293-301). The relation between power and path dependence remains understudied and tends to focus on how power asymmetries beget power asymmetries, creating path dependence (Fioretos 2011: 377; Pierson 2015), rather than how path dependence can undermine power asymmetries, such as during the Trump administration's negotiations with Mexico and Canada.

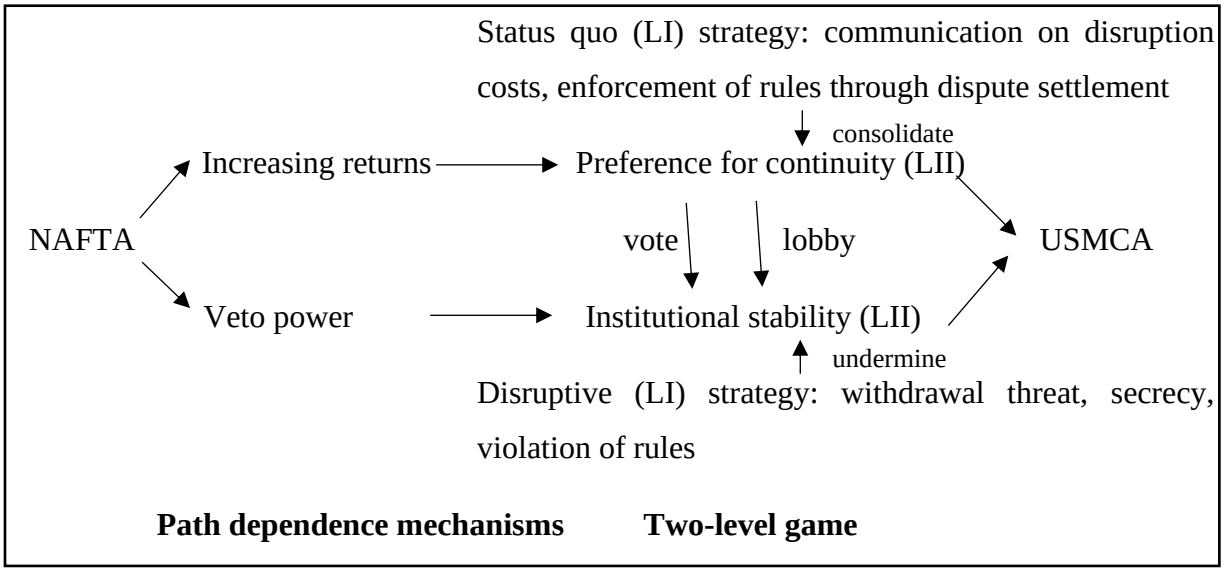
If historical institutionalism is to provide a full theory of institutional evolution, it must explain not only institutional continuity but also institutional change. To account for change, it is necessary to examine the distributional effects of institutions (Mahoney and Thelen 2010: 7). Institutions create winners and losers. Losers often do not go away, but 'live to fight another day, and they typically carry out this fight from *within* the institutions whose imposition they unsuccessfully resisted' (Thelen and Conran 2016: 64). When the institutional status quo no longer serves the preferences of powerful actors, institutional change becomes more likely (Jupille, Mattli and Snidal 2013: 7, 35). In the case of US trade policy, import competition repeatedly led to changes in the interests of powerful domestic actors, leading them to change existing institutions (Table 1 below).

1.2.3. Application to the NAFTA Renegotiation

Figure 1 schematises the model integrating historical institutionalism into the two-level game theoretical framework. While 1989 was the main critical juncture for Canada, with the entry into force of the Canada-US FTA (CUSFTA), it was 1994 in the case of Mexico and the US with the entry into force of NAFTA. Both CUSFTA and NAFTA were the product of leadership initiatives and faced strong domestic opposition in all three countries. In the US, NAFTA was

only adopted by a small margin following the addition of side agreements on labour and the environment. In Canada, newly elected Prime Minister Jean Chrétien had initially vowed to renegotiate NAFTA but gave his support after obtaining US guarantees (Milner 1997: 214). In Mexico, NAFTA sparked the Zapatista uprising in Chiapas. President Salinas of the incumbent PRI party had won the 1988 election against left-wing candidate Cuauhtémoc Cárdenas despite widespread allegations of fraud. This enabled the PRI to continue its economic liberalisation efforts, culminating in the locking-in of free trade policies through NAFTA.

FIGURE 1. MODEL OF THE NAFTA RENEGOTIATION



Source: Author's own.
LI: Level I, LII: Level II (two-level game framework).

Locking-in is achieved through a combination of veto power and increasing returns: withdrawing from a PTA typically requires joint support from the legislature and executive, and the costs of withdrawing increase as time passes and trade integration intensifies. The institutional reconfiguration gives some actors de jure (legislative, executive) or de facto (business groups) veto power over changes to the PTA. Veto power promotes institutional stability by undermining the possibility of a PTA withdrawal while increasing returns benefit PTA supporters, who accumulate more resources and have a greater incentive to defend the

status quo. Increasing returns to the PTA can change the position of actors who were originally opposed, and weaken their ability to affect change.

Although path dependence mechanisms (increasing returns, veto power) primarily act on domestic politics (Level II) by shaping preferences and institutions, they also shape negotiator strategies (Level I). Negotiators seeking radical change will adopt a disruptive strategy to overcome the path-dependent mechanisms undermining change, such as by threatening to withdraw from the PTA, violating obligations, and maintaining secrecy about their objectives to avoid domestic opposition. By contrast, negotiators attempting to preserve the status quo will communicate the costs of disruption and attempt to raise them. Given the strength of increasing returns and veto power in a PTA renegotiation, however, a disruptive strategy is more likely to result in the modest modification of the existing PTA than a withdrawal from the PTA.

The model in Figure 1 can be applied to answer the sub-research questions (RQ1-4). To understand the Mexican government's decision to embrace further policy space constraints during the NAFTA renegotiation (RQ1), it is necessary to analyse the constraints created by Mexico's development strategy. Since NAFTA, the Mexican government further locked in its policy space by negotiating numerous PTAs, including with Chile (1999), the European Union (2000), Japan (2005), Colombia (2011), and Israel (2012), among others. Following Trump's withdrawal from the Trans-Pacific Partnership (TPP) in 2017, Mexico signed the Comprehensive and Progressive TPP (CPTPP).[2] Changing Mexico's development strategy would have required not only opposing provisions in USMCA but renegotiating the other PTAs that Mexico was part of and its Most Favoured Nation (MFN) rates at the WTO. Given that Mexico's development strategy is built on guaranteeing investment certainty and market access, the Peña Nieto government embraced further policy space constraints in USMCA. Although

[2] TPP had been signed by President Obama in 2016 but had not been voted through Congress, which enabled Trump to withdraw from the agreement by executive decree.

Mexican President López Obrador was historically critical of NAFTA and free trade, he supported most changes given that the costs to Mexico of changing course were immense. Even in energy, where he actively sought to regain policy space, Mexico's prior commitments in CPTPP prevented any concrete changes.

Similarly, the model explains the Trump administration's inability to implement its initial negotiating objectives despite US power asymmetry with Canada and, especially, Mexico (RQ2). The veto power of Congress over a NAFTA withdrawal, although contested by the executive, undermined the Trump administration's leverage. More importantly, Trump needed the support of Congress to pass USMCA, leading in 2019 to amendments requested by Democrats which coincided with the demands of Mexican and Canadian negotiators, such as improving the functioning of the state-to-state dispute settlement mechanism. Just as in Mexico and Canada, NAFTA also generated increasing returns in the US, such that the US economy would have been significantly affected by a withdrawal. The US business sector lobbied successfully to moderate the Trump administration's radical objectives. Even US labour unions and Congressional Democrats, who opposed NAFTA in 1992, rejected a withdrawal in 2017 given the costs of doing so (RQ3). As to the Mexican and Canadian governments, they sought to preserve the status quo by communicating on disruption costs and using the dispute settlement mechanisms to retaliate strategically against US unilateral steel and aluminium tariffs.

The mechanisms at play in the model also help explain the Mexican government's support for the unprecedented labour provisions in USMCA (RQ4). The Peña Nieto government wanted to reflect in USMCA the stronger labour commitments that Mexico had negotiated in previous PTAs, including most recently CPTPP. The López Obrador government went further, however, by seeing in USMCA an opportunity to lock in its ambitious labour reform agenda, just as NAFTA was used in 1992 to lock in economic liberalisation. Officials in the López Obrador

administration had been proposing a labour reform for decades while in opposition. They worked with USTR to include the reform in the Annex to the USMCA labour chapter, thereby rendering the trade and investment benefits of USMCA conditional on the reform being voted and implemented. Even the Rapid Response Mechanism, criticised by the Peña Nieto government, was seen by López Obrador as a helpful mechanism to force reluctant firms to comply with the labour reform and open space for independent unions.

Beyond explaining the process of institutional change, it is necessary to explain the demand for institutional change. Economic disruption caused by the economic development of US trading partners, most notably China, raised protectionist sentiments in the US. The second and third chapters draw on structuralist economics to explain how import competition shaped demands for change in US trade policy since World War II (WWII), focusing on two dimensions of change in US trade policy affecting economic development opportunities in the global South: the level of access to the US market and US tolerance for trading partners' industrial policies. Table 1 outlines the evolution of US trade policy as a result of import competition.

TABLE 1. EVOLUTION OF US TRADE POLICY

	Magnanimous	Competitive	Restraining	Power-based
Period	1944-70	1971-90	1991-2016	2017-
Policy objective	Develop US allies	Protect domestic industry	Create export platforms abroad	Re-shore production
Access to the US market	Open	Uncertain	Open	Uncertain
Tolerance of others' ATIP*	Authorised	Authorised (but challenged)	Restricted	Restricted

*ATIP: Activist trade and industrial policies

Source: Author's own.

Analysing US trade policy since WWII enables an investigation of the relevance of historical institutionalist concepts before NAFTA. Even though US policymakers were not constrained by PTA commitments until the late 1980s, they did not implement radical trade policy changes

but rather adapted to the constraints imposed by previous trade policies, such as membership of the GATT. US trade policy post-WWII created stronger international economic integration which impeded a return in the 1970s to the protectionist policies of the 1920s, despite important trade shocks (Milner 1988). The US government instead implemented a new form of protectionism in the 1970-80s based on creating market access uncertainty. Similarly, a return to the 1970-80s approach in 2017 was unlikely due to the costs of disrupting the supply chains created by the US policy of negotiating PTAs in the 1990s and 2000s. Just as constraints on US trade policy led to a 'new protectionism' in the 1970s-80s based on non-tariff measures (NTMs) and market access uncertainty, constraints on US trade policy led the Trump administration to develop a more subtle form of protectionism based on review periods, labour rules, and stronger regionalism.

1.3. Methodology

1.3.1. Process Tracing

As in most other historical institutionalist analyses, process tracing is the method chosen given its usefulness in identifying causal mechanisms within a single case study (Fioretos, Falleti, and Sheingate 2016; Rixen and Viola 2016). Process tracing was conducted through a detailed analysis of the sequence of events and accounts of the negotiation process. Analysing the sequence of events helps identify which possible explanations are plausible. For instance, analysing the sequence of events provided a tentative explanation for Trump's decision not to withdraw the US from NAFTA on the hundredth day of his presidency. Although Trump announced that his phone calls with President Trudeau and Peña Nieto were determinant, he had been presented a few hours before with a map of US states hardest hit by a NAFTA

withdrawal, which were mostly Republican. The timing of his decision indicated that the economic costs of a US withdrawal from NAFTA were a key factor shaping his decision.

Relying on the sequence of events alone leaves the causal mechanism as a black box and thus does not amount to process tracing (Beach and Pedersen 2019). Keeping with the previous example, drawing on first-hand accounts of the negotiation process allows for a more complex explanation: President Trump was initially committed to withdrawing from NAFTA but did not do so through a combination of factors, including White House officials preventing or dissuading him from doing so (Woodward 2018), lobbying by the business sector and members of Congress, and the concessions of Mexican negotiators on auto industry rules of origin. Interviewees go beyond descriptive analyses of sequences by providing their account of the causal mechanisms at play.

To ensure that the causal mechanisms identified through process tracing are clearly stated, a model (Figure 1 above) outlines the theoretical argument defended (Büthe 2002). Providing a model of the causal mechanism helps distinguish the parts of the explanation that are most important to the overall outcome. For instance, although some White House officials initially deceived Trump not to withdraw from NAFTA by removing presidential decrees from his desk (Woodward 2018: 233), deception was not a long-term factor in his decision not to withdraw and his administration's inability to include their initial objectives in USMCA. Modelling history facilitates the identification and testing of an explanation by other researchers, as well as distinguishing the context-specific from the generalisable (Büthe 2002; Sewell 1996: 270).

1.3.2. Sources and their Analysis

The sources used in this research can be classified into three main types: official documents, elite interviews, and media coverage. The sources and the methods used to analyse them are outlined below. Further information is included in the Annex.

Official documents

The research draws on the NAFTA and USMCA texts to conduct a detailed comparison of key changes. It also refers to other trade agreements such as the Trans-Pacific Partnership (TPP), which was set in 2016 to *de facto* replace NAFTA as Mexico, the US and Canada were signatories. Although President Trump withdrew the US from TPP in 2017, the trade agreement remained relevant as many provisions in USMCA were copied from TPP, reflecting the negotiating work undertaken over eight years.

In Chapter Four, which contains a section comparing Mexico's policy space and market in NAFTA and USMCA, the analysis focuses on both *de jure* and *de facto* changes. This is because the content of a trade agreement alone is insufficient to determine the restrictions on policy space and stability of preferential market access provided by a trade agreement. Certain actions by a trading partner can increase uncertainty over market access, such as threatening to withdraw from an agreement or to unilaterally impose trade barriers. Late-industrialising countries may also restrict their policy space further than their legal obligations due to pressures from trading partners, such as threats of losing preferential market access, facing expensive legal action, or not receiving foreign aid (Wade, 2003). While the analysis of *de jure* changes in market access and policy space is conducted by comparing the original and revised trade agreements, the *de facto* changes are identified by drawing on the additional sources detailed below.

Aside from the NAFTA and USMCA legal texts, official documents used include the September and November 2017 list of negotiating objectives published by USTR, as well as the list of negotiating objectives provided by Mexico and Canada (USTR 2017a, 2017b;

Government of Canada 2017; Secretaría de Economía de Mexico 2017). The research also draws on letters sent by government organisations, in particular between USTR and Congress members, as well as communiqués published by businesses and labour unions.

Elite interviews

The author conducted one hundred and eight interviews with negotiators, stakeholders, and experts of the NAFTA renegotiation process (cf. Annex). A first round of eighty interviews was conducted online between September 2020 and December 2021 due to the COVID-19 pandemic. As negotiations of the USMCA text and its interpretation ended in December 2019 and June 2020, respectively, respondents had a fresh memory of the events that unfolded. The author conducted a second round of interviews from March to June 2023 while in Washington D.C., which also provided insights on the implementation of USMCA in its first three years. Interview respondents included Trump administration negotiators, US Democratic Party officials, members of the Peña Nieto and López Obrador governments, Canadian negotiators, business and labour representatives, and experts.

The interviews were conducted following the principles of saturation and triangulation. Saturation consists of conducting interviews until no new information is obtained from additional respondents to maximise the probability of collecting all rival accounts (Bennett and Checkel 2014). Triangulation entails comparing the data obtained from different sources to ensure the information provided is accurate. The number and diversity of respondents interviewed, including negotiators, policymakers, experts, and business and labour elites in all three countries, facilitated this process. Triangulation was also possible by consulting other types of sources, in particular the legal texts of the agreement and media coverage of the negotiations. When contradictions were encountered between different sources, respondents were invited to clarify their comments. Together, triangulation and saturation mitigated the risk of incorrect causal inference from interview data (Mahoney 2010; Rathbun 2008).

The interviews were conducted to allow for both positivist and interpretivist methodologies. While a positivist methodology favours the collection of facts rather than opinions, facts alone are insufficient to analyse a negotiation process, which typically involves pressure tactics and interpersonal relations. Furthermore, certain variables of interest, such as levels of market access uncertainty and *de facto* policy space, are based on policymakers' and other stakeholders' opinions. In addition to the events that unfolded, interview respondents were also asked about their perception of the negotiation process and provided with opportunities to raise unexpected issues (Mosley 2013; Piore 2006). The latter was particularly important to understand issues which had not been considered and ensure the author's theoretical lens did not condition interview responses.

Media coverage

The research draws on press coverage from a range of media outlets, in particular the specialised news agency *Inside US Trade* (IUST). The author reviewed over two thousand articles on the NAFTA renegotiation published by IUST between September 2016 and July 2020, which provided detailed information on the negotiation process and enabled further triangulation of information provided by interview respondents. Some negotiators and stakeholders wrote columns in newspapers and participated in radio, television and podcast interviews, including Mexican chief negotiators Kenneth Smith Ramos and Jesús Seade, Canadian chief negotiator Steve Verheul and USTR Lighthizer (cf. Annex). USTR Lighthizer also published articles explaining the Trump administration's trade policy in *Foreign Affairs* and *The Economist* (Lighthizer 2020, 2021), as well as in a book (Lighthizer 2023). Jared Kushner, Senior Adviser to President Trump, wrote a memoir which includes a chapter on his role in the NAFTA renegotiation (Kushner 2022). Books on the inner workings of the Trump administration, written by journalists Bob Woodward (2018) and Michael Wolff (2018), were also consulted.

1.3.3. Limitations

Historical institutionalist works are mostly developed inductively through detailed analyses of case studies rather than deductive reasoning generating testable theories, which can generate several limitations. First, some of its explanatory concepts, such as increasing returns, have sometimes been vaguely defined and invoked rather than meticulously proven (Pierson 2004: 72; Thelen and Conran 2016). The theoretical framework and empirical chapters address this concern by defining and detailing the causal mechanisms at play. Second, and relatedly, the thick descriptions and context-specific analyses characteristic of historical institutionalism undermine generalisability. In several chapters and particularly in the conclusion, the analysis addresses this issue by comparing the NAFTA renegotiation to other trade agreement renegotiations and identifying the factors which can overcome path dependence mechanisms. Third, the lack of testable hypotheses limits confidence in the results and the predictive power of historical institutionalism. Based on the NAFTA renegotiation and other trade renegotiations, the concluding chapter provides three hypotheses to be tested in future research. Historical institutionalism is best at explaining the past, although combining it with insights from rational choice institutionalism improves its predictive power (Jupille, Mattli, and Snidal 2013; Zürn 2016). As such, the thesis draws on self-interested motivations (instead of norm-driven) given that the Trump administration pushed for an 'America First' agenda, breaking with past norms of trade liberalisation.

This single case study remains susceptible to incorrect inference due to incomplete information or reasoning errors. Confidence in the results of this analysis will have to be tested by the presence or absence of contradictory evidence, gathered from sources unused or inaccessible in this study. In particular, despite all the evidence accumulated, it is difficult to evaluate the extent to which the Trump administration was committed to all its stated negotiating objectives or rather used them as negotiating ploys to obtain more narrow concessions. As chief US

negotiator John Melle remarked, negotiators 'do not want the other states to know what their goals are' (interview, 16 December 2020). For this reason, the research relies on the (often anonymous) interviews of negotiators gathered after the renegotiation rather than their statements during the renegotiation or the negotiating objectives published by USTR in September and November 2017 to meet its legal requirement to inform Congress.

Online interviews can be less informative than in-person interviews if the lack of physical contact or visualisation of body language undermines the respondent's trust. This can also occur if the respondent is not certain of the confidentiality guarantees provided by an online interview (Janghorban, Roudsari, and Taghipour 2014). Online interviews can also prevent the researcher from observing non-verbal cues, such as the body language of the respondent or the environment in which the interview takes place, commonly referred to as metadata (Lo Iacono, Symonds, and Brown 2016). These concerns were not very relevant to this research for several reasons. First, certain types of metadata, such as the environment in which the interview took place, carried little value in this research focused on the events that unfolded. Non-verbal cues of interest, on the other hand, were well transmitted online. For instance, several respondents used pauses, facial expressions, and laughter to transmit a clearer message. As to respondents' trust in the confidentiality of the interviews, this was attenuated by the fact that many respondents agreed to speak on the record. The notable exceptions are US and Canadian negotiators, who mostly chose to speak off the record. Many respondents speaking off the record provided politically sensitive details on the negotiation process which were verified through triangulation, suggesting that trust was not an issue.

'Theory is always for someone and for some purpose' (Cox 1981: 128). As a thesis in international development, the analysis is driven by a concern for how policies in the global North affect development opportunities in the global South. It draws on structuralist economics, which remains marginalised in many economics departments but has become mainstream in

policy circles since 2017 due to geopolitical rivalries, supply chain disruptions caused by the COVID-19 pandemic, and domestic discontent over income inequality and job quality. Although the reader should keep those frameworks in mind, they should also know that interview respondents' emphasis on path dependence is reflected throughout the analysis, which led the author to reconsider the feasibility and effectiveness of traditional structuralist economic policies.

1.3.4. Ethics

The main ethical concern during this research was not to harm the interests of interviewees. Interviews were conducted with elites, including trade negotiators, politicians, Congressional staff, and business and labour representatives. This required ensuring that sensitive information provided confidentially could not be traced back to the person. Each respondent was given the choice of speaking anonymously. To ensure confidentiality, the transcripts of the interviewees were anonymised and protected by a password, and the list associating each interviewee with the corresponding transcript number was hand-written and stored in a separate location. Respondents who chose to speak anonymously are referred to by a generic title (for instance: 'Mexican negotiator'). The methodology was approved by Oxford University's Research Ethics Committee.

1.4. Thesis Outline

Part I, consisting of chapters two, three and four, draws on structuralist economics to explain the *demand for change* leading to the NAFTA renegotiation. Chapter Two contrasts neoclassical and structuralist economists' predictions of NAFTA's effects, and argues for the structuralist interpretation in light of NAFTA's impact on the Mexican economy. North-South

PTAs can be interpreted from a neoclassical or structuralist logic. Neoclassical economists argue that such PTAs contribute to economic development in both the North and South by increasing economic efficiency and reducing investment uncertainty. Structuralists, however, contend that those PTAs undermine long-term development by restricting the global South's space to implement activist trade and industrial policies. Following a neoclassical logic, NAFTA was passed through the US Congress in 1993 with the promise that it would lead to wage convergence between Mexico and the US. Twenty-five years later, however, real wages in Mexico were lower than in 1993 (Blecker 2019: 160-1). Although many other factors are at play, including competition from China and wage repression, structuralist economics provides important insights into the Mexican economy's failure to catch up.

Chapter Three develops a typology of the global North's trade policies, from which it identifies four eras of US trade policy since WWII leading to different developmental impacts on trading partners. From a structuralist logic, the global North can best promote economic development in the global South by providing 1) open and stable market access and 2) space for the global South's activist trade and industrial policies. From this can be created a 2x2 typology of US trade policy. Following WWII, the US pursued a 'magnanimous' trade policy consisting of supporting allied economies through access to its market while tolerating their protectionist policies. From 1971, a victim of the success of its previous policy, the US shifted to a 'competitive' trade policy to protect domestic producers from import competition. While allies continued to conduct activist industrial policies, access to the US market became less stable but not less open given that economic integration created path dependence. NAFTA and the creation of the WTO marked the transition towards a 'restraining' trade policy as the US restricted trading partners' policy space in exchange for stable access to its market. This policy was condemned by Trump for offshoring jobs given that it incentivised firms to create export

platforms abroad. Since 2017, US policy shifted to 'power-based' as the US undermined stable access to its market while maintaining restrictions on trading partners' industrial policies.

Chapter Four evaluates the extent to which the NAFTA renegotiation indicated a shift in US trade policy towards its neighbours. While the Trump administration pursued a 'power-based' trade policy globally and during the NAFTA renegotiation, by signing USMCA it largely maintained the 'restraining' trade policy towards Mexico and Canada. Market access certainty was restored, although the USMCA sunset clause facilitates a return to a 'power-based' trade policy during USMCA review periods. USMCA further restricted Mexico's policy space, which was already severely curtailed by NAFTA. This was welcomed by Mexican negotiators given that the country's policy space was already tied by other PTAs and that policy space restrictions were necessary to promote investment certainty. Path dependence undermined the structuralist logic that increases in policy space necessarily help promote economic development.

Part two, consisting of chapters five, six and seven, draws on historical institutionalism and the two-level game framework to explain the *process of institutional change* from NAFTA to USMCA. Chapter Five focuses on the renegotiation process over ten negotiating objectives pursued by the Trump administration which were described as 'red lines' or 'poison pills' by the Mexican and Canadian negotiators, as well as President Trump's repeated threats of unilaterally withdrawing the US from NAFTA unless he reached his negotiating objectives. It demonstrates that the Trump administration did not obtain any of its ten negotiating objectives in their original form, while half were included in a severely weakened form in USMCA. Despite this, Trump did not act on his threat to withdraw the US from NAFTA to gain leverage in the negotiations. The chapter concludes by providing evidence that Trump and high-level officials in his administration, most notably USTR Lighthizer, were not bluffing: they were determined to achieve those ten negotiating objectives.

Chapter Six explains the power paradox: even though the Trump administration was committed to radical negotiating objectives and benefited from US power asymmetry with Canada and especially Mexico, it was unable to implement its initial negotiating objectives. It argues that NAFTA led to changes in actor preferences and political institutions, which undermined radical change. First, increasing returns from North American economic integration led to strong opposition from US businesses and Congress to Trump's agenda, while even labour unions, which were historically opposed to NAFTA, argued that withdrawing was undesirable given the high costs. Second, the passage of NAFTA in the US Congress generated veto power as, even though Trump could have probably withdrawn from NAFTA by unilateral decree, he needed Congressional support to repeal the NAFTA implementation bill and pass USMCA. Electoral competition and the influence of civil society on government further reinforced path dependence as the Republican Party worried about the electoral effects of trade disruption and the business sector successfully lobbied the Trump administration to 'do no harm'.

Chapter Seven argues that USMCA labour provisions were supported for different reasons by the US and Mexican governments. Faced with the difficulty of overhauling NAFTA, the Trump administration sought to incentivise manufacturing production in the US through the creation of a Labour Value Content auto rule of origin and an annex to USMCA specifying that Mexico must implement its labour reform. Following their victory in the December 2018 midterm House elections, Congressional Democrats pursued similar protectionist objectives by conditioning passage of USMCA through Congress on mechanisms to enforce labour standards, including a Rapid Response Mechanism (RRM). In Mexico, whereas the Peña Nieto government was reticent to accept the RRM and other unprecedented labour provisions, President López Obrador accepted them as a means to lock in his ambitious labour reform. In their first three years, USMCA labour provisions contributed to limited improvements of labour conditions in Mexico's export sector without reducing access to the US market, which can be

explained by a combination of US political will to raise RRM cases and support Mexico's labour reform, Mexican political will to address those cases, and the auto industry's successful lobbying efforts to ensure that the Labour Value Content rule of origin would not undermine investments in Mexico.

Chapter Eight concludes by summarising the argument, highlighting the main research contributions, identifying the future research agenda, and providing policy reflections based on the findings. The three main research contributions are: providing the first overarching account of the NAFTA renegotiation based on primary sources, identifying changes in the market access – policy space trade-off characteristic of North-South trade agreements, and integrating historical institutionalism into the two-level game framework to understand how NAFTA shaped power and preferences during its renegotiation. The future research agenda consists of developing the theoretical framework into a theory of PTA renegotiations and assessing the implications of the latest shift in US trade policy for the global trade regime. As other large economies copy US protectionist policies, countries in the global South not part of regional economic blocs will face lower market access. Paradoxically, Mexico's biggest return on investment from joining NAFTA is occurring after NAFTA.

PART I – DEMAND FOR INSTITUTIONAL CHANGE

Chapter 2. The Promises of NAFTA

> *The original promise of NAFTA was that wages in Mexico and the United States are going to converge. They're going to come together. That didn't happen when NAFTA came into effect. The peso fell immediately and wages never converged.*[3]
>
> Trump administration official, interview, 10 March 2021

> *There was a sense that the NAFTA deal was toothless with regard to labour and the environment, that we had to remedy those failed promises. The fact that the rules are now within the trade agreement rather than outside is symbolically very powerful.*
>
> Congressional Democrat official, interview, 23 October 2020

2.1. Introduction

Most neoclassical economists argue that free trade agreements (FTAs) promote economic development by increasing efficiency, locking in market reforms and incentivising foreign direct investment inflows (Heydon 2020). Structuralist economists, however, contend that this view does not account for the way many countries industrialised, which involved activist trade and industrial policies (Aiginger and Rodrik, 2020; Chang and Andreoni, 2020). Successful late industrialisers such as Japan, South Korea, Taiwan, and China temporarily protected their infant industries with tariff barriers until they were productive enough to compete in international markets. They also resorted to policies aimed at transferring foreign technology to domestic firms, such as through foreign investment requirements and weak intellectual property protection. By contrast, FTAs restrict the use of such industrial policies by eliminating tariffs, banning most requirements on foreign investment, strengthening intellectual property rights,

[3] Although Mexico's nominal exchange rate depreciated compared to the US dollar between 1994 and 2016, Mexico's real effective exchange rate (REER) appreciated between the early 2000s and 2016 (Blecker 2022).

and restricting state intervention in the economy (Shadlen 2005; Thrasher and Gallagher 2008). From the structuralist perspective, North-South trade agreements involve a trade-off: countries in the global South obtain the short-term benefits of stable preferential market access to the North in exchange for the long-term cost of restricting their policy space for activist trade and industrial policies (Chang, Irfan, and Hauge 2016; Shadlen 2005, 2008).

After outlining the politics that led to NAFTA's ratification in 1994, the chapter presents neoclassical and structuralist theories advocating for free trade and ATIP, respectively, and reflects on the historical evidence. It draws on the structuralist interpretation to argue that the logic of North-South PTAs is for countries in the global South to restrict their policy space for ATIP in exchange for stable preferential access to markets in the global North. It then contrasts the predictions of neoclassical economic models in the early 1990s of minimal disruption costs in the US and economic convergence between Mexico and the US with the reality in 2016: long-term wage declines for US workers who faced import competition from Mexico and economic divergence between the US and Mexico. It concludes that structuralist economics provides important insights into the Mexican economy's failure to catch up, while an analysis of the China shock is necessary to understand attitudes towards NAFTA in the US. The failed promises of NAFTA contributed to the election of Trump and López Obrador as US and Mexican presidents.

2.2. The Road to NAFTA

Throughout most of the twentieth century, Canadian and Mexican governments were opposed to signing a PTA with the United States. They feared that further dependence on the US economy would increase power asymmetries with the US government in future negotiations (Krasner 1985: 55; McLaren 1997). Economic integration occurred through smaller steps, such

as the Maquiladora Industrialization Program from 1964 at Mexico's northern border, which enabled producers to import inputs duty-free as long as the final good would be exported, and the US-Canada 1965 Automotive Pact.

Canadians rejected a PTA with the US in the 1911 presidential election by voting for the Conservative Party, which had campaigned on a protectionist and anti-American platform. Between 1935 and 1984, Canada and the US negotiated some tariff liberalisation which targeted specific sectors, most notably autos. By the early 1980s, however, the proliferation of US protectionist policies incentivised Canadian businesses to support a PTA with the US (Doern and Tomlin 1991). Conservative Prime Minister Mulroney (1984-93) seized on the growing appeal of free trade to differentiate himself from the Liberal Party's interventionist policies, which had been implemented by Prime Minister Pierre Trudeau. Reagan accepted Mulroney's proposal to negotiate and by 1987 the Canada-US FTA (CUSFTA) was signed, liberalising nearly all tariffs between the two countries, with exceptions for Canada's agricultural supply management system and cultural industry. The deal also included the creation of an antidumping and countervailing duties dispute settlement mechanism to enable Canada to contest the liberal use trade remedies by the US. The 1988 Canadian election was mostly fought over CUSFTA and won by the Conservatives, which enabled Mulroney to ratify the agreement.

In Mexico, governments pursued an import substitution industrialisation (ISI) policy until the early 1980s, consisting of imposing high tariffs on imports and local content requirements on foreign investment. Mexican Presidents did not wish to sign a trade agreement with the US, which would only increase their dependence (Ojeda 1976; Selee 2018). By the 1970s, however, Mexico's development model was contributing to a balance of payments crisis. Taking advantage of the high price of oil and the global financial sector's abundance of petrodollars in the 1970s, President Luis Echeverría (1970-76) embarked on a public spending spree financed by dollar-denominated debt borrowed at floating interest rates (Pastor 2011: 53-55). From 1980,

however, US Federal Reserve Chair Paul Volcker sharply increased interest rates to tackle domestic inflation, up to 20 per cent in 1981. By 1982, Mexico was no longer able to service its debt and defaulted. Just two years earlier, President López Portillo (1976-82) had maintained Mexico's historical stance towards the US by dismissing President Reagan's idea of negotiating a North American FTA and abandoning the project of joining the General Agreement on Tariffs and Trade (GATT).

The 1982 financial crisis lasted until the end of the decade when the 1989 Brady Plan enacted sufficient debt restructuring to enable Mexico to recover economically. As part of its structural adjustment commitments, the Mexican government progressively introduced market reforms in the 1980s (Lustig 1992). Following unilateral tariff liberalisation, Mexico joined the GATT in 1986. By 1990, however, Mexico still faced balance of payments constraints. Given that trade liberalisation and market reforms did not incentivise sufficient capital inflows by themselves, President Salinas de Gortari first attempted to convince Western European countries to invest in Mexico (Cameron and Tomlin 2000: 1-5). They were not interested, however, given their focus on German reunification and the European project. As a last resort, Salinas turned to the US and proposed to negotiate a bilateral trade agreement. The Bush Sr. administration agreed and was later joined by the Canadian government which faced domestic opposition to free trade but did not want to lose influence over US trade policy. The result was the North American Free Trade Agreement (NAFTA), signed in 1992 and ratified in 1993 after the inclusion of labour and environmental side agreements.

Entering into force on 1 January 1994, NAFTA eliminated most tariffs between the US, Mexico, and Canada immediately, while others were phased out within ten or fifteen years, such as certain US agricultural exports to Mexico. In Mexico, the agreement locked in President Salinas' market reforms and faced strong opposition from labour unions, peasants, the left-wing party (PRD), protected industries in the centre of the country, and even from Salinas' party

(Poitras and Robinson 1994). On the day NAFTA entered into force, an armed uprising began in the southern state of Chiapas and was suppressed militarily. In Canada, the agreement was opposed by labour unions and parts of the Liberal Party (Milner 1997: 214). Its leader, Jean Chrétien, vowed to renegotiate NAFTA if elected. When his party won a landslide election in 1993, ratification of the agreement was put in doubt and only passed after assurances from the US government (Ibid.).

The agreement also faced strong opposition from within the US. President Clinton won the 1992 election by focusing on economic welfare. On NAFTA, he took a middle ground between Bush Sr.'s support for NAFTA and independent candidate Ross Perot, who warned of a 'giant sucking sound' of US jobs leaving for Mexico should NAFTA enter into force (Mayer 1998: 167). Clinton conditioned the passage of NAFTA on the inclusion of labour and environmental side agreements, which were negotiated in 1993. Even with those, however, Clinton faced an uphill battle to convince Democrats in Congress to vote for NAFTA in the face of vocal opposition from labour unions, environmental groups, and protected industries such as textiles and seasonal agricultural producers. NAFTA passed in the US Congress by a slim margin, helped by side payments and last-minute concessions including a worker retraining programme, the creation of a North American development bank, an environmental commission, and promises of continued subsidisation of certain industries (Mayer 1998; Milner 1997: 213-14).

Politicians and economists in the US, Mexico and Canada praised the benefits of free trade and market reforms in terms of economic growth, development, and regional competitiveness (Hufbauer and Schott 1992; Mayer 1998). President Clinton hosted former US presidents and Nobel laureate economists at the White House to launch his campaign to ratify NAFTA. The likely effects of NAFTA were analysed by numerous neoclassical economic models which concluded that the trade agreement would cause minimal disruption costs in the US and promote, if accompanied by other market reforms, economic convergence between Mexico and

the US (see Hufbauer and Schott 1992 for a review). By contrast, structuralist economists warned that policy space restrictions would undermine economic convergence. The next section details this debate.

2.3. Neoclassical vs Structuralist Theory

2.3.1. Theories of Trade and Development

The neoclassical and structuralist schools draw on two different theories of trade, static and dynamic comparative advantage, leading to two different recommendations for trade policy in the global South: free trade and infant industry protection. The prevailing view amongst most neoclassical economists is that free trade is conducive to economic development in all countries because it increases economic efficiency (Heydon 2020: 7; Krugman 1987: 131-2; Wolf 2004; Bhagwati 2004; Aistleitner and Puehringer 2021). Preferential trade agreements (PTAs) are considered conducive to economic development, provided that trade diversion inefficiencies (trade displacement from high-productivity countries external to the PTA to lower-productivity countries within the PTA) do not outweigh efficiency gains from trade liberalisation (Viner 1950). Removing tariff and non-tariff barriers to trade forces protected domestic firms to compete with foreign firms, thereby pressuring them to reduce their costs and increase the quality of their products. In a Darwinian process, only competitive firms survive trade liberalisation. Failing ventures free resources, such as labour and capital, which are then accessible to more productive firms. By opening export markets, PTAs also raise economic efficiency by allowing domestic firms to take advantage of economies of scale. As trade openness becomes the norm, firms also stop wasting resources to lobby for government protection and instead invest them more productively (Krueger 1974, 1996; Grossman and Helpman 1994). In addition to higher allocative efficiency, sustained international competition

also stimulates dynamic efficiency by pressuring firms to invest and innovate to remain competitive. The increase in individual firms' economic efficiency resulting from those different channels generates higher national income.

Beyond their direct positive effect on economic efficiency, PTAs are also considered conducive to economic development by neoclassical economists due to their promotion of market reforms, which in turn increase economic efficiency. This view was shared by Jaime Serra, Mexican chief negotiator during the original NAFTA negotiations, who argued that it did not make sense economically for Mexico to remove tariff barriers on certain products and not others, as the higher costs of goods and services in protected sectors would undermine the competitiveness of liberalised sectors (Mayer 1998: 124). Trade agreements promote market reforms by including commitments to liberalise foreign investment and financial markets and eliminate 'market-distorting' government interventions such as subsidies and support for state-owned enterprises (Heydon 2020: 25-6).

Trade agreements also contribute to economic development by reducing uncertainty (Ibid.). Signing a trade agreement locks in market reforms beyond national legislation by committing a country to international law. International trade commitments have been perceived by new governments as less desirable to overturn than domestic policies because doing so undermines the state's credibility. As such, some countries in the global South with a reputation for policy reversals, such as in Latin America, considered signing PTAs as a means to signal their long-term commitment to free-market policies (understood as strong property rights and minimal government intervention) (Baccini and Urpelainen 2014). Sanction mechanisms in trade agreements lock in market reforms, such as Investor-State Dispute Settlement (ISDS), which protects foreign investors from expropriation, unfair competition, and changes in government policy (Fernández 1999). By regulating intellectual property rights, state support to domestic firms, and state-owned enterprises, trade agreements also reduce the risk for foreign firms of

facing competition from domestic firms that engage in technological theft, receive subsidies or preferential access to government contracts. Foreign investment regulation prevents governments from imposing burdensome requirements on foreign firms, such as contracting domestic producers or transferring technology. Such restrictions on policy space reduce investor uncertainty and are thus considered conducive to investment.

Similarly, trade agreements are also considered to promote economic development by reducing uncertainty over access to the trading partner's market (Handley and Limão 2015; Fernández 1999). Signing a trade agreement is expected to prevent the trading partner from reverting to protectionism, and as such to provide greater certainty for investors wishing to export. In the case of trade agreements between unequal partners, PTAs are meant to protect more vulnerable countries from beggar-thy-neighbour policies (Mayer 2009). As such, PTAs signed with the US, such as NAFTA, were thought to 'insulate countries from bilateral pressures' as 'a bilateral trade agreement […] is no longer a unilaterally granted concession that can be withdrawn at the US discretion, but rather a non-removable, reciprocal commitment' (Shadlen 2017: 178). By contrast, the US had used its Generalised System of Preferences (GSP) to unilaterally grant or remove preferential market access, thereby creating leverage on countries benefitting from its GSP programme (Ibid.).

The analysis of the benefits of PTAs outlined above, however, does not account for the way many late-industrialising countries developed, which involved activist trade and industrial policies (ATIP). Chang's (2002) analysis of development strategy in historical perspective demonstrates that many of today's high-income countries industrialised by implementing protectionist policies such as tariff barriers, subsidies to domestic firms, weak or no intellectual property rights protection for foreign technologies, requirements on foreign investment, and state-owned enterprises. The United Kingdom implemented protectionist policies to catch up

with Holland and Belgium, France and Germany to catch up with the UK, and the US to catch up with Western Europe (Ibid.; List 1974).

Several influential case studies of Japan, South Korea and Taiwan – the East-Asian late industrialisers which caught up with industrialised countries at record growth rates – also provide evidence of the role of ATIP, including tariffs, quotas, export subsidies, a depreciated exchange rate, weak intellectual property rights, capital controls, joint venture and technology licensing requirements (Johnson 1982; Amsden 1989; Wade 1990; Ang, Madsen, and Robertson 2015; Lane 2022). To reduce risks of corruption and inefficiencies, East Asian states employed 'reciprocal control mechanisms' whereby governments would condition subsidies on performance requirements, such as export targets (Amsden 1989, 2001). This required 'embedded autonomy': states had to be both embedded in society to understand the needs of businesses, yet sufficiently autonomous to discipline firms into meeting performance requirements (P.B. Evans 1995). While more open to trade and foreign investment than other East-Asian miracle economies, Singapore imposed strict conditions on foreign companies. More recently, China's high growth rates have been accompanied by ATIP to promote technology transfer and protect infant industries (Rodrik 2007; K. Lee 2021). Although the global South retained some policy space in the WTO, PTAs with the US, and to a lesser extent the EU, severely curtailed the use of such policies (Gallagher 2007).

No perfect counterfactual exists, which weakens claims that ATIP caused economic development. A contending explanation offered is that the East Asian miracle economies would have grown faster with free trade and that their high growth rates were the result of good 'fundamentals', such as a high savings rate and investment in education (Young 1994; Krugman 1994). However, the low growth rates in countries which followed the 'Washington Consensus' policies of free trade and minimal regulation, such as in Latin America and parts of Eastern Europe, undermined the belief that free trade is conducive to high growth (Rodrik 2007).

Furthermore, the record-high growth rates of countries that opened to trade while retaining protectionist policies, such as China and other Asian countries, can hardly be interpreted as evidence that free trade causes economic development. Even though there is now widespread agreement that ATIP had some positive effect on economic development in East Asia (Gallagher 2007: 65), this does not imply that a country can implement those policies successfully. There are numerous examples of governments wasting resources by supporting the wrong industries, failing to discipline firms, or succumbing to rent-seeking (P. B. Evans 1995; Krueger 1996; A. Harrison and Rodríguez-Clare 2010).

Drawing on the historical evidence presented above, many economic theories contest the beneficial effects of free trade and unregulated foreign investment by highlighting the role of sectors and structural change in economic development (Rodrik 2015; Szirmai and Verspagen 2015; Chang and Andreoni 2020). Structuralist economists such as Prebisch (1950), Furtado (1970), and Cardoso and Faletto (1979) criticised free trade policies for undermining economic development by locking in the global South in the production of low value-added primary commodities. They argued that primary commodities are typically characterised by a low-income elasticity of demand and declining prices relative to imported manufactured goods, resulting in worsening terms of trade. Those factors increase the dependency of the global South on the global North and can only be reverted by protecting domestic industries in higher value-added sectors until those become globally competitive.

Similarly, political economists such as Rosenstein-Rodan (1943), Hirschman (1958) and Gerschenkron (1962) stressed the importance of state intervention to change the structure of the economy towards sectors more conducive to economic development. Specialising in manufacturing is more conducive to productivity growth than other sectors, and certain manufacturing activities in particular can best promote development by generating numerous forward and backward linkages with other activities. By incentivising the global South to

specialise in producing primary commodities, free trade promotes unequal exchange as those countries remain stuck in a comparative advantage of producing low-productivity goods generating low wages.

Foreign investment by multinationals can also hinder structural change by reinforcing a country's static comparative advantage in the extraction of commodities or exploitation of low-wage labour. Drawing on varieties of capitalism theory, Schneider (2013) concludes that MNCs in the global South perpetuate vicious economic and political cycles, such as by spending close to nothing on research and development in the host country and yet, by their higher productivity, preventing the development of domestic firms' productive and innovative capabilities. Those insights echo developments in evolutionary economics, such as the national system of innovation approach pioneered by Freeman (1982), Nelson (1993), and Lundvall (1995), which stress the need to focus on the development of domestic productive and innovative capabilities (see also Verspagen 1993; K. Lee 2013; McMillan, Rodrik, and Sepúlveda 2017). Whereas neoclassical trade theory focuses on gains from exchange, critics call for bringing the study of production back into economic development (Amsden 1997; Chang and Andreoni 2021).

More recent theories within neoclassical economics, often borrowing from the work of institutionalist and structuralist economists (Nelson 1997), also provide justifications for protectionist policies by challenging certain assumptions of theories justifying free trade, such as constant returns to scale and perfect information (Grossman 1992; Krugman 1991; Romer 1990; Szirmai 2012; Dosi, Roventini, and Russo 2019). Endogenous growth theory (Romer 1990), new economic geography theory (Krugman 1991), and strategic trade theory (Grossman 1992) all give credence to infant industry protection by stressing the importance of technological innovation, increasing returns to scale and path dependence. Although many of the theories' proponents remain supporters of free trade, those theories provide support to the view that free trade can entrench the global South in a static comparative advantage

unconducive to long run development, such as producing low value-added goods by competing through low wages (Krugman 1987: 134; Qiu et al. 2019). Temporary protection of domestic infant industries can enable countries to learn by doing and develop economies of scale, leading to the creation of a dynamic comparative advantage in higher value-added products (Ibid.). South Korea's growing steel exports from the late 1970s, for instance, could not have been foreseen nor explained by the neoclassical theory of comparative advantage, which suggested that the country specialises in low-value-added goods rather than heavily investing in a state-owned steel company. Neoclassical economists concede that certain regulations in PTAs undermine economic development, such as stringent intellectual property rights protections, which transfer income from the global South to the global North, as well as capital account liberalisation, which contributed to financial crises in developing countries (Bhagwati 2004).

2.3.2. The Logic of North-South PTAs

From a neoclassical economic perspective, North-South preferential trade agreements (PTAs) promote economic development. From a structuralist economic viewpoint, however, North-South PTAs can hinder long-term economic development by restricting the global South's policy space for activist trade and industrial policies (ATIP). Although WTO rules restricted the use of many industrial policies used in the past by late industrialisers to catch up, such as local content and trade balancing requirements on foreign investment, countries in the global South retained significant policy space thanks to 'Special and Differential treatment' allowing them to implement temporary infant industry protection, among other policies (Amsden and Hikino 2000). Developing countries also bound their tariffs at high levels, enabling them to raise their tariffs for industrial policy purposes, while many omissions, loopholes and exceptions allowed WTO members to conduct limited forms of industrial policy, such as using

state-owned enterprises to offer cheap loans to domestic firms (Ibid.). Furthermore, since the 1970s, many countries of the global South were also granted preferential access to markets in the global North under the GATT 'Generalised System of Preferences' (GSP). Some countries in the global North even expanded their GSP programmes, such as the US with the launch of the African Growth and Opportunity Act (AGOA) in 2000 (Narlikar 2020: 45-46).

Given the policy space and preferential access to high-income markets the global South retained in the WTO, the question arose as to why many signed regional or bilateral trade agreements with the global North, in the process severely restricting their policy space (Shadlen 2005; Shadlen 2008). Indeed, North-South PTAs prevent the use of most of the remaining ATIP authorised under the WTO: tariffs, as well as many non-tariff barriers, are eliminated, intellectual property rights protection is enhanced, financial controls are liberalised, and nearly all performance requirements on foreign investment are prohibited (Thrasher and Gallagher 2008). The domino effect theory of the proliferation of PTAs (Baldwin 1993) suggests that, as countries signed PTAs, non-members felt increasing pressure to obtain similar preferential market access to remain competitive. However, this theory begs the question of why countries in the global South conceded policy space for preferential market access given that they already benefited from considerable preferential market access under the GSP. PTAs did provide limited market access gains, as the GSP often excluded politically sensitive sectors such as agriculture, apparel and textiles. Even without considering GSP, however, Mexico's preferential access to the US market under NAFTA was only two per cent better than under US MFN tariffs (Heydon 2020: 88).

For Shadlen (2008: 3), 'the promise of an RBTA (Regional or Bilateral Trade Agreement) is preferential market access that is secure, stable, and non-removable', by contrast to GSP's 'nature as unilateral concessions that are easily removable and alterable' (Ibid.: 5-6). Given that GSP concessions are not bound under the WTO, countries in the global North can and did

remove them for domestic reasons or to exert pressure on GSP receivers, which created 'political trade dependence' (Ibid.; Manger and Shadlen 2014. In the 1980s, the US offered Mexico preferential market access under the GSP in exchange for stronger intellectual property rights protection (Lustig 1992: 129-30). The US chief negotiator for USMCA played a direct role in this process:

> I actually started working on Mexico trade issues in 1988 or 89. The prior position I had at USTR was as Deputy Director of the Generalised System of Preferences, which is a tariff preference program that many wealthy countries offered to third-world countries. And because Mexico was willing to make changes to its intellectual property laws at that time, we were expanding their benefits under the GSP program. So the change in Mexico predates NAFTA (John Melle, interview, 16 December 2020).

Although the US government expanded Mexico's GSP benefits, those were withdrawn in 1987 for some chemical products in protest of Mexico's weak intellectual property protection (Lustig 1992: 129-30). Just like Mexico, most countries in the global South had not significantly benefited from GSP due to the uncertainty created by political conditionality (Brenton 2003; World Bank 2002; Hoekman and Ozden 2005). By entering NAFTA, Mexico traded its policy space for ATIP in exchange for *stable* preferential market access, with the hope that lower uncertainty would stimulate foreign investment inflows (Cameron and Tomlin 2000: 1-2). President Salinas and his Secretary of Commerce Jaime Serra believed that unilateral trade liberalisation without market access certainty would be insufficient to attract foreign investment given that many countries were also implementing trade liberalisation reforms (Ibid.). In 1993, one year before the entry into force of NAFTA, nine per cent of Mexican exports to the United States received unilateral preferential trading arrangements, which could thus be removed at any moment (Shadlen 2005: 764).

Many countries in the global South followed Mexico's path of trading policy space for stable preferential market access (Manger and Shadlen 2014; Shadlen 2005). For structuralist

economists, the costs of restricted policy space on long-term development prospects outweighed the benefits of *stable* preferential access to markets in the global North (Chang, Irfan, and Hauge 2016). For neoclassical economists, both stable market access and policy space restrictions would promote economic development. The next section examines the impact of NAFTA on the Mexican and US economies, which were more affected than the Canadian economy.

2.4. Explaining the Backlash

2.4.1. The Impact of NAFTA

Most neoclassical economic models of the 1990s predicted that NAFTA would lead to 1) low adjustment costs in the US and 2) economic convergence between Mexico and the US, conditional on macroeconomic stability reforms which Mexico implemented following the 1995 financial crisis (Hufbauer and Schott 1992). This section demonstrates that both predictions did not materialise, contributing to the backlash against NAFTA in the US.

According to proponents of NAFTA and other North-South PTAs, the benefits to Mexico (and other late industrialisers) in terms of preferential market access would far outweigh the costs, if any, of policy space restrictions. Most neoclassical economists thought that Mexico and other countries in the global South, by adhering to free trade and free market reforms, would grow fast to converge with the income per capita levels of the global North (DeLong 2006; Hufbauer, Cimino, and Moran 2014). Politicians were also enthusiastic. Mexican President Salinas de Gortari, who signed NAFTA, predicted that the agreement would cause economic convergence with the US (Blecker 2019: 149). Similarly, Mexican President Fox envisaged in 2000 that, by 2020, Mexico would have sufficiently converged economically with the US to open the border for free movement of labour (Harman 2001). The agreement would also benefit the US:

neoclassical economic models showed that workers would benefit from the PTA through rising living standards and that few adjustment costs were expected (Mayer 1998: 5).

23 years after the entry into force of NAFTA, however, Trump won the 2016 US presidential elections on a populist campaign denouncing free trade in general and NAFTA in particular (Thrush 2018). Trump blamed NAFTA for the offshoring of production to Mexico, which he claimed was the cause of the US trade deficit with Mexico. His campaign proved particularly effective in the 'Rust Belt' states most hit by deindustrialisation, such as Michigan, Pennsylvania and Ohio, which were decisive in Trump's victory. Dissatisfaction with NAFTA was not novel in the US as the trade agreement had long been criticised within the Democratic Party for the adjustment costs it had caused, including by President Obama. By 2016, trade agreements had become so unpopular with the US electorate that Democratic Party presidential candidate Hillary Clinton called to renegotiate NAFTA and abandon the Trans-Pacific Partnership trade agreement signed by Obama (Klein and Pettis 2020: 222). Bipartisan discontent over NAFTA in the US electorate contrasted with the positive expectations of neoclassical economic models when the agreement was signed: 'Given the huge size of the US economy, the models typically calculate that the laid-off workers will be employed elsewhere after a very small average decline in wages' (Hufbauer and Schott 1992: 50).

Similarly in Mexico, populist candidate López Obrador was elected President in 2018 on an anti-neoliberal platform. The first left-wing president since the 1930s, he was a vocal critic of NAFTA during his 2006 and 2012 presidential campaigns. López Obrador criticised NAFTA as devastating for Mexican small farmers in particular (Cunningham 2018). He won a record 53 per cent of the vote in the 2018 elections, more than 30 percentage points ahead of the runner-up. He also won a controlling majority in both chambers of the Mexican Congress. The landslide election of a vocal critique of NAFTA also questioned neoclassical economic models predicting that NAFTA had benefited Mexican workers.

The resonance of Trump's and López Obrador's criticisms of the NAFTA era with the US and Mexican electorates respectively warrant an evaluation of the trade agreement's impact on the US and Mexican economy (Canada did not experience a similar backlash, in part because it is less integrated with Mexico than the US). Assessing the effects of NAFTA is difficult, however, due to the impossibility of controlling for all the variables affecting the North American economy, in particular the fact that the entry into force of NAFTA in 1994 coincided with an uprising in Chiapas and was followed in 1995 by a financial crisis in Mexico. 1995 also marked a reduction in Mexico's preferential market access to the US as the WTO came into force. In 2001, China's entry into the WTO led to severe competition with Mexico for the US market. Drawing on a multitude of studies spanning two and a half decades, the impact of NAFTA in the US and Mexico in terms of trade and investment, economic growth, adjustment costs, inequality, and changes in economic structure, are analysed in turn.[4] Table 2 provides a summary.

[4] This brief evaluation cannot do justice to the numerous studies on the effects of NAFTA. For a more comprehensive review, see Blecker (2019).

TABLE 2: ECONOMIC IMPACTS OF NAFTA

	US	Mexico
Trade and investment	Between 1993 and 2016, surge in regional trade from 290 billion to 1.1 trillion $US, and US FDI outflows to Mexico from 15 to 100 billion $US (Chatzky, McBride, and Sergie 2020).	Sevenfold increase in trade with the US and Canada, although the causal effect is smaller (Blecker, 2019: 153-5; Romalis, 2007). Huge increase in FDI inflows, from 1.2 per cent to 2.7 per cent of GDP (Ibid.).
Economic growth	Insignificant: 0/0.1 per cent (Romalis 2007; Caliendo and Parro 2015).	Insignificant: 1.3 per cent (Caliendo and Parro 2015), -0.3% (Romalis 2007).
Adjustment costs	Low overall but highly localised: 17 per cent lower wage growth for workers in the most protected industries before NAFTA (apparel, footwear) (Hakobyan and McLaren 2016).	High: Almost 5 million farmers lost their livelihoods (Watts 2016).
Inequality	Probable increase due to easier outsourcing (Bronfenbrenner 1996; Polaski 2006) and lower wages for affected communities (Hakobyan and McLaren 2016).	Increased (Nicita 2009; Kay and K. L. Evans 2018: 167). No real wage increases for production workers since 1994 (Blecker 2019).
Economic structure	Possible contribution to deindustrialisation, although no proof of causal effect (Griswold 2002).	Export diversification and increased manufacturing production, yet specialisation in low value-added activities and high informal sector remain. (Ibid.; Binelli 2016)

Trade and investment

The primary effect of a PTA should be to increase trade between the trading partners. Between 1993 and 2016, trade between NAFTA members nearly quadrupled from 290 billion to 1.1 trillion US dollars (Chatzky, McBride, and Sergie 2020). Mexican exports to Canada and the US increased sevenfold from 45 to 313 billion US dollars (Blecker 2019: 153). Attempts to identify the causal effect of NAFTA on regional trade, however, suggest a more modest impact. Romalis (2007) finds that NAFTA increased US-Mexican trade by 23.2 per cent, while Caliendo and Parro (2015), by including trade in intermediate goods, conclude that NAFTA tariff cuts increased regional trade by 118 per cent for Mexico, 41 per cent for the US, and 11 per cent for Canada.

NAFTA's impact on regional trade is less impressive when considering the evolution of each country's share of trade with NAFTA partners in its total trade. Between 1993 and 2019, US exports to NAFTA partners increased from 31 to 34 per cent while US imports from NAFTA partners remained stable at 26 per cent. During the same period, in Mexico, both exports to and imports from NAFTA partners decreased, from 86 to 82 per cent and 76 to 49 per cent, respectively. Similarly, both Canada's exports and imports to NAFTA partners decreased, from 81 to 77 per cent and from 69 to 57 per cent, respectively. This decline was largely due to NAFTA members' rising share of imports from China, which more than tripled from 5 per cent in 1993 to 18 per cent in 2019 (Ibid.). The creation of the WTO in 1994 and China's accession in 2001 reduced the relative preferential market access provided by NAFTA.

NAFTA was also signed by the Mexican government in the hope that it would increase FDI inflows. This expectation proved accurate as US FDI outflows to Mexico surged from 15 to 100 billion US dollars between 1993 and 2016 (Chatzky, McBride, and Sergie 2020). Total FDI inflows in Mexico increased from 1.2 per cent of Mexican GDP in the pre-NAFTA period (1980-1993) to 2.7 per cent of GDP post-NAFTA (1994-2016) (Blecker 2019: 155). By contrast, the US experienced net FDI outflows following its 1989 PTA with Canada (CUSFTA) and in the early years of NAFTA (Ibid.: 157).

Economic growth

The most robust econometric studies have found little impact of NAFTA on US and Mexican economic growth. Caliendo and Parro (2015) conclude that NAFTA tariff cuts increased Mexican GDP by 1.3 per cent and US GDP by less than 0.1 per cent. Another study, taking into account the trade diversion effects caused by NAFTA, finds that the trade agreement decreased Mexican GDP by 0.3 per cent (Romalis 2007). While NAFTA's minor impact on US economic growth was forecasted by neoclassical economic models due to the small share of trade with

Mexico in the US GDP (Mayer, 1998: 5), the effect of NAFTA on Mexico was expected to be significantly positive (Hufbauer and Schott, 1992: 61-62; DeLong, 2006; Hufbauer et al., 2014).

Given the minor effect of NAFTA tariff reductions on Mexico's GDP, one can look for other channels through which NAFTA promoted economic growth, such as the higher investment certainty provided by secure market access and the market reforms that Mexico committed to as a result of NAFTA. In their econometric study, Galan and Olapido (2009) conclude that export changes as a result of NAFTA contributed to Mexico's economic growth, but found no effect of foreign direct investment on Mexican economic growth. Furthermore, instead of economic convergence with the US, Mexico experienced economic divergence. Mexico's GDP per capita at purchasing power parity (PPP) increased by 30 per cent between 1990 and 2019, from 15,356 to 20,032 constant 2017 US dollars, whereas US GDP per capita PPP increased by 54 per cent during the same period (World Bank 2022b). Mexico's growth rate between the signing of NAFTA and the beginning of its renegotiation declined over time and averaged one per cent per year per capita (Sánchez Juarez and Moreno Brid 2016; Weisbrot et al. 2018).

Adjustment costs

Critics in the US and Mexico focused on the adjustment costs NAFTA would create in terms of employment and wages. Mexico faced much higher adjustment costs than the US or Canada in joining NAFTA, yet the Mexican government did not introduce a policy to help its workers and farmers. In Mexico, certain activities such as corn production were decimated by subsidised US imports, leading to a loss of jobs and livelihoods for almost five million Mexican farmers between 1991 and 2007 (Watts 2019). The adjustment costs caused by NAFTA contributed to Mexican immigration to the US in the 1990s and 2000s, fuelling anti-immigration sentiments.

In the US, Trump decried NAFTA for causing a loss in US manufacturing jobs and the decline of working-class wages. As predicted by economic models, NAFTA had an insignificant impact on aggregate employment in the US (Burfisher et al. 2001; Blecker 2019). However, contrary to predictions of small adjustment costs, robust econometric analyses find that NAFTA caused significant manufacturing job losses concentrated in certain industries, communities and segments of the US labour force, leading to outmigration (Hakobyan and McLaren 2016). Following trade liberalisation, wages declined 17 per cent in industries that were most protected before NAFTA (footwear, apparel), compared to unprotected industries, with blue-collar workers and high-school dropouts living in those communities hardest-hit, such as in Georgia, the Carolinas, and Indiana (Ibid.). Using a similar methodology, Choi et al. (2021) found that US counties vulnerable to Mexican import competition suffered large employment losses concentrated in manufacturing following the passage of NAFTA. By 2000, employment in the quartile of US counties most exposed to Mexican import competition was 5-8 log-points lower than in the quartile of US counties least exposed.

Inequality

Neoclassical economic models predicted that NAFTA would have an insignificant effect on real wages in the US, except for weakly depressing wages of low-skill workers (Leamer 1993; Reynolds 1995). In Mexico, it was predicted that NAFTA would increase wages and reduce wage inequality (see Hufbauer and Schott 1992: 58 for a review). Although NAFTA had little effect on average real wages in the US (Burfisher, Robinson, and Thierfelder 2001), it significantly depressed wages for low-skill workers facing import competition from Mexico, as suggested by the findings by Hakobyan and McLaren (2016) presented above. This logic is captured by Rodrik's (2011: 57) estimate that, in the United States, for every dollar gained from increased trade, 50 dollars are redistributed between different economic groups, typically from

low to high-skill workers. NAFTA contributed to increased wage inequality in the US, especially given that the greater ease of outsourcing production weakened the bargaining position of labour (Bronfenbrenner 1996; Polaski 2006). Nevertheless, most of the rise in income inequality in the US since the 1980s is attributable to the rising share of the top one per cent, rather than competition from low-wage labour in the global South (Irwin 2017: 669).

In Mexico, predictions of rising wages and declining wage inequality proved incorrect (Kay and K. L. Evans 2018: 167). While some skilled workers benefited from higher wages (Nicita 2009), median real wages in Mexico remained stagnant. The average real hourly wage of production workers in Mexico was even lower in 2016 than when NAFTA entered into force in 1994 (Blecker 2019: 160-1). Although increases in wage inequality cannot be solely attributed to NAFTA, the agreement did not cause a wage increase for working-class workers in the US and Mexico. The share of national GDP captured by Mexican workers fell from 43 to 36 per cent between 1994 and 2019, while it remained at approximately 60 per cent in the US and declined from 72 to 65 per cent in Canada during the same period (Otero 2024).

Economic structure

NAFTA was also criticised in the US and Mexico for its effect on each country's economic structure. In the US, Trump condemned the trade agreement for causing deindustrialisation. This critique of the structural economic changes caused by NAFTA was developed by his economic adviser Peter Navarro, Secretary of Commerce Wilbur Ross, and US Trade Representative (USTR) Robert Lighthizer, who pointed to the offshoring of production to Mexico since NAFTA (Lighthizer 2020). Multinationals relocated to Mexico to take advantage of lower labour costs, which between 2007 and 2014 were on average five times lower than in the US in assembly and eight times lower in parts manufacturing (Menck and Swiecki 2016: 32). Relocations were reflected in the share of North American vehicles produced in Mexico,

which increased from 6.2 per cent in 1995 to 19.5 per cent in 2016, at the expense of US production which declined from 78 to 67 per cent (Ibid.). It is unclear whether US deindustrialisation would have occurred to the same extent or more without NAFTA, however, as North American economic integration also helped prevent further offshoring to Asia by rendering US manufacturing more competitive (Griswold 2002).

In Mexico, FDI inflows transformed the structure of the economy by diversifying its exports away from oil and into manufacturing, as well as increasing manufacturing production and employment, especially in the auto industry (Blecker 2019). Mexico attained world-class productivity in manufacturing exports, such as in automobiles, electronics, and aerospace. Between 1993 and 2019, Mexican exports surged nearly ninefold from 52 to 460 billion US dollars (WITS 2023). Change in economic structure was limited, however, in that Mexico largely remained specialised in low value-added activities such as assembly, thereby importing a high percentage of inputs rather than sourcing them from domestic firms (Sánchez-Juarez and Moreno Brid 2016). NAFTA also failed to reduce the predominance of the informal sector in the Mexican economy, which instead increased from approximately 50 per cent of total employment in the early 1990s to nearly 60 per cent since the early 2000s (Binelli 2016; Gurria 2019; ILO 2014).

2.4.2. NAFTA as a Symbol

The level of backlash against NAFTA in the US cannot be attributed solely to its consequences on the US economy. As Mayer (1998) emphasized, NAFTA symbolised economic globalisation to the US electorate, which explains the discrepancy between the small effects of the trade agreement predicted by economists and the fierce opposition of US Congressional Democrats, environmental groups and labour unions during its negotiation and ratification in the early

1990s. Since then, the consequences of NAFTA have been associated by US politicians and the electorate with the consequences of free trade policies adopted by the US, such as the loss of approximately 1.5 million US manufacturing jobs to China between 1990 and 2007 (Autor et al. 2013). US counties which voted for Trump often had little trade with Mexico, with the exception of counties in the Great Lakes and lower Midwest, which often formed part of swing states which proved decisive in the 2016 elections (Hinojosa Ojeda and Telles 2021).

From 2001, NAFTA's effect on US manufacturing employment was dwarfed by the effect of China's entry into the WTO. Between 2001 and 2009, US manufacturing employment dropped by *33 per cent* from 17.1 to 11.5 million (US Bureau of Labour Statistics 2021). Autor et al. (2013: 2140) estimate that Chinese import competition accounted for 26 per cent of US manufacturing employment decline between 2000 and 2007. Acemoglu et al. (2016) found that the US lost 2 to 2.4 million jobs due to import competition from China between 1999 and 2011 (including indirect job losses). Similarly, Campbell (2020: 10-11) concludes that approximately 2.5 million US manufacturing jobs were lost due to trade between 1998 and 2007, of which 1.5 million can be attributed to an overvalued dollar, and the remaining to China's accession to the WTO in 2001. The China shock caused long-term adjustment costs in US localities where import-competing industries were concentrated (Autor et al. 2013, 2016). Ten years after China entered into the WTO, wages in those areas remained depressed and unemployment rates high. Although other countries in the global North were also hit by the China trade shock, adjustment costs were attenuated by their stronger welfare systems and their having granted Permanent Normal Trading Relations (PNTR) to China earlier (Pierce and Schott 2016). Furthermore, the large US trade deficit with China, which increased from 83 to 344 billion US dollars between 2001 and 2019, contributed to lower employment growth in the US (Autor, Dorn, and Hanson 2016; US Census Bureau 2021).

In addition to the China shock, automation was also responsible for the fall in manufacturing jobs in the US and other countries (Autor et al. 2013, 2016). During the 2000s, however, the loss of manufacturing jobs in the US was proportionally higher than in other high-income countries, except for the UK (Guilford 2018; International Federation of Robotics 2021, Houseman et al. 2018). Although the US automation rate lagged behind competitors, such as Germany and South Korea, those countries experienced far fewer job losses (Ibid.). Economists before 2016 pointed to the growth of US manufacturing output on par with US GDP growth as a signal of the health of the US manufacturing sector, yet this was largely due to the extraordinary growth of the US computer industry. Other US manufacturing industries, by contrast, barely grew in the 2000s (Houseman et al. 2011; Houseman 2018). Automation cannot account either for the net loss of over 91,000 US manufacturing plants between 1997 and 2018 (Scott 2020).

Although the US lost jobs in the manufacturing sector, many more jobs were created in the service sector (Feenstra et al. 2017). This shift was accelerated by outsourcing as manufacturing firms subcontracted services such as cleaning and maintenance to other firms. However, by contrast to manufacturing employment, which offered good pay and stable jobs for workers without a college education, most services jobs created were temporary and poorly paid. Manufacturing workers who lost their jobs often did not find a new one matching their skill set, forcing them to enter long-term unemployment or take a precarious job in the service sector (Autor, Dorn, and Hanson 2016; Case and Deaton 2020). President Trump's protectionist platform was partly a response to those broader structural changes and adjustment costs (Ibid.).

2.5. Structuralism Vindicated?

Mexico suffered high adjustment costs, especially for small farmers, while median wages remained stagnant throughout the period and even decreased for production workers (Blecker 2019: 160-1). Although the export structure of the Mexican economy diversified away from oil and into manufacturing, the country remained largely stuck in low-value-added activities. Due to NAFTA's disappointing results, proponents of free trade progressively moved the goalposts to argue that free trade must be complemented with other market reforms for economic growth to take off (Blecker 2022). In addition to free trade, Mexico had to guarantee private property rights and macroeconomic stability for economic convergence with the US to occur.

In the first years of NAFTA, Mexico struggled with macroeconomic stability. On 1 January 1994, the day of the entry into force of NAFTA, the so-called 'Zapatistas' led a violent uprising in the Southern state of Chiapas to protest against the trade agreement and the federal government. The Zapatista uprising was quickly suppressed by the Mexican army, yet political instability persisted and was heightened when presidential candidate Colosio, the chosen successor of President Salinas, was assassinated in March 1994. The political instability, combined with Salinas' expansionary policies to maximise support during the presidential election, put downward pressure on the Mexican peso. The Mexican central bank defended the peso's peg to the US dollar but capital flight continued. By the end of 1994, the Mexican central bank was running out of reserves, which forced a devaluation of the peso. Banks raised interest rates to reduce capital flight, which worsened the economic recession. The Mexican economy recovered from the 1995 'tequila' crisis in large part thanks to a US financial bailout and a currency depreciation.

Since the 1995 financial crisis, the Mexican government has secured macroeconomic stability by conducting conservative fiscal and monetary policies, yet economic growth has not taken off. Private property rights were enforced and protected by the NAFTA Investor-State Dispute Settlement (ISDS). The contrast between the expectations set for NAFTA and the reality is

summarised by DeLong (2006): ‘Success at creating a stable, property respecting domestic environment has not delivered the rapid increases in productivity and working-class wages that neoliberals like me would have confidently predicted when NAFTA was ratified’. A closer analysis of the Mexican economy, contrasted with the experience of other countries during the same period, sheds further light on the neoclassical vs structuralist debate.

2.5.1. The Mexican Economy

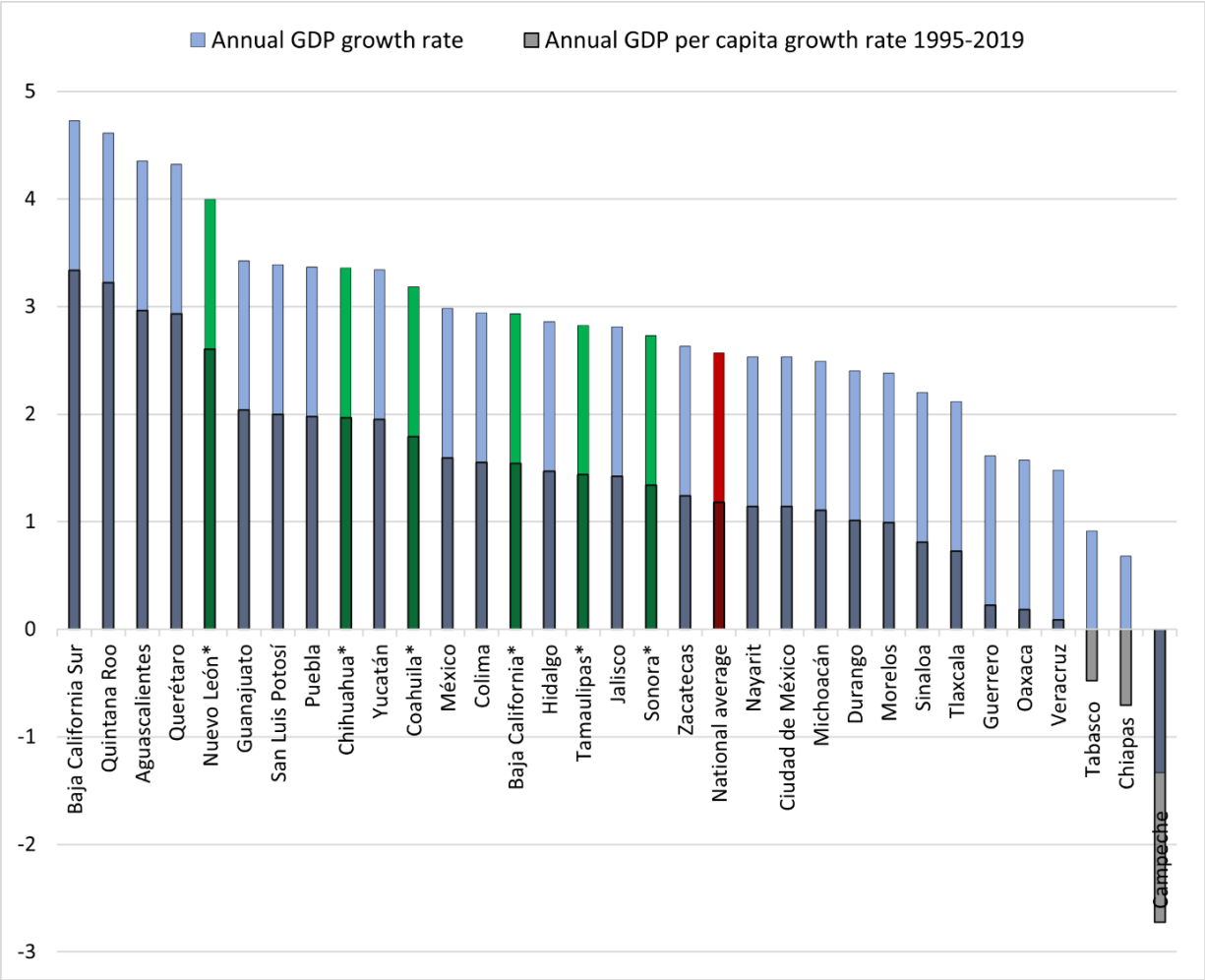
Ironically, the prudent fiscal, monetary, and exchange rate policies intended to promote growth and stability have contributed to Mexico’s low economic growth (Blecker 2022). Fiscally, Mexican governments followed a procyclical policy due to a balanced budget rule intended to prevent new financial crises. Given the lack of fiscal reform, Mexico in 2019 earned less tax revenue as a share of GDP than all other OECD countries, and most Latin American countries (OECD 2023; TPC 2023). The result is a large public spending deficit in infrastructure, technology, health, education, and sanitation. In terms of monetary policy, the Mexican central bank became independent in 1994 and was tasked with prioritising low inflation above all other considerations, such as growth, employment, and a competitive exchange rate. Monetary policy was conducted asymmetrically in the first years of the Central Bank as it raised interest rates when the peso depreciated but did not lower them when the peso appreciated (Galindo and Ros 2008). The result was a sharp real appreciation of the peso in the early 2000s coinciding with the time when the Chinese yuan was undervalued, which undermined Mexican exports’ competitiveness.

Similarly, the trade liberalisation reforms and NAFTA in particular contributed to limiting Mexico’s economic growth by exacerbating the Mexican economy’s reliance on the (relatively low) rate of growth of the US market. Despite Mexico’s efforts at diversifying its export

destinations through the signing of numerous PTAs, approximately 80 per cent of its exports continued to be sent to the US. Since NAFTA, the sensitivity of Mexican economic growth to US economic growth has been statistically significant (Blecker 2009). Given the high share of imported inputs in the value of its exports, the Mexican economy would have faced balance of payments constraints by growing faster than the US, which has been facing secular stagnation since 2008 (Blecker 2022; Polanco and Schmidt 2019). Structuralist policies to increase the domestic value-added in Mexican exports could have helped overcome this external constraint.

A subnational analysis of the Mexican economy provides a somewhat more positive assessment of NAFTA. Figure 2 compares the average annual growth rates of Mexican states between 1995 and 2019, measured in constant pesos. Mexican border states, which benefited the most from NAFTA, grew faster than the national average. The fastest-growing border state, Nuevo Leon, grew its GDP by 4 per cent per year (2.6 per cent per capita) such that in 2019 it had a GDP per capita at purchasing power parity (PPP) similar to Portugal. States in the Bajio region (in between Mexico City and the US frontier), such as Aguascalientes and Querétaro, also grew rapidly by becoming more economically integrated into North American supply chains. Aguascalientes became a leader in auto manufacturing and Querétaro pioneered Mexico's entry into the manufacturing of small airplanes by attracting a Bombardier plant in 2007. By contrast, states in southern Mexico were not economically integrated and mostly failed to grow their GDP per capita. Some even witnessed a decline in GDP per capita during the same period, such as Campeche and Chiapas. NAFTA partly contributed to poor growth rates and precarity in those regions, however, by enabling US-subsidised agribusinesses to outcompete local farmers.

FIGURE 2. MEXICAN STATES' AVERAGE ANNUAL GROWTH RATE, GDP/GDP PER CAPITA (1995-2019)



Source: Author's own based on data from INEGI (2022).
*US border states (in green)

Although Mexican states more closely integrated with the US grew faster, the economic growth did not translate into higher real wages for production workers (Blecker, 2019: 160-1). The difficulty of achieving economic and social upgrading has been experienced in many other countries of the global South (Milberg 2013: 255). Taking advantage of their monopsony or oligopsony position, lead firms encourage fierce competition amongst suppliers, often resulting in both downward pressure on wages and markups insufficient for domestic firms to invest in upgrading production (Milberg 2013: 241). Multinationals implement strategies which undermine the industrial upgrading of their suppliers in the global South, including branding, minimising technological transfer, and shifting risks to suppliers (Ibid.: 127-9).

The Mexican economy faced several problems during the NAFTA period which have reinforced the factors listed above, but also sometimes resulted from them (Wilson 2019). First, government corruption and organised crime increased the costs of doing business and created investment uncertainty. Although similar levels of corruption can be found in developing countries with much higher growth rates during this period, the violence of drug cartels in Mexico accentuated investment uncertainty. Under the presidency of Calderón (2006-12), the government launched a 'war against drugs' to dismantle cartels, leading to counterproductive results as new cartels emerged and fought for territory. Although increased violence helps explain Mexico's low and declining growth rates, the causality runs both ways: the weak growth rate of formal sector jobs made it easier for cartels to recruit.

Second, the high cost of certain essential services, in large part due to poor regulation of monopoly power, undermined Mexican competitiveness. As part of its market reforms but also as a result of financial pressures during the 1995 financial crisis, the Mexican government privatised many state-owned enterprises (Harvey 2005). Most famously, the telecommunications company Telmex was privatised in 1990. Taking advantage of its monopoly power, the company charged high prices, contributing to Mexican investor Carlos Slim becoming the richest person in the world in 2010. Firms which were not privatised, such as oil company PEMEX and electricity company CFE, also charged high prices due to their low productivity. Mexican energy prices fluctuate drastically and were over four times higher than in the US in 2018. These issues were exacerbated by electricity shortages and power cuts (Bloomberg 2018). The privatisation of banks following the 1995 financial crisis also led to abuses of monopoly power as banks focused on charging exorbitant fees instead of providing credit to businesses (Blecker 2022; Harvey 2005).

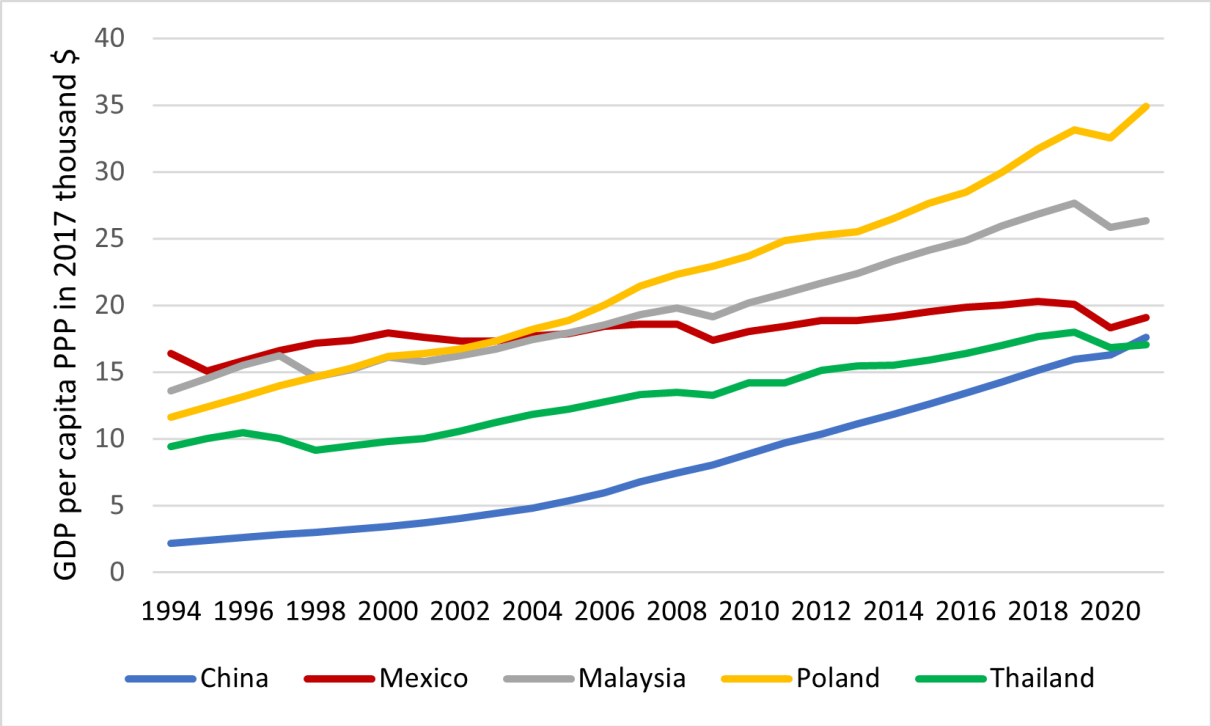
Third, China's accession to the WTO in 2001 reduced Mexico's preferential market access to the US market relative to its competitor. According to the theory of factor price equalisation, it

also undermined the potential for wage growth in Mexico. Given that Mexico and China were competing in the same market, wages in Mexico could not rise as long as Chinese wages were lower. By 2011, however, China's average hourly wages had already surpassed Mexico's (TACNA 2023). Although China and other Asian economies had state-owned companies, monopoly power, and other market distortions decried by neoclassical economists, they witnessed rapid and sustained economic growth, as detailed in the next section. Market distortions were used to promote economic growth through structural transformation. China undermined Mexico's comparative advantage in manufacturing exports precisely because it implemented structuralist instead of neoclassical economic policies.

2.5.2. Experiences of Other Countries

Figure 3 compares Mexico's GDP per capita at purchasing power parity (PPP) since NAFTA with that of China, Thailand, Malaysia, and Poland between 1994 and 2021. To make comparisons more favourable to Mexico, I analyse growth rates from 1995 (low value due to the Mexican financial crisis) to 2019 (before the COVID-19 recession). During that period, China's GDP per capita PPP in constant 2017 US dollars increased nearly sevenfold, Poland's nearly tripled, and Malaysia and Thailand's nearly doubled. By contrast, Mexico's GDP per capita PPP grew by 33 per cent. Between 2000 and 2018, Mexico's GDP per capita growth rate averaged 0.8 per cent per year, by contrast to 1.4 per cent for Latin America (Blecker 2022: 227).

FIGURE 3. GDP PER CAPITA (PPP) OF SELECTED ECONOMIES (1994-2021)



Source: Author's own based on data from World Bank (2023)

China implemented structuralist economic policies to catch up rapidly with the technological frontier, often ignoring WTO policy space restrictions and norms until it had built its innovative capabilities (Fu 2015; Gallagher and Porzecanski 2010; Rodrik 2007). The Chinese government provided financial support to state-owned enterprises, promoted technology transfer from multinationals to local firms, and imposed local content requirements. China's high growth rates enabled other Asian countries to benefit from its growth engine but also crowded them out from certain manufacturing activities. Malaysia and Thailand, more comparable to Mexico in terms of size and level of GDP per capita, emulated some of China's policies, albeit with less impressive results in terms of growth rate or development of national champions. By the late 2000s, China's progress up the value chain and increased wages meant that other countries in Asia, such as Vietnam, could become manufacturing powerhouses by proposing lower labour costs.

While Asian countries retained policy space and implemented structuralist economic policies, Eastern European countries such as Poland experienced economic growth while restricting their policy space, just like Mexico. In contrast to NAFTA, however, membership in the European Union generated deeper economic integration. Most importantly for economic development, it included freedom of movement, a customs union, and structural policies aimed at reducing regional differences in economic development. Freedom of movement and a customs union also reduced trade costs. In North America, the rules of origin necessary to mitigate the lack of a customs union were estimated to cost 36 billion US dollars annually, while border checks and delays cost an estimated 27 billion (Pastor 2011: 197). The EU regional cohesion policies are financial programs funded largely by Western European countries which are spent on public infrastructure and development programmes in poorer regions of the EU. Although the EU took away policy space from countries, it compensated for this loss by implementing structuralist policies at the supranational level.

The debate over the relative merits of structuralist and neoclassical economics will not be settled by the evidence in this chapter, in large part because of the difficulty of establishing counterfactuals (Harrison and Rodríguez-Clare 2009). Chile illustrates this complexity. On one hand, despite signing a PTA with the US in 2004, the country's GDP per capita PPP surpassed Mexico's in 2004 and nearly tripled between 1990 and 2021 (World Bank 2023). This evidence would support the neoclassical analysis of North-South PTAs. On the other hand, Chile's lack of structural transformation remains glaring: it continues to rely on exports of raw materials, most notably copper, which nurture an undiversified, unequal and highly monopolised economy. Chile successfully implemented an industrial policy in some sectors, such as its salmon industry, but did not succeed in moving up manufacturing value chains.

2.6. Conclusion

Writing at the turn of the millennium, Amsden (2001: 292-3) observed that 'two submodels promise to vie for global market share and mentoring in the next ten to twenty years: the "independent" approach of China, India, Korea and Taiwan and the "integrationist" approach of Argentina, Chile, and especially Mexico'. While the 'independent' strategy centred on activist trade and industrial policies (ATIP) to build domestic capabilities, the 'integrationist' approach focused on attracting foreign investment by securing stable and preferential access through PTAs with high-income markets, in the process relinquishing policy space for ATIP. The first approach drew from structuralist economic thought and the second from neoclassical economics.

This chapter contrasted neoclassical economic models' predictions that NAFTA would cause minimal disruption in the US and US-Mexico economic convergence with the reality of highly localised adjustment costs and economic divergence. It sought to demonstrate the continued relevance of the structuralist economic school in explaining the relationship between trade policy and economic development. While free trade generates economic development according to neoclassical economists, structuralist economists argue that free trade produces uneven development: countries in the global South gain less as they remain stuck in a comparative advantage of low value-added production and low-wage jobs (Kiely 2007: 13-24). The experiences of Japan, South Korea, Taiwan and China, the few economies in the global South which experienced rapid catch-up, suggest that activist trade and industrial policies *and* market access to the global North are necessary for economic development. The next chapter develops this insight to build a typology of US trade policies centred around the global South's access to the US market *and* space for industrial policies.

Chapter 3. Eras of US Trade Policy

> *For a long time, USTR had the view that our clients are the multinational companies that are doing business across borders, and we're just going to lower barriers everywhere so that those multinationals can do well. And we disagree with that. And I think your average American disagrees with that. Our view is trade agreements should help further the economic goals in the country. And so it requires you to kind of step back and say, what are the economic goals with the country? Within the Trump administration, one of these was: we want to have more manufacturing, we think our national security is linked to having strong supply chains, which now everybody says is conventional wisdom but it wasn't, it wasn't three years ago.*
>
> Trump administration official, interview, 10 March 2021

3.1. Introduction

Trade rules, whether formal or informal, influence opportunities for development in the global South. Since WWII, those rules have largely been determined by the US, which was the hegemonic power. Drawing on the structuralist economic interpretation of the relation between trade and development detailed in the previous chapter, this chapter creates a typology of US trade policies based on two dimensions impacting development in the global South: the level and stability of access to the US market, and US trading partners' space for industrial policies. By contrast to most historical accounts of the impact of US policy on the global South, which distinguish between pre-and post-1980 eras (Amsden 2007; Gerstle 2022), this chapter identifies three eras of US trade policy responses to political-economic changes between World War II and 2016 and their resulting consequences for productive development opportunities in the global South. Although the US ability to design the trade regime weakened as other countries gained global market share, it remained by far its main architect, even during the fourth era which began with the Trump administration (2017-).

The first era of US trade policy, from 1944 to 1970, focused on helping US strategic allies develop. The US implemented trade liberalisation, providing its allies with stable access to its market. In the context of the Cold War, the US also encouraged allies' industrial policies in the late 1940s and 1950s and tolerated their industrial policies in the 1960s. The second era, from 1971 to 1990, was a direct reaction to the success of the previous policy as the economic development of US allies pressured the US government to protect its producers from import competition. Market access became increasingly unstable as the US resorted to trade sanctions and non-tariff barriers to trade. The US contested trading partners' industrial policies, although they were not formally restricted by trade agreements. In the third era, from 1991 to 2016, the US succeeded in formally restricting trading partners' industrial policies in exchange for abandoning its policy tools creating market access uncertainty. This policy helped US-headquartered multinationals create export platforms abroad. In 2017, Trump's campaign against NAFTA, in the context of China's rise, constituted a reaction to this third era of US trade policy as stable market access and restrictions on trading partners' industrial policies (in particular the protection of intellectual property and investments) both incentivised multinationals to offshore production, causing significant adjustment costs in the US.

In each protectionist era, path dependence constrained changes in US trade policy through the mechanisms of increasing returns and veto power. During the 1970s-80s, US multinationals resisted protectionism due to the economic returns generated by post-WWII trade liberalisation (Milner 1988), while US Presidents vetoed some of Congress's attempts to protect domestic industries (Dryden 1995). In the protectionist era sparked by the Trump administration, multinationals also lobbied to maintain trade liberalisation, while Congress instead of the executive sought to preserve trade liberalisation. By showing how US trade policy has responded to structural changes in the global economy, this chapter foreshadows the importance

of path dependence in the NAFTA renegotiation while also contributing to debates on the history of US trade policy.

3.2. Accounts of US Trade Policy

Most historians and economists, whether neoclassical or structuralist, emphasise two eras of US foreign economic policy: pre- and post-1980 (albeit they diverge on the impact of post-1980 US policy on the global South). Structuralist economist Alice Amsden, for instance, distinguishes two American 'Empires' with opposite consequences for development prospects in the global South:

> Under the First American Empire, from 1950 to 1980, the world enjoyed an economic Golden Age. Growth in developing countries, whether Africa or the Middle East, soared […] As the 1970s passed, as news went from bad to worse, the plucky, prosperous era lasting from Franklin Roosevelt to Richard Nixon came to a halt. A Second American Empire arose in 1980, with the elections of Ronald Reagan and Margaret Thatcher. Soon a debt crisis convulsed poor countries, and for at least the next 25 years the Second American Empire's orthodox medicines failed to revive them (Amsden 2007: 1).

Amsden argues that the first era of US policy towards the global South was characterised by tolerance of trading partners' industrial policies, provision of non-reciprocal market access, and a stable monetary system, whereas the second period consisted of trade agreements restricting trading partners' policy space, protection of US manufacturing industries, and a US monetary policy inconsistent with the needs of the global South (Amsden 2007: 3, 48). The first era gave way to the second due to a combination of events occurring in the 1970s: the costs of waging war in Vietnam, the oil shocks of 1973 and 1979, import competition from Japan, and cheap credit provided at floating interest rates to the global South. She points to the fact that most countries of the global South witnessed higher annual growth rates in 1950-1980 than in 1980-2000.

Similarly, historian Gary Gerstle (2022; cf. Fraser and Gerstle 1989) distinguished between the pre-1980 New Deal order and the post-1980 neoliberal order in US policy. The 'New Deal order' echoes Amsden's argument that US policy towards allies in the global South was more benevolent. As to the neoliberal order, it was spread abroad through the US domestic policy of combating inflation. Federal Reserve Chair Paul Volcker, appointed in 1979 by Jimmy Carter, raised US interest rates to a peak of 20 per cent in 1981. This was hardest felt by countries in the global South which defaulted on their debts, having borrowed in US dollars under floating interest rates. For their debts to be refinanced, those countries implemented structural adjustment programmes largely designed by the International Monetary Fund (IMF) and the World Bank. Structural adjustment entailed a shift from structuralist to neoclassical economic policies through the abandonment of infant industry protection and other industrial policies in favour of liberalisation, privatisation, and deregulation. The consensus is that 1980 was a US-led turn in world policy towards privatisation, deregulation, and liberalisation (Burgin 2012; Harvey 2005; Levy 2021; Prasad 2006).

US trade policy under Reagan was not characterised by trade liberalisation, however, but rather by the imposition of trade remedies (temporary tariffs), the multiplication of non-tariff barriers, and pressures on economic competitors to impose voluntary export restraints. By contrast to the US liberal trade policy from 1944-70 and 1991-2016, the US trade policy under Nixon, Carter, and Reagan was protectionist (Dryden 1995; Irwin 2017; McKenzie 2020; Ruggie 1982: 405). The neoliberal narrative cannot explain US protectionist policies from 1971-90. Although ideologically committed to free trade, US presidents during this period implemented protectionist policies to avoid more radical action from Congress, framing their policies as providing temporary breathing space to domestic firms hurt by import competition, as well as a tool to maintain the US technological edge in new industries (Rowe, *forthcoming*). It was only in the 1990s with the creation of the WTO and the signing of bilateral PTAs that the US returned

to a free trade policy. As such, arguing that US policy in 1980 reflected the Washington Consensus of trade liberalisation conflates free trade with the other pillars of neoliberalism. The 1980 cut-off point does not apply to US trade policy. Drawing on the structuralist economic analysis of Chapter Two, the next section provides a framework to understand the evolution of US trade policy and its consequences on the global South.

3.3. A Development-Oriented Typology of US Trade Policies

Due to US economic and political hegemony post-WWII, US trade policies played a decisive role in shaping development prospects abroad. US trade policy mattered as countries with stable and high access to the US market could develop through export-led growth. US trade policies also mattered because they largely shaped the trade policies of other countries, and thus the overall trade regime. Following Krasner (1985: 4):

> Regimes are principles, norms, rules, and decision-making procedures around which *actor expectations converge*. Principles are a coherent set of theoretical statements about how the world works. Norms specify general standards of behaviour. Rules and decision-making procedures refer to specific prescriptions for behaviour in clearly defined areas (emphasis added).

Trade regimes include not only traditional trade rules and norms such as tariff levels and expectations of compliance with trade rules, but also non-tariff barriers to trade such as rules on foreign investment, intellectual property, and sanitary standards (McKenzie 2020). Although modern trade agreements can include financial rules, such as on exchange rate determination and capital mobility, those issues form the international financial regime and are typically governed by financial institutions such as the International Monetary Fund (IMF). Financial rules are sometimes referred to in this chapter given their influence on the trade regime. Finance shapes the trade regime, such as financial liberalisation enabling MNCs to invest abroad and

repatriate their profits. Finance is also shaped by the trade regime, such as stable access to the hegemon's market favouring capital flows to the global South.

While actor expectations must converge for a trade regime to exist, not all actors are equal. A hegemonic actor in particular will influence the behaviour and expectations of other actors. Historically, the hegemon's support for the trade regime has been essential in ensuring other countries' support. As the largest economy in the interwar period, the US was already shaping the trade regime, precipitating a trade war in the 1930s by implementing the Smoot-Hawley tariffs. In 1950, countries did not ratify the Havana Charter once it became clear that the US preferred the Generalised Agreement on Tariffs and Trade (GATT) over the creation of an International Trade Organisation (McKenzie 2020: 11, 182). In the 1970s and especially the 1980s, the US nearly broke the GATT system by imposing unilateral tariff and non-tariff barriers to trade (Ibid.; Dryden 1995). In the 1990s, the US was crucial to the revival of a rules-based trade regime through the creation of a World Trade Organisation (WTO) regulating new areas including investment, services, and intellectual property. Since WWII, an analysis of global trade regimes must thus centre on US trade policy.

US trade policy had an impact on the productive development opportunities of its trading partners. Productive development is defined as the acquisition of domestic productive and technological capabilities, with countries in the global South having relatively fewer capabilities than countries in the global North (Amsden 2001: 5-6; Rodrik 2004). Historically, productive development has driven long-term economic development. Drawing on the structuralist analysis of the previous chapter, two different US trade policies are retained here as particularly influential on the productive development of its trading partners: the level and stability of access to the US market provided to trading partners; and US tolerance of trading partners' industrial policies.

First, high and stable access to the US market facilitates productive development in trading partners by stimulating their export sector. While the level of market access can be measured by average US tariffs, market access stability is more difficult to measure given that it partly relies on expectations. Stable access to the US market reduces investment uncertainty, thereby incentivising firms to make long-term investments in export capacity abroad. Foreign direct investment promotes technological diffusion, although this process is not automatic but rather conditioned by the capabilities of domestic firms and the regulatory environment (Rugraff, Sánchez-Ancochea, and Sumner 2009; Fu, Emes, and Hou 2021). Exporting to the US market also enables countries to acquire dollars, which are key to buying the capital goods imports necessary for industrialisation.

Second, US tolerance of the global South's activist trade and industrial policies facilitates the latter's productive development. Industrial policies aim to transform the structure of an economy by developing higher domestic productive and technological capabilities. Historically, they typically included tariff and non-tariff barriers aimed at protecting infant industries, export subsidies to conquer foreign markets, as well as policies designed to gain technological capabilities such as weak protection of foreign intellectual property and active use of local content or technology transfer requirements on FDI (Chang 2002). Although the role of industrial policies in promoting economic growth remains controversial, with structuralist economists arguing in favour of activist trade and industrial policies and neoclassical economists generally preferring free trade and free markets, both schools converge on the importance of knowledge diffusion from North to South in promoting structural change (Amsden 2001; Bhagwati 2004: 182-85; Lester and Zhu 2019; Rikap 2021). This dimension has more long-term consequences on productive development than the first (access to the US market), which provides export opportunities but not necessarily structural change (Chang, Irfan, and Hauge 2016: 132).

A two-by-two matrix is constructed from the two US trade policies influencing prospects for productive development in the global South: the level and stability of access to the US market, and US tolerance of trading partners' industrial policies (Figure 4). The analysis focuses on the stability rather than the level of access to the US market given that, since its trade liberalisation post-WWII, the US has maintained average tariffs of 5-6 per cent (cf. Figure 5), yet the stability of access to the US market varied considerably as it resorted to trade remedies and non-tariff barriers. With regard to Cold War rivals, the US implemented higher tariffs and export controls aimed at undermining technology transfer. As such, those countries do not fit the classification below (except for the period 1991-2016 as discussed below).

FIGURE 4. DEVELOPMENT-ORIENTED TYPOLOGY OF US TRADE POLICIES

Access to the US market

Tolerance of trading partners' industrial policies		**Stable (and open)**	**Uncertain (and open)**
	Authorised	Magnanimous	Competitive
	Restricted	Restraining	Power-based

The US pursues a *magnanimous* trade policy when it provides high and stable market access while trading partners' industrial policies are authorised under the trade regime (designed largely by the US since WWII). A *competitive* trade policy occurs when access to the US market is uncertain but trading partners' industrial policies are authorised under the trade regime. A *restraining* trade policy is one where access to the US market is stable but the use of most industrial policies is restricted. A *power-based* trade policy is characterised by both uncertain access to the US market and restrictions on trading partners' ability to use industrial policies. The next section applies this typology to analyse US trade policy since WWII.

3.4. Application to US Trade Policy since WWII

The analysis starts from WWII as the US could not play the role of economic hegemon until the early twentieth century and refused to do so in the interwar period (Kindleberger 1973). As US government objectives evolved from developing strategic allies (1944-70) to protecting domestic producers (1971-1990) to helping US multinationals create export platforms abroad (1991-2016), US trade policy shifted from magnanimous to competitive to restraining, respectively. Except in the latter period, US trade policy towards China and Russia was different from US trade policy towards the rest of the world given that they were considered geopolitical rivals, which entailed restrictions on market access and export controls. 2017 marked a return to this differentiation.

3.4.1. Develop Strategic Allies (1944-1970): Magnanimous Trade Policy

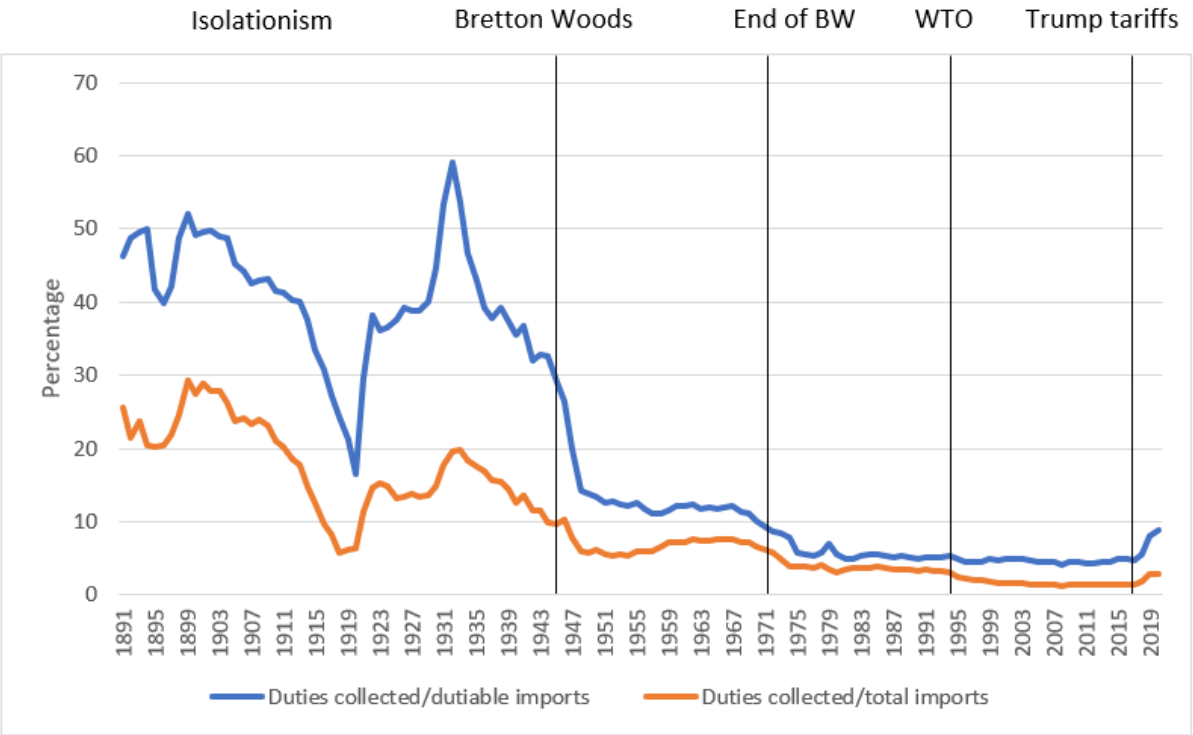
At the end of WWII, the United States was the undisputed global economic hegemon: it controlled 70 per cent of global financial assets and its economy produced more than half of the world's manufacturing output (Wilkinson 2006: 24). US economic and military hegemony during WWII enabled it to dictate the rules of global economic governance at the 1944 Bretton Woods conference. In trade, the US government initially agreed to the creation of an International Trade Organisation (ITO). By 1950, however, persisting opposition from the US Congress over the ITO's founding document, the Havana Charter, led US President Truman to withdraw US support for an ITO, resulting in no other country ratifying the Havana Charter. The General Agreement on Tariffs and Trade (GATT), more limited in scope, became the platform to establish trade rules and negotiate tariff liberalisation between member countries. The rules were largely determined by the US with inputs from other Western industrialised powers, reflecting US economic hegemony (McKenzie 2020: 11-13). In the following decades,

the GATT progressively expanded to include most non-communist countries, but also some members of the Soviet Bloc such as Czechoslovakia (founding member), Poland (1967) and Romania (1971) (McKenzie 2020: 88-93). Some exceptions remained, however, notably the USSR and China which hardly benefited from US market access liberalisation due to the Cold War.

The US created a trade regime based in principle on the recognition of the superiority of free trade. Trade liberalisation reflected both US economic interests as the most competitive country and US leaders' support for the role of free trade in promoting peace and prosperity (Krasner 1985: 61). Many foreign leaders at the time agreed that the protectionist policies adopted by rich countries after the Great Depression, starting with the 1930 Smoot-Hawley tariffs in the US, exacerbated the global economic slump and contributed to the outbreak of WWII. The trade liberalisation process began in 1934 as President Roosevelt obtained authorisation from Congress to negotiate trade agreements. It continued post-WWII due to the combination of specific tariffs and high inflation in the US. The GATT, designed as a tool for countries to negotiate trade liberalisation, led to sharp tariff cuts during the Kennedy (1964-7) negotiating round.

Figure 5 shows the evolution of US average tariffs between 1891 and 2020. Between 1944 and 1971, average US tariffs on dutiable imports fell from 33 to 9 per cent (they still fell slightly in the next few years, in part due to prior commitments: the Kennedy round tariff cuts were implemented progressively). Some sectors remained protected, however, such as agriculture and textiles, to the detriment of the global South (Amsden 2007: 3; Ruggie 1982: 403).

FIGURE 5. AVERAGE US TARIFF RATES (1891-2020)



Source: Author's own based on data from the US International Trade Commission (2021).

Although preaching free trade, in practice the US encouraged allies' use of industrial policies to catch up economically during the late 1940s and 1950s and mostly tolerated them in the 1960s, in large part due to its prioritisation of military cooperation and containment of communism (Maxfield and Nolt 1990; Helleiner 2014; Amsden 2007: 47). The US provided technology transfer to its strategic allies (in particular in Europe and Asia), while the trade regime did not contain intellectual property protection (Amsden 2007). Furthermore, the US often tolerated allies' use of infant industry protection and technology transfer policies, such as counterfeiting and reverse-engineering, implemented in particular by Japan, South Korea and Taiwan to develop domestic technological capabilities (Amsden 1989; Wade 1990; Chang 2002).

In Western Europe, the US encouraged its allies to form a regional economic union and allowed them to protect their national champions (McKenzie 2020: 108, 119, 136). France implemented

a dirigiste economic policy set by President De Gaulle to develop capabilities in economically and militarily strategic industries such as automobiles and nuclear power. West Germany resorted to widespread import restrictions, which were largely tolerated by the US due to the Cold War (McKenzie 2020: 124-5). Similarly, the US encouraged Latin American industrial policies during the post-war era. This policy was supported by US multinationals as they invested in those countries to produce for the domestic market and were shielded from import competition by high tariff barriers (Maxfield and Nolt 1990). Given that the US also provided high and stable market access, its trade policy in this period was *magnanimous*, following the classification developed in the previous section. These characteristics held the strongest for US strategic allies but also applied to other countries with a few exceptions (most notably the USSR and China) (McKenzie 2020: 91-93). In the case of the USSR, China, and other geopolitical rivals, access to the US market was low and the US resorted to export controls to undermine technology transfer (Ibid.).

In addition to the rapid economic development of the USSR, US allies in Europe and Asia experienced unprecedented economic growth, leading to the progressive erosion of US economic hegemony (Wilkinson 2006: 71). Most Western European countries had recovered their pre-war economic output by 1950. Between 1950 and 1973, growth rates per year averaged 2.5 per cent in the UK, 4.1 per cent in France and 5 per cent in West Germany, by contrast to 2.2 per cent in the US (Marglin et al. 1990: 47). In Europe, West Germany quickly recovered its position as the continent's industrial powerhouse. Japan's post-war economic boom was even more impressive, with its GDP growing at 8.4 per cent per year during the same period (Ibid.). Japan's share of world manufacturing output increased from 2.9 per cent in 1953 to 8.8 per cent by 1973 (Huntington 2011: 86). Other US allies in East Asia also experienced high growth rates, such as Taiwan and South Korea. In Latin America, Brazil and Mexico doubled

their joint share of the world's manufacturing output from 0.8 per cent in 1938 to 1.6 per cent in 1973 (Ibid.).

In the 1960s, as the US became less competitive economically and its capital account deficit surged, other countries began to question the US commitment to maintain dollar convertibility into gold, which was the foundation of the international monetary system. By 1971, the US trade balance had shifted from a post-war surplus of ten billion US dollars to a deficit (Brett 1983: 173). The US capital account had remained in deficit since 1950 and reached 19.8 billion dollars in 1971. By the mid-1960s, the US was running persistent trade deficits with Japan and West Germany (Kiely 2007: 60). To restore US competitiveness and prevent a run on the dollar, President Nixon abandoned gold convertibility in 1971 and forced Japan and large European countries to revalue their currency against the dollar, marking the end of the Bretton Woods monetary system (Stein 2010: 42-7). Those measures were combined with an across-the-board ten per cent tariff which signalled the beginning of a 'new protectionism' in US trade policy characterised by unstable access to the US market and contestation of trading partners' industrial policies (Dryden 1995: 149-52; McKenzie 2020; Ruggie 1982: 405, 410).

3.4.2. Protect Domestic Industry (1971-1990): Competitive Trade Policy

After a short revival, by 1973 the fixed exchange rate regime of Bretton Woods had entirely succumbed to floating exchange rates. On the trade front, despite the import competition faced by the US industry in the 1970s, the US did not revert to the protectionist policies of the 1920s (Milner 1988; Stein 2010). Nixon removed the ten per cent tariff four months later, GATT negotiations continued to produce some tariff liberalisation (Tokyo Round concluded in 1978), and by 1975 the US provided preferential market access to some countries of the global South through the Generalised System of Preferences (GSP). Milner (1988) attributes this continuity

to US firms' higher export dependence and transition into multinationals by the 1970s, which increased the costs of protection. Her research points to the importance of path dependence: as the US became more integrated into the world economy post-WWII, a return to pre-war protectionist policies became undesirable due to the costs of breaking increasing returns from the GATT. Another important reason for continuity is the US government's objective of preserving the world order it had created (Stein 2010). In the 1970s, geopolitics continued to be prioritised over economics in the making of US trade policy (Ibid.; Dryden 1995; Irwin 2017). Although the US government increasingly contested trading partners' export-led growth model, it did not succeed in significantly changing their trade and industrial policies (Stein 2010: 171, 255).

Although US protectionism was less radical than in the 1920s, it took new forms that were costly to its trading partners given the increase in global economic integration. While US average tariffs on dutiable imports remained relatively stable during the 1970s and 1980s (on average 5-6 per cent, cf. Figure 5), in practice the stability of access to the US market deteriorated as the US government resorted to trade remedies (temporary tariffs) and non-tariff barriers (NTBs) to trade. Following the '*de facto* abandonment of the GATT's dispute settlement procedures', the US developed unilateral trade sanctions through the 1974 Trade Act. This included the creation of Section 301 targeting 'unfair' trade practices, which was used extensively in the 1980s to reduce imports (Wilkinson 2006: 73-4). The US created market access uncertainty by removing countries from its Generalised System of Preferences schemes and forcing allies to impose voluntary export restraints. In the context of increasing competition from European and East Asian firms and instability caused by the 1973 and 1979 oil shocks, the US government sought to protect its society from trade shocks (McKenzie 2020: 18, 94; Stein 2010). Given that the US did not negotiate trade agreements comprehensively restricting

trading partners' industrial policies until the 1990s, its trade policy during 1971-1990 was *competitive.*

As tariff rates were bound by national commitments under the GATT, countries increasingly resorted to temporary tariffs and NTBs to protect their domestic producers. The US (but also European countries and Japan) implemented antidumping and countervailing duties, technical and administrative regulations, sanitary and phytosanitary standards, quotas, government procurement restrictions and other restrictions to protect their domestic producers. Between 1966 and 1986, the share of imports protected by NTBs increased from 36 to 45 per cent in the US, from 25 to 54 per cent in the European Economic Community (EEC), and from 31 to 43 per cent in Japan (Irwin 2017: 613). By the end of the 1970s, 'as much as one-fifth of OECD manufacturing imports were affected by quantitative restrictions […] a quadrupling over the decade' (Ostry 1997: 76-7). These mostly constituted a defensive strategy: protecting domestic firms and workers from import competition. While the US was already experiencing competition from Europe and Asia by 1970, the economic transformations of the next twenty years would further increase demands for protectionism.

Korea and Taiwan participated in Japan's economic miracle as their national champions supplied Japanese firms. The Korean and Taiwanese governments imitated the Japanese developmental model, transforming their economies by implementing activist trade and industrial policies (Amsden 1989; Wade 1990; P.B. Evans 1995). They conditioned industry protection on export targets and resorted to technology transfer through weak protection of intellectual property, arguing that imitation was a necessary step in the development process (Wade 1990: 268-9). Foreign direct investment was also regulated to ensure technology transfer and increased local content. To finance their industrialisation despite US aid drying up by the late 1960s, they increasingly relied on incentives for high rates of savings, capital controls, and restrictions on the consumption of luxury goods, which allowed them to discipline banks and

other capitalists into funnelling capital to national champions (Amsden 2001; Wade 2018). By the early 1990s, following Deng Xiaoping's economic liberalisation reforms, China had also become part of the East Asian industrial powerhouse, with core firms such as Taiwan's national champion Foxconn producing in Shenzhen.

Taiwan and South Korea's GDP grew on average at more than six per cent per year between 1962 and 1997, while from 1978 China experienced even higher growth rates, averaging nearly ten per cent per year until 2007 (Wade 2018: 523; Gallagher and Porzecanski 2010: 5). Combined with automation, the rise of East Asian competitors caused adjustment costs in the West, especially within the US given its previous hegemony on world markets and the limited development of its welfare state. From a peak of 19.6 million in 1979, US manufacturing employment declined by 13 per cent to 17 million by 1991 (US Bureau of Labor Statistics 2021). Japan's spectacular economic growth threatened US economic hegemony as Japanese manufacturers outcompeted their counterparts in the US in an increasing number of industries, in particular automobiles and electronics. By 1987, Japan had surpassed US GDP per capita levels in current US dollars, a position it would retain until 2001 (World Bank 2022a).

As competition from East Asia threatened US economic hegemony, the election of Ronald Reagan in 1980 led to a stronger US commitment to curb trading partners' industrial policies, yielding mixed results under his presidency yet laying the foundations for the policies of the early 1990s. Domestically, Reagan campaigned against government intervention in the economy, which he argued had contributed to stagflation in the 1970s. Once elected, he sharply decreased taxes and welfare provisions while implementing deregulation and privatisation policies. Paradoxically, Reagan increased total government spending by relaunching the arms competition with the USSR, which constituted in effect an industrial policy supporting military innovation. This industrial policy would later yield multiple economic pay-offs and reinforce the US position as the global economic leader. Most notably, the Defense Advanced Research

Projects Agency (DARPA) played a key role in developing the internet and supporting new US national champions such as Google and Apple (Mazzucato 2011). Reagan's tax cuts and high military spending increased the US trade deficit, however, which exacerbated tensions with US trading partners.

In trade, Reagan imposed trade remedies aimed at protecting US workers from 'unfair competition' and forcing other countries to abandon their industrial policies. Although conditioning access to the US market on policy space restrictions yielded partial results for some countries, this trade-off was not formally integrated into the global trade regime until the 1990s with the signing of PTAs and the creation of the WTO. The US imposed a variety of unilateral trade sanctions to pressure trading partners into accepting new commitments. The Reagan administration used trade sanctions developed by the Nixon and Ford administrations, such as Section 301 of the 1974 Trade Act, which enabled the executive to impose trade sanctions to incentivise a trading partner to remove policies or practices that the US considered 'unreasonable, unjustifiable, or discriminatory' and that 'burden or restrict US commerce' (Irwin 2017: 607). Reagan expanded Section 301 by passing through Congress in 1988 a 'Super 301' provision requiring the US Trade Representative (USTR) to identify priority countries and pressure them into providing greater market access to US exports, as well as a 'Special 301' provision allowing USTR to identify countries breaking US intellectual property rights and negotiate higher protection (Irwin 2017: 607-12).

During this period, changes to the global economy which had begun in the 1970s accelerated (Baldwin 2019: 54). Improvements in information and communication technology reduced the coordination costs linked with offshoring and outsourcing production. By 1991, the entry of China (which had already begun in the 1980s), India, and former Soviet Union countries within the capitalist system doubled the global labour force, creating immense offshoring opportunities to take advantage of low-wage labour (Gerstle 2022: 145; Milberg 2013: 51). Trade in

intermediate goods, which was insignificant in 1970, increased to nearly 2 trillion US dollars by 1991 and would reach 8 trillion by 2008 (Ibid.: 38). To fully seize the opportunities of creating export platforms in the global South, US multinationals pressured their government to sign trade agreements that protected their investments and intellectual property abroad while stabilising access to the US market for their exports (Rodrik 2018).

3.4.3. Create Export Platforms (1991-2016): Restraining Trade Policy

As the Reagan and Bush Sr. administrations became increasingly frustrated with the lack of progress on negotiating new GATT provisions based on trade liberalisation and the removal of industrial policies, they sought to address those concerns in bilateral trade agreements instead. The US had already negotiated a bilateral PTA with Canada in 1986-7 (CUSFTA), during which the Canadian government sought to eliminate the use of trade remedies given that the US had been extensively applying them in the 1970s and 1980s (Canada obtained binational dispute settlement panels instead – CUSFTA chapter 19). Mexico's proposal in 1990 to negotiate a bilateral trade agreement offered the US an opportunity to exert further pressure in GATT negotiations by threatening to focus on bilateral and regional agreements instead (Cameron and Tomlin 2000: 6). Building on its bilateral PTA with Canada negotiated in 1987, the US demanded new trade rules protecting foreign investment, services, and intellectual property (Lustig 1992: 131-2). By contrast to other countries in the global South, Mexican President Salinas de Gortari was ready to accept commitments in all three areas given that he was desperate to attract foreign capital and committed to neoclassical economic ideas (Ibid.: 1-2).

While Mexico already benefited from preferential access to the US market under the GATT Generalised System of Preferences (GSP), this access could be removed at any time by the US

Congress or impeded by temporary tariffs such as antidumping duties (Shadlen 2005). In 1987, for example, the US withdrew Mexico's GSP treatment for some chemical products in protest of Mexico's weak intellectual property protection. The US placed Mexico on its 'priority watch list' a year later (Lustig 1992: 129-30). The Mexican government responded in 1991 by strengthening intellectual property protection, including increasing patent terms from fourteen to twenty years, which was essential for progress on a US-Mexico trade agreement. Given the high share of Mexican products entering the US market through the GSP and other US tariff schedule exceptions (Sklair 1989: 8-13), the Mexican government believed that a trade agreement would stabilise preferential access to the US market, thereby increasing foreign investment inflows by reducing uncertainty (Manger and Shadlen 2014; Lustig 1992: 137; Shadlen 2008). A PTA would also reduce uncertainty by locking in liberalisation reforms (Lustig 1992: 134).

The North American Free Trade Agreement (NAFTA), signed in 1992, gave the US government most of what it wanted, especially with regard to intellectual property and foreign investment protection (Cameron and Tomlin 2000; Sell 2003: 55; Stiglitz 2020: 80). The agreement guaranteed patent protection for twenty years and contained the first Investor-State Dispute Settlement mechanism (ISDS). The US, Mexico and Canada committed to the progressive elimination of all their tariffs, the harmonisation of their non-tariff barriers, and the creation of dispute settlement mechanisms. After intense negotiations, Canada succeeded in keeping the trade remedies dispute settlement mechanism (DSM) of its 1989 PTA with the US, which became NAFTA Chapter 19. This DSM provided Mexico and Canada with an independent tool to contest the US imposition of antidumping and countervailing duties and, in cases when the DSM panel ruled in their favour, the right to retaliate by imposing trade sanctions. From a neoclassical economic perspective, NAFTA promoted Mexican economic development by enforcing sound economic policy: free markets and free trade. From a

structuralist economic perspective, NAFTA provided Mexico with stable access to the US market at the cost of severe restrictions on its policy space (Shadlen 2005).

At the GATT Uruguay Round, NAFTA negotiations incited other countries to make concessions to maintain the multilateral trade regime (Irwin 2017: 626, 651). Countries in the global South accepted sharp tariff cuts and bans on certain industrial policies such as export subsidies. By forming a united front, the US, Japan and Western Europe succeeded in pushing their intellectual property agenda, leading to the 'Agreement on Trade-Related Aspects of Intellectual Property Rights' (TRIPS) providing patent protection for twenty years (Sell 2003). They also succeeded in obtaining guarantees for the investments of their multinationals abroad in the 'Agreement on Trade-Related Investment Measures' (TRIMS), including the prohibition of most industrial policies aimed at disciplining foreign investment, such as local content and export performance requirements. In exchange for the inclusion of new trade areas such as intellectual property and investment protection, the US accepted constraints on its use of unilateral trade sanctions, such as a ban on voluntary export restraints and the creation of a WTO dispute settlement mechanism. This commitment was mostly respected during the twenty years following the creation of the WTO as the US favoured solving trade disputes through the WTO dispute settlement mechanism (Irwin 2017: 655). US trade policy in this period was thus *restraining*: it provided stable and high market access in exchange for countries committing to restrictions on their policy space. The WTO did allow some opportunities for industrial policies in the global South, however, in the form of 'Special and Differential' treatment. Following the end of the Cold War, China and Russia were integrated into the global trade regime (China acceding the WTO in 2001 and Russia in 2012);

Although NAFTA and the WTO represented a shift towards rule-based trade governance, they were shaped by North-South power asymmetries. At the multilateral level, the WTO TRIPS and TRIMS agreements undermined technology transfer and foreign investment regulation,

used in the past by late industrialisers to catch up (Chang 2002). Sharp tariff cuts and the ban on export subsidies deprived the global South of the tools historically used to develop national champions. The WTO's functioning also revealed that, behind the promise of a democratic system, important negotiations were conducted in a 'Green Room' between the most powerful countries. While the WTO dispute settlement mechanism allowed countries to legally challenge rule-breaking and obtain the right to retaliate, retaliation by small economies caused insignificant economic costs to large economies. Yet North-South power asymmetries were greatest in bilateral negotiations. Following NAFTA, some countries in Latin America and Africa competed to obtain stable preferential market access to the US and the European Union by signing trade agreements with them, in the process committing to drastic tariff cuts, TRIPS+ and TRIMS+ regulations, and renouncing 'Special and Differential' treatment, which further undermined their capacity to implement industrial policies (Shadlen 2008, 2017; Thrasher and Gallagher 2008).

By contrast, Asian countries abstained from signing PTAs with the US, thereby retaining the greater policy space provided by the WTO (South Korea signed a PTA with the US in 2007, by which time it was already a high-income country). Furthermore, some Asian countries, spearheaded by China, implemented industrial policies, sometimes breaking the letter or the spirit of their WTO commitments to facilitate technology transfer, develop domestic industries, and conquer export markets (Naughton 2021). Vietnam, Thailand, Malaysia and Indonesia implemented industrial policies, although to a lesser extent than China (Cherif and Hasanov 2019; Chesier and Penrose 2007). The US government targeted China in particular for violating its legal commitments under the WTO, such as by imposing local content and technology transfer requirements, export controls and subsidies, discriminatory taxes, and market access barriers (USTR 2021: 6-7). China was also accused of violating the spirit of the WTO by undervaluing its currency by thirty per cent during the 2000s to stimulate its exports and relying

on state-owned enterprises, which are weakly regulated under the WTO (Ibid.; Bacchus, Lester, and Zhu 2018). While some of these accusations have been substantiated by WTO dispute settlement panels, certain key aspects of Chinese industrial policy, such as capital controls, a high savings rate, and high R&D spending, did not break WTO rules.

China and other Asian countries' industrial policies have been accompanied by high economic growth and the rise to dominance of East Asian value chains. By 2019, Asia represented 52 per cent of the world's manufacturing output, followed by Europe (22 per cent) and North America (20 per cent including Mexico) (UNCTAD 2023). Asia's share of global container shipping traffic reached 62 per cent in 2015-17, while 60 per cent of all goods traded were within the region (McKinsey Global Institute 2019). The growth of Asian supply chains was accompanied by rising living standards in the region. By the 2016 presidential election, the 'China shock' had caused significant adjustment costs in the US leading to growing demands for protectionism (cf. Chapter Two).

3.4.4. Re-shore Production (2017-): Power-Based Trade Policy

US manufacturing workers who lost their jobs to import competition and automation could often only find precarious jobs, while those who kept their jobs faced declining real wages (Case and Deaton 2020). Their suffering was voiced by candidates Bernie Sanders and Donald Trump in the 2016 presidential campaign, who advocated for trade protectionism (Ibid.: 153-6). Trump blamed trade with China and Mexico in particular as reasons for US economic problems.

> Our politicians have aggressively pursued a policy of globalization - moving our jobs, our wealth and our factories to Mexico and overseas. […] NAFTA was the worst trade deal in history, and China's entrance into the World Trade Organization has enabled the greatest jobs theft in history (Trump 2016).

Although NAFTA's effect on the US economy was dwarfed by the China trade shock, Trump identified NAFTA as a symbol of the 'unfair' trade rules which, by facilitating offshoring, had undermined workers' bargaining power. Criticism of NAFTA was also rampant in the Democratic Party. By 2016, both Presidential candidates Hillary Clinton and Donald Trump pledged to renegotiate NAFTA. The Trump administration criticised the US post-1991 trade strategy focused on creating export platforms abroad. A Trump administration official recalled:

> For a long time, USTR had the view that our clients are the multinational companies that are doing business across borders, and we're just going to lower barriers everywhere so that those multinationals can do well. And we disagree with that. And I think your average American disagrees with that (interview, 10 March 2021).

By stabilising access to the US market and curbing trading partners' industrial policies, the previous *restraining* trade policy encouraged offshoring. Trump's trade representative Robert Lighthizer complained that NAFTA's Investor-State Dispute Settlement mechanism (ISDS) incentivised US firms to offshore production by guaranteeing the rule of law in foreign countries (Lighthizer 2020: 88). By 2017, the US government had changed its position from promoting the economic efficiency and international competitiveness of US multinationals, which entailed offshoring production, to keeping manufacturing jobs in the US. A Trump administration official recalled:

> All this stuff from the 90s, none of it worked. It was insanity to say 'Okay, what we're gonna do is we're gonna take our high wage economy, we're gonna merge it with these low wage economies, and then we're going to sell more stuff to them' […] But in America, in the 90s, and up until the time Trump was elected President, that was just common sense. Why would you pay Americans 25 dollars an hour to make cars when you can pay people in Mexico 3 dollars an hour (interview, 7 May 2021)?

Furthermore, the promise of curbing trading partners' industrial policies was only partially met, leading to growing frustration in the US:

> If you look at what the American politicians promised, and then you look at what happened, the promises and what happened didn't match. We were told that if we joined the WTO and we got dispute settlement, we'd be able to force Japan to open its market. Well, that turned out not to be true. We were told that if we joined the WTO and we got dispute settlement, we'd be able to get Europe to back off on some of its things like its policies blocking our beef. Well, that turned out not to be true. We were told that if we did this deal with Mexico our trade surplus with Mexico would grow because we would sell more stuff to Mexico. Well, that was also not true. We were told that if we did a trade deal with China, China will liberalise and become more open and more free. Well, that was also not true (Ibid.).

Since Trump, US trade policy towards China has reverted to the pre-1991 norm. China faces lower access to the US market as Trump imposed 25 per cent tariffs on Chinese products. The Biden administration has maintained the tariffs and imposed considerable export controls on China aimed at undermining technology transfer (Bown and Kolb 2023). To compensate US farmers for Chinese trade retaliation, Trump also provided billions in subsidies through the Commodity Credit Corporation, created during the Great Depression to stabilise prices and support farmers' income, which reduced all trading partners' access to the US market. Both Trump and Biden implemented industrial policies to maintain the US technological edge and reduce dependence on Chinese imports. This policy was extended to Russia following its invasion of Ukraine in 2022. Just as during the Cold War, US trade policy towards China and Russia has become largely determined by geopolitical imperatives. As such, it is necessary to analyse US trade policy towards allies to assess the degree of change in US trade policy.

With regards to its allies, US trade policy became *power-based*: access to the US market remains open but has become unstable as the US implements trade remedies and industrial policies, while trading partners still face WTO and PTA policy space restrictions. President Trump imposed safeguard tariffs of 30 to 50 per cent on solar panels and washing machines and national security tariffs of 25 per cent on steel and 10 per cent on aluminium (Bown and Kolb 2023). He threatened to impose tariffs on other products, most notably a 25 per cent tariff on passenger vehicles. He forced the renegotiation of the US-South Korea FTA (KORUS) to

include voluntary export restraints on steel and postpone the elimination of US tariffs on trucks (the US had originally agreed to eliminate its tariffs by 2019) (Lighthizer 2023: 288). Pursuing a policy started under Obama, Trump blocked the appointment of members to the WTO Appellate Body, which seized to function in December 2019 (Gantz 2021: 204). Since then, WTO dispute settlement resolutions have been *de facto* non-binding as members can 'appeal into the void', which occurred over twenty times between 2020 and 2023 (WTO 2023b). Summarising the spirit of the times, Hopewell (2021: 271) argued that 'President Trump is widely seen as reversing 70 years of US trade policy and abdicating the American hegemon's traditional leadership role in the multilateral trading system'.

Trump's trade policies have largely been maintained by the Biden administration, indicating a bipartisan shift towards protectionism. According to Krueger (2022), the Biden administration 'has failed to reverse its predecessor's disastrous policies, leaving American producers and their workers worse off'. During his first week in office, President Biden signed an executive order further strengthening 'Buy American' government procurement policies, which undermined US commitments in PTAs (The White House 2021). Although Biden sought to improve trade relations with US allies, he kept Trump's safeguard and national security tariffs. Just as Trump negotiated voluntary export restraints (VERs) with some countries (including Canada and Mexico) on steel and aluminium, Biden negotiated VERs with the EU and Japan (Lincicome 2022). His administration continued to block the appointment of members of the WTO Appellate Body. Biden provided large subsidies to domestic firms as part of the 2022 Inflation Reduction Act's green energy provisions and the CHIPS Act, which encouraged US production of semiconductors (Ibid.). Those policies violated WTO rules, which ban both VERs and subsidies linked to local content requirements.

Although the US has remained part of the WTO and all its bilateral trade agreements (as of 2023), it seized to pursue new trade agreements. Whereas every President since Reagan had

signed an FTA, starting with trade agreements with Israel in 1985 and Canada in 1989, the Trump and Biden administrations refused to sign FTAs (with the obvious exception of USMCA). In a public address, Katherine Tai, USTR for the Biden administration, echoed the concerns raised by her predecessor:

> We've been doing FTAs for almost forty years now. And while some sectors of the economy have benefited, many in this room know that the traditional approach to trade – marked by aggressive liberalization and tariff elimination – also had significant costs: concentration of wealth, fragile supply chains, de-industrialization, offshoring, and the decimation of manufacturing communities. […]. We believe industrial policy and trade policy must complement each other (Tai 2022).

Instead of FTAs, the Biden administration chose to negotiate agreements which promote new policy space restrictions without providing additional access to the US market, such as the Indo-Pacific Economic Framework and agreements on critical minerals, which form part of its industrial policy (US Department of Commerce 2023).

Just as in previous eras, the shift in US policy since 2017 shaped the trade regime. The European Union implemented its industrial policy to achieve 'strategic autonomy' while Japan and South Korea subsidised their national champions to move production out of China (Maciejewska and Alifandi 2023). The US call for 'reshoring', 'nearshoring' and 'friend-shoring', sparked by the US-China trade war, was adopted by other countries in the global North as new causes of supply chain disruption strengthened domestic calls for reindustrialisation, such as the COVID-19 pandemic, bottlenecks in key maritime routes such as the Suez and Panama Canals, Russia's invasion of Ukraine, and climate change. Between 2019 and 2022, the total number of trade restrictions imposed annually nearly tripled (IMF 2023). By contrast to previous eras of US trade policy, however, US support for the trade regime seems less essential: other countries have indicated that they will remain in the WTO even if the US exited, and pursue trade liberalisation without the US in the form of regional agreements such as RCEP and CPTPP.

3.5. Conclusion

Figure 6 summarises the eras of US trade policy between 1944 and 2023 based on the development-oriented typology detailed in section two. Except for the period 1991-2016, US trade policy towards China and Russia was distinct as they faced low access to the US market and US export controls.

FIGURE 6. ERAS OF US TRADE POLICY (1944-2023)



Source: Author's own.

From 1944 to 1970, the US pursued a *magnanimous* trade policy aimed at helping its strategic allies develop economically. The US offered high and stable market access while tolerating industrial policies or even assisting its allies through financial and technology transfers. As a response to rising competition from Europe and Asia, the US engaged in trade wars from the 1970s, leveraging its power asymmetry by unilaterally imposing non-tariff barriers. Given that

the US did not negotiate trade agreements comprehensively restricting the global South's industrial policies until the 1990s, its trade policy during 1971-1990 was *competitive*. Since 1991, to help its multinationals operate abroad, the US government pursued a *restraining* trade policy. It successfully negotiated the prohibition of most industrial policies in NAFTA, the WTO, and subsequent trade agreements in exchange for providing stable and increasing market access, especially for signatories of PTAs. By 2016, trade adjustment costs in the US provoked a backlash against the post-1991 trade policy, leading to a shift towards a *power-based* trade policy.

During the protectionist turn of the 1970s, US Presidents were constrained by path dependence to preserve some of the elements of the previous era. Despite similar economic disruptions to the 1930s, they did not revert to high tariffs due to the costs of breaking with the increasing economic returns created by the GATT system (Milner 1988). Instead, the US government implemented 'new protectionism' by undermining market access stability. Although US average tariff rates on dutiable imports remained stable, the widespread use of temporary tariffs and non-tariff barriers increased the costs and uncertainty of access to the US market. Similarly, US trade policy post-2017 preserved elements of the previous era, such as membership of the WTO and PTAs, while breaking with the spirit or the letter of those trade agreements, such as by providing subsidies tied to local content, requiring trading partners to impose voluntary export restraints, and refusing to support the dispute settlement system.

At first sight, the NAFTA renegotiation should epitomise the shift in US trade policy as Trump threatened to withdraw the US from the agreement, imposed tariffs on Mexican and Canadian steel and aluminium, threatened to impose tariffs on passenger vehicles, requested the elimination of all dispute settlement mechanisms (DSMs) and the creation of a 50 per cent US-specific auto rule of origin. However, USMCA maintained zero tariffs, rendered the state-to-state DSM operational and strengthened regional integration through stricter regional rules of

origin. Membership in USMCA even allowed Mexico and Canada to benefit from the subsidies provided by the US Inflation Reduction Act (Reinsch, Chauhan, and Duncan 2022). The next chapter examines changes in US trade policy towards its neighbours during the NAFTA renegotiation based on the development-oriented typology introduced in this chapter.

Chapter 4. USMCA: A Power-Based Trade Policy?

> *Once Ambassador Lighthizer was confirmed, we were able to see what the US meant by changing the agreement. And some things were not acceptable for us, and I don't think for the Canadians either because they would lessen the value of the agreement significantly. I think the most important one was the sunset clause as initially presented. If you have an agreement that every five years essentially dies and needs to be resurrected by the leaders of the three countries, that would have created significant uncertainty that would undermine the value of the agreement. One of the main purposes of an agreement like this is to attract long-term investment, so having an agreement that is potentially eliminated after five years would have been a major problem. It kind of defeats the purpose of providing certainty.*
>
> Negotiator, Peña Nieto administration, interview, 7 April 2021

> *I think respecting international treaties has a huge value for both sides. Respect by one country has a huge value for the other side and for itself. I believe in that. Not everybody in North America believes in that but Mexico does.*
>
> Jesús Seade, Mexican chief negotiator, López Obrador administration, interview, 15 October 2020

4.1. Introduction

Chapter Two introduced the logic of North-South PTAs pioneered in 1994 by NAFTA: countries in the global South restrict their use of activist trade and industrial policies in exchange for *stable* preferential access to markets in the global North (Shadlen 2008: 2). Chapter Three applied this logic to US trade policy since World War II, creating a development-oriented typology of US trade policies based on the stability of access to the US market and US tolerance of trading partners' industrial policies. US trade policy evolved from magnanimous (1944-70) to competitive (1971-90) to restraining (1991-2016) to power-based (2017-). Following the market access uncertainty caused by President Trump's tariffs and threats to

withdraw the US from NAFTA, however, USMCA preserved Mexico and Canada's access to the US market and reinforced regional integration. The extent to which the NAFTA renegotiation weakened the certainty of preferential access to the US market and further reduced space for industrial policies remains unexplored in the literature.

Drawing on the NAFTA and USMCA trade agreements, daily newspaper coverage and more than one hundred interviews conducted with actors and stakeholders of the NAFTA renegotiation, this chapter analyses the extent to which the renegotiation of NAFTA signalled a change in US trade policy by reducing market access certainty and space for industrial policies. It contends that, throughout the NAFTA renegotiation, the Trump administration sowed the seeds of a *power-based* trade policy by increasing uncertainty over Mexico and Canada's preferential access to the US market while demanding stronger policy space restrictions. The inclusion of a sunset clause in USMCA institutionalised uncertainty, while the pressure tactics used by the Trump administration during the NAFTA renegotiation and USMCA implementation also generated long-term uncertainty. Some of those tactics were replicated by the Biden administration, which refused to comply with a panel ruling against the unconventional US interpretation of USMCA auto rules of origin. USMCA also further restricted Mexico's policy space, although not considerably given that it was already highly restricted under NAFTA and more recent trade agreements signed by Mexico. Despite these changes, path dependence also mattered: in particular, by signing the USMCA, the US restored its *restraining* trade policy towards Mexico and Canada. The US extended access to the Inflation Reduction Act's subsidies on electric vehicles to its PTA partners, which benefited mostly Mexico and Canada (Reinsch, Chauhan, and Duncan 2022).

The chapter focuses on policy space for activist trade and industrial policies: tariffs, trade remedies (temporary trade barriers), technical barriers, intellectual property, state-owned enterprises, foreign investment regulation, and financial regulation (Chang, Irfan, and Hauge

2016; Thrasher and Gallagher 2008). Labour and environmental provisions, although restricting the global South's policy space, are an integral part of sustainable development (Brandi et al. 2020; Maskus 1997; ILO 2013). Labour rules in USMCA are analysed in detail in Chapter Seven. Environmental provisions in USMCA include measures to protect biodiversity and adhere to certain Multilateral Environmental Agreements. They are integrated in USMCA and enforceable through the state-to-state dispute settlement mechanism, in contrast to the NAFTA where environmental provisions were part of a side agreement (the North American Agreement on Environmental Cooperation) (Laurens et al. 2019). Given that Trump refused to include provisions related to climate change, USMCA's biggest environmental measure is arguably the weakening of the Investor-State Dispute Settlement (ISDS) mechanism (cf. section 4.3.6). Although this chapter evaluates separately changes to the level of market access certainty and policy space, certain provisions affect both, such as the stricter automotive rules of origin. For simplicity, those provisions are analysed in the market access section. Given the scope of this chapter, changes considered of minor importance are not covered.

4.2. Changes in Access to the US Market

Until 2016, North-South trade agreements fulfilled their promise of locking-in market access, while negotiations over new trade agreements sought to achieve further trade liberalisation by removing non-tariff barriers. Things, however, changed after the election of Donald Trump, as he repeatedly threatened to withdraw the US from NAFTA while his administration advanced protectionist negotiating objectives, causing a drastic increase in market access uncertainty (Thrush 2018; Woodward 2018). Baker, Bloom, and Davis (2019) find that 'the recent rise in trade policy uncertainty is extraordinary', using as metrics both keywords in newspapers and stock market prices. In addition to dubbing NAFTA the 'worst trade deal ever approved in this

country'(Severns 2016), Trump increased uncertainty over Mexico-US relations by denouncing the Mexican people as 'rapists', 'bringing crime' and 'bringing drugs' (Phillips 2017). Trump further broke diplomatic norms by arguing that Mexico would pay for a border wall between the two countries to block illegal migrants from entering the US (BBC 2017; Severns 2016).

Trump's disruptive trade policy was characteristic of value-claiming tactics in trade negotiations, by contrast to value-creating moves (Odell and Ortiz Mena 2004; Jones 2013: 79-86). These tactics include making threats and imposing sanctions, opening with high demands while refusing to make concessions, and attempting to worsen negotiating partners' alternatives (Ibid.; Jones 2013: 84). As Mexico refused to pay for the border wall, Trump argued that Mexico would indirectly pay through the provisions in the new trade agreement (Qiu 2018). Trump's threats and insults were unprecedented, as well as his use of trade to leverage concessions on immigration (Pastor 2011: 133). A Mexican negotiator interviewed was shocked by Trump's protectionist objectives, in contrast to the perceived value-creating negotiating strategy of the Obama administration:

> When I was negotiating the Trans-Pacific Partnership, my counterpart in the Obama administration wanted the same things. We wanted free trade, we wanted to have a strong multilateral trade system. And then suddenly Trump came and changed everything (interview, 11 November 2020).

Key officials in the Trump administration, such as US Trade Representative (USTR) Robert Lighthizer, economic adviser Peter Navarro, and Secretary of Commerce Wilbur Ross, agreed with Trump's trade agenda. According to a Trump administration official, the US needed to 'rebalance' NAFTA because Mexico had benefited far more from the trade agreement: '9 out of the last 11 North American auto plants were built in Mexico' (interview, 30 September 2020). Furthermore, Trump administration officials interviewed complained that Mexico was shifting from producing low-value-added cars to producing trucks and high-value-added

products (see also Lighthizer 2023: 218). Rebalancing the agreement would occur by promoting reshoring to the US so that the agreement benefits US working people.

In addition to the offshoring of production to Mexico since NAFTA, Trump administration officials complained about institutional drift: NAFTA automotive rules of origin had become in effect weaker due to the provision that auto parts not listed in NAFTA were 'deemed' to originate in North America. Auto parts such as circuit boards, sensors, and batteries for electric vehicles were not on the NAFTA tracing list, created in the early 1990s (CAR 2017). According to Lighthizer (2023: 219), 'By the 2010s, that meant a car could qualify for duty-free treatment under NAFTA even if over half of its content originated outside the region' (by contrast to the NAFTA 60/62.5 per cent auto rule of origin). Institutional drift (changes to the environment while rules remain fixed) reinforced demands for institutional change triggered by the reaction to the 'restraining' US trade policy since the 1990s (Mahoney and Thelen 2010).

Through its value-claiming negotiating tactics and objectives, the Trump administration undermined the belief that NAFTA provided *stable* preferential market access. The importance of market access stability, emphasised in Chapter Three, is confirmed by negotiators and business representatives interviewed. According to a Trump administration official:

> The market needed certainty and when you combine those things, it almost gave us leverage to get what we wanted, because they (firms) wanted certainty, certainty so badly. And that was one big outcome actually. Realisation on our part that some of these companies are not as concerned with what the rules are, they are more concerned with just having the rules and being able to comply with them and be able to have a predictable outcome (interview, 10 March 2021).

Although US governments before the Trump administration also caused uncertainty over Mexico's access to the US market, they did not attempt to radically alter the trade agreement. Typically, previous US governments used loopholes in the agreement to slightly reduce market access. For instance, a few years after NAFTA entered into force, the US reduced imports of

Mexican sugar, which led Mexico to demand a state-to-state dispute settlement panel. The US government responded by blocking the appointment of roster members to the dispute settlement system and maintained this policy in other NAFTA dispute settlement cases brought against the US (Lester, Manak, and Arpas 2019). Trump's pledge to renegotiate NAFTA was not new either. In 2007, presidential candidate Barack Obama had promised a renegotiation and threatened to withdraw the US from NAFTA if Mexico or Canada did not cooperate (Pastor 2011: 8). Obama focused mostly on enhancing labour and environmental provisions, however, and renounced the renegotiation by April 2009 as US public opinion had reverted in support of NAFTA following the recovery from the 2008 financial crisis. Trump's policies undermining the level and stability of Mexico and Canada's access to the US market are summarised below.

TABLE 3. POLICIES UNDERMINING MEXICO AND CANADA'S ACCESS TO THE US MARKET

Policy type	Policy
Threats	Withdraw the US from NAFTA by executive decree (2016-2019). Impose tariffs on Mexican cars, seasonal and fresh agricultural products, and up to 25 per cent on all Mexican products (2016-2019). Use Section 301 of the 1974 Trade Act to unilaterally impose trade remedies against labour rights violations in Mexico.
Demands	Mexico to impose voluntary export restraints 50 per cent US-specific rule of origin in the auto industry 5-year sunset clause Eliminate all dispute settlement mechanisms Facilitate the imposition of trade remedies on Mexican agricultural exports Eliminate restrictions on safeguards Restrict Mexico's access to the US government procurement market
Actions	Imposed tariffs on Canadian and Mexican steel (25 per cent) and aluminium (10 per cent) from March 2018 to May 2019. Obtained a 6-year review period and 16-year sunset clause in USMCA. Obtained an increase in regional value content for auto rules of origin to 70/75 per cent, the extension of RVC to core parts, a 70 per cent rule of origin for steel and aluminium, and that 40-45 per cent of the value of autos be produced in plants where direct production workers earn on average at least 16 US dollars per hour. Obtained a weakened Investor-State Dispute Settlement (ISDS) mechanism. Implemented a controversial, stricter interpretation of the auto rules of origin (contested by a USMCA DSM ruling in January 2023).

The rest of this section analyses Trump's efforts to reduce the level and stability of access to the US market, focusing on the removal of preferential market access, unconventional use and interpretation of US and international law, efforts to reduce market access in USMCA, and two sets of provisions in USMCA: the sunset clause and the automotive rules of origin.

4.2.1. Removal of Preferential Market Access

In January 2018, President Trump imposed safeguard tariffs of 30 to 50 per cent on solar panels and washing machines (Bown 2018). Two months later, he approved tariffs of 25 per cent on steel and 10 per cent on aluminium. Along with several other countries, Mexico and Canada were temporarily exempted from the steel and aluminium tariffs on the condition that they would concede to US demands during the NAFTA negotiations (IUST 2020a). Considering that Mexico and Canada had not made sufficient concessions, on 31 May 2018 the Trump administration unilaterally imposed the steel and aluminium tariffs on Mexico and Canada. Those lasted until May 2019, by which time the US agreed to suspend its tariffs in exchange for Mexico and Canada eliminating their retaliatory measures (Swanson and Bilefsky 2019). The US steel and aluminium tariffs undermined the belief that trade agreements like NAFTA locked in market access. As a result, they gave greater credibility to the Trump administration's other threats of removing preferential access to the US market.

From the beginning of his presidential campaign in 2015 to the ratification of USMCA in 2020, Trump used aggressive rhetoric to advance his 'America First' doctrine, claiming that the US had been exploited by Mexico and Canada due to NAFTA. President Trump's rhetoric focused on reducing the bilateral trade deficit between the US and Mexico and reshoring Mexican auto industry plants to the US (the US had a trade surplus with Canada). This aggressive rhetoric was magnified during the presidential campaign and throughout the negotiations by threats of a US withdrawal from NAFTA unless Mexico adhered to the US negotiating objectives.

Kenneth Smith Ramos, the chief negotiator for President Peña Nieto, remembers the negotiations as '18 months with the constant threat of the possibility (of the US) pulling out' (IUST 2019b; interview, 13 October 2020). Media coverage of the negotiations and interviews with US and Mexican officials confirm the credibility of Trump's withdrawal threat. After the 2018 mid-term elections during which the Democratic Party won control of the House of Representatives, Trump again considered unilaterally withdrawing from NAFTA to force Congressional Democrats to choose between the USMCA and no agreement (Thrush 2018). The Trump administration also threatened to remove access to the US market by imposing tariffs, drawing on unconventional uses and interpretations of US and international law, as detailed below.

4.2.2. Unconventional Uses and Interpretations of US and International Law

As president-elect, Trump had already created market access uncertainty by threatening to impose a 35 per cent tariff on specific US companies offshoring plants to Mexico, such as Ford and BMW (Campbell 2017). The Trump administration's threats to remove Mexico's access to the US market were built on novel interpretations and uses of US and international law. Most notably, the Trump administration claimed that the President could unilaterally withdraw the US from NAFTA, even though the US Constitution states that Congress has the power to 'regulate commerce with foreign nations' (US Constitution, Article I Section 8). The Trump administration's interpretation rested on the argument that trade agreements are also a matter of foreign policy, which is under the President's authority, as well as Section 125 of the 1974 Trade Act, which provides the President with the authority to withdraw from trade agreements (Hufbauer 2017; IUST 2017r). Given that NAFTA was implemented through legislation passed in Congress, however, it was unclear whether Trump would have been able to remove that

legislation even if he succeeded in unilaterally withdrawing the US from NAFTA (Bradley 2018; Trachtman 2017). Nevertheless, the threat of such a procedure was enough to increase uncertainty over Mexico's access to the US market.

To justify the imposition of tariffs on steel, aluminium, and potentially on the automotive industry, the Trump administration referred to Article XXI of the WTO General Agreement on Tariffs and Trade allowing a country to take 'any action which it considers necessary for the protection of its essential security interests' (WTO 2002). However, Article XXI specifies three categories relative to essential security: nuclear products, weapons, and times of war or other emergency in international relations. At the time, the unique WTO ruling on the use of Article XXI, concerning Russia's policies towards Ukraine, referred to those categories to confirm Russia's conformity with the Article (Prazeres 2020). The Trump administration argued that Article XXI was self-judging, and therefore that the US could rightfully consider any economic interest a matter of national security, thereby opening the door for imposing tariffs on any product (Ibid.). The Trump administration then ensured that the WTO would not provide a binding ruling on this issue by blocking the appointment of judges to the WTO Appellate Body. This policy was initiated by the Obama administration in protest of the WTO's judicial overreach (Bahri 2019). Since December 2019, no cases can be considered in appeal due to a lack of judges, which renders the WTO dispute settlement mechanism incapable of functioning and thus incapable of invalidating the US interpretation. The Trump administration's understanding of Article XXI was unusual given that US officials did not consider the article to be self-judging when the GATT was created following WWII but rather were concerned that other countries would interpret it in such a manner to justify any protectionist policy (Pinchis-Paulsen 2020). The change in the US interpretation of Article XXI increased uncertainty over market access by signalling that the US could impose national security tariffs on any product, including cars and auto parts.

Similarly, Trump used his authority over national security matters to impose tariffs without consulting Congress. The Trump administration drew on Section 232 of the 1962 Trade Expansion Act, in which Congress allowed the President to impose national security tariffs recommended by the US Secretary of Commerce. In 2017, President Trump demanded a review from Secretary of Commerce Wilbur Ross on the risks to US national security from steel and aluminium imports, which led to the imposition of tariffs. In 2018, he requested an investigation into imports of cars and auto parts. The report concluded that President Trump could impose tariffs of up to 25 per cent, thereby threatening access to the US market for Mexican and Canadian automobiles and auto parts (Johnson and Restuccia 2019). By rendering clear that economic interests could be interpreted as matters of national security, the report also increased market access uncertainty for all US trading partners. Although the Trade Act dates from 1962, its national security provisions did not constitute a major cause of trade uncertainty until the Trump administration because they had rarely been used since the creation of the WTO (and even less so against allies), and did not target consumer goods such as cars (Bown 2017a).

Under Section 301 of the 1974 Trade Act, a US President can also unilaterally impose trade barriers to obtain the removal of measures or practices that violate a trade agreement or that are considered ‘unjustifiable’, ‘unreasonable’, or ‘discriminatory’ (Schwarzenberg 2019). Just as Section 202, Section 301 had rarely been used since the creation of the WTO due to the US policy shift from ‘competitive’ to ‘restraining’ (Bown 2017b; cf. Chapter Three). In addition to resorting to Section 301 to address concerns over intellectual property protection in China, the Trump administration also proposed novel uses of Section 301. In 2019, USTR Lighthizer attempted to convince House Democrats to support USMCA by arguing that Section 301 could be used to enforce labour rights in Mexico (Rodriguez 2019). This interpretation of Section 301 was disputed by trade lawyers and considered unconvincing by Congressional Democrats. Nevertheless, it reaffirmed the Trump administration’s disregard for settling disputes through

international panels, preferring instead to unilaterally impose trade sanctions. The declining US commitment to the dispute settlement mechanisms of trade agreements increased uncertainty over access to the US market not only for Mexico and Canada but also for other US trading partners.

The most dramatic use of US domestic law to increase uncertainty over Mexico's access to the US market occurred in May 2019, when President Trump referred to the 1977 International Emergency Economic Powers Act (IEEPA) to threaten to impose tariffs of up to 25 per cent on all Mexican goods until the end of illegal immigration to the US from Mexico (Pierson and Hals 2019). According to a Trump administration official, the idea came from Trump's advisor Peter Navarro:

> When we invoked that (IIEPA) on Mexico, that was Peter Navarro and Stephen Miller. They've been allies on the campaign trail; they've shared a very populist position on a lot of things. Obviously, Peter was the trade specialist. Miller was the immigration guy. Somewhat similar worldview in a lot of ways so that they sort of came together because Miller wanted to do something on immigration and Peter saw the opportunity to use that as a way to get some positive outcomes on trade too. And so they came together. And when the President said "Hey, let's do this, and either we're gonna solve the immigration problem or we're gonna solve some of our trade deficit problems with Mexico. So either way we win" (interview, 25 January 2021).

The IIEPA authorises the President to regulate trade in case of a national emergency originating outside of the United States. Although the IEEPA had been frequently used, what differed was both the nature of the emergency and the response favoured by the President. Past measures targeted regimes hostile to the US, such as Iran and North Korea, over emergencies such as terrorism, war, and drug trafficking. Typical responses included the freezing or seizure of assets owned by governments, other organisations or individuals involved in such activities. By contrast, Trump's proposed use of IEEPA was unprecedented because it targeted a US ally, defined illegal immigration as a national emergency, and proposed tariffs of up to 25 per cent on all imported goods as an adequate response. Trump agreed not to impose tariffs after

obtaining the Mexican government's assurance it would invest resources to prevent immigration to the US (Shear and Haberman 2019).

Other domestic laws gave the US President authority to impose tariffs without consulting Congress, such as Section 201 of the 1974 Trade Act, which was used in 2018 to impose safeguard tariffs on imports of solar panels and washing machines (Bown 2018). The sense of unrestrained policy space for imposing tariffs is well illustrated by an interview with an official in the Trump administration. When asked what the administration would have done if Congress prevented a withdrawal from NAFTA, he replied:

> We had enough alternative tariffs at our disposal that we could have done a national security investigation, or a 201, or what we probably would have done is a provision we have that has not been used since I think Nixon was the President, that once you put up to 15 per cent tariffs on anything from any country […] that was intended to be a balance of trade remedy and lets you do that up to 6 months.[5] We would have probably done that immediately, and say we are imposing tariffs up to 15 per cent to match what the WTO rates are against Canada and Mexico, and in those 6 months, we would have done a 232 investigation (a national security investigation), or something else along those lines, probably a 301, which we did on China, to say we are now going to impose those tariffs on you using executive action at a rate equivalent to what the WTO rate is (interview, 25 January 2021).

The Trump administration's novel interpretations and uses of US domestic law to impose tariffs breached WTO rules. By showing his willingness to challenge the rule of law, Trump created trade uncertainty and thus weakened NAFTA's basic objective. Trade agreements lock in market access only insofar as governments commit to honouring them, even if they were signed by previous governments. Trump could choose to act unilaterally instead due to the large power asymmetry with its trading partners, as Mexico and Canada had much more to lose from a US withdrawal from NAFTA. Whereas the US can ignore WTO rulings or retaliation by trading partners because of the small repercussions on its economy, a smaller country cannot disregard

[5] Section 201 can only be used by a US President based on the findings of an independent investigation by the US International Trade Commission. The interviewee then refers to the US Trade Act of 1974, Section 122.

potential retaliation by the US (or other large trading partners such as the EU) due to the large economic costs that would ensue. By choosing to act unilaterally, the Trump administration crushed illusions that the rule of law embodied in trade agreements could substitute the law of the mightiest. The US laws used by the Trump administration to create uncertainty already existed for a long time, thereby demonstrating that market access stability was less a result of legal requirements under NAFTA than US politicians accepting the norm that PTAs should provide certainty.

4.2.3. Efforts to Reduce Market Access in USMCA

The official US objectives for the NAFTA renegotiation were published in July and November 2017 as part of the US Trade Representative's legal obligation to inform Congress (USTR 2017a, 2017b). US chief negotiator John Melle warned against overinterpreting those objectives given that they were written before the 'thick of the negotiations' and that 'negotiators never want to talk about what their goals are, especially in a public document that your negotiating partners can read' (interview, 16 December 2020). To mitigate the first concern, this section is also informed by the US negotiating objectives that emerged during the negotiation process. The second concern is addressed in Chapter Five, which identifies the Trump administration's commitment to its negotiating objectives. This is less relevant here given that communicating protectionist objectives was sufficient to undermine trust in the stability of Mexico and Canada's preferential access to the US market.

The central US negotiating objective, stated in both official negotiating objectives and by US negotiators, was to reduce the trade deficit between the US and its NAFTA partners. USTR targeted Mexico, which had a trade surplus with the US, rather than Canada, which had a trade deficit (interview, Trump administration official, 9 September 2020). The Trump

administration's focus on the US trade deficit led to unprecedented negotiating objectives directly aimed at undermining Mexico's access to the US market, such as a 50 per cent US-specific rule of origin in the automotive industry (IUST 2018u). US negotiators also demanded that Mexico impose voluntary export restraints, a measure banned by the WTO (Elms 2018). Another major protectionist demand concerned government procurement, for which the US sought greater policy space to discriminate in favour of its domestic firms, and 'dollar-for-dollar' market access: restricting access to the US government procurement market to the size of the Mexican and Canadian government procurement markets. Those measures were directly targeted at reducing Mexico and Canada's access to the US market.

US objectives also included measures indirectly aimed at reducing market access, such as eliminating both restrictions on the use of trade remedies and mechanisms to ensure the agreement is enforced. USTR Lighthizer first asked for the elimination of the state-to-state dispute settlement mechanism, then argued that it could be maintained only if the US had the power to unilaterally nullify a ruling when 'a panel has clearly erred in its assessment' (interview, Ken Smith Ramos, 16 October 2020; USTR 2017b: 17). The US also demanded the elimination of the antidumping and countervailing duties dispute settlement mechanism (AD/CVD DSM), cherished by Canada but also Mexico given the historic use by the US of such trade remedies (USTR 2017b: 14). Similarly, US negotiators demanded the elimination of the NAFTA global safeguard exclusion, which protects NAFTA members from safeguard measures as long as they are not one of the five main exporters of the targeted product (Ibid.). Although the last two objectives were set by the Trump administration, they reflected a bipartisan consensus in the US Congress on the necessity to retain the power to impose trade remedies (US Democratic Party official, interview, 26 February 2021).

Other US negotiating objectives were directly aimed at increasing market access and investment uncertainty, such as eliminating the Investor-State Dispute Settlement mechanism (ISDS) and

introducing a five-year sunset clause to the agreement that would be tied to the reduction of the US trade deficit (IUST 2017r). According to Lighthizer, ISDS undermined the US comparative advantage in the rule of law by providing guarantees to firms that invest overseas (IUST 2017i). Lighthizer also considered that the locking-in of market access through trade agreements incentivised US firms to offshore production. By creating the risk of losing market access after five years, a sunset clause would increase the costs of offshoring production and as such dissuade firms from doing so:

> And then (US firms) say 'Oh we can't have a sunset; we can't have a provision where you actually look after five years to see whether it's been good or not.' Why? 'Because we won't be able to invest!' And I'm thinking 'Why don't you just calculate that into your investment?'' (Lighthizer, quoted in IUST 2017m).

In addition to creating market access uncertainty, a five-year sunset clause would also increase US bargaining power in future negotiations, as discussed below.

4.2.4. USMCA Sunset Clause

USMCA Article 34.7 specifies that the agreement will be reviewed every six years and expire ten years after the review period should no new agreement be reached. This constitutes a sixteen-year sunset clause. Even though the US proposal of a five-year sunset clause was not included in the agreement, the six-year review periods and the sunset clause create the risk of regular challenges to Mexico and Canada's preferential access to the US market. NAFTA was historically used as a scapegoat by US politicians. The review periods create an incentive for US politicians to appeal to voters by demanding new concessions from Mexico and Canada, while the sunset clause generates uncertainty which can be used as leverage in negotiations.

The sunset clause gives the US a new route to withdrawal, in addition to a vote in Congress, as the President could let USMCA expire by refusing to renew it. Jesús Seade, chief negotiator in

the López Obrador government, resisted the US demand for a five-year sunset clause primarily for this reason:

> I recognised immediately that the sunset clause was a really gigantic danger because not only in five years we don't know what is going to happen, but it would resolve the legal issue for the (US) government: if today you (the US government) cannot pull out because maybe you need Congress's permission, in five years, just by not signing, you can pull out' (interview, 15 October 2020).

This route to withdrawal is less likely to occur with the sixteen-year sunset clause, however, given that it requires the US to notify other NAFTA members eleven years in a row (from the sixth to the sixteenth year of USMCA) of its intention to withdraw (Article 34.7.4). As such, a withdrawal using the sunset clause requires support from three consecutive US administrations. Nevertheless, US governments are likely to be tempted to use this process to gain leverage in future trade negotiations, as well as to incentivise investments in the US by creating uncertainty over the continuity of Mexico and Canada's preferential access to the US market.

Most respondents interviewed, including business representatives, expressed disbelief in the idea that the US could withdraw from USMCA using the sunset clause, given that doing so would hurt the US economy considerably (although less than the Mexican and Canadian economies). Mexican negotiators interviewed even praised those changes, arguing that review periods every six years ensure that the agreement is modernised and problems are fixed rather than left to grow as was the case under NAFTA. According to a Mexican official interviewed:

> The sunset clause was really turned into a review clause, that is a mechanism that I think is even better than what we had before because this creates an obligation for the countries to sit down and review what are their views about the agreement. And I think that it can prevent the sort of crisis that happened when President Trump was elected (interview, 7 April 2021).

Mexican chief negotiator Kenneth Smith Ramos even argued that the review periods would help Mexico weaken some of the provisions accepted in USMCA because of the Trump administration:

> We're likely to come back and review […] some of the rules of origin. Because the tendency in the world, if you look at what we did in TPP, what we did with the European Union, the tendency is to make rules of origin – over these big advanced manufacturing sectors that source from everywhere in the world – the tendency is to make the rules more flexible and not stricter (Smith Ramos, interview, 16 October 2020).

Business confidence in the continuity of USMCA to some extent vindicates Mexican negotiators' confidence in the harmlessness of the sunset clause, although the fact that business groups opposed the inclusion of a sunset clause in the agreement suggests it does negatively impact the business environment.

Even though the US withdrawing from USMCA is unlikely, considerable market access uncertainty can be created by US politicians who threaten withdrawal or refuse to renew the agreement for several years. US chief negotiator John Melle referred to the sunset clause as a 'sixteen-year ticking clock' (interview, 16 December 2020). Similarly, during the negotiations, USTR Lighthizer was clear that the purpose of a sunset clause would be to create market access uncertainty to persuade firms to invest in the US rather than Mexico (IUST 2017i). The Trump administration demonstrated how to create market access uncertainty, and such techniques may be re-applied in review periods. Although the AFL-CIO (the US largest trade union) endorsed USMCA, not all labour unions approved of the agreement, and most (including the AFL-CIO) lobbied for a shorter sunset clause (US labour union representatives, interviews, 15 and 17 March 2021, 2 April 2021). According to a US labour union leader:

> We supported the six-year (sunset) period. But it was changed, as you know, to a review. I can't remember what the number was at the end, but that was still for us acceptable. But yes, as you mentioned, we preferred a shorter sunset clause. Just to let you know, as a rule, we support shorter review periods for trade agreements, so that the governments can assess whether they are accomplishing their objectives and renegotiate

> if necessary. From our perspective, NAFTA was not working very well for workers in the United States but it had no review period, NAFTA was going indefinitely. And our experience was not very positive with this. […] We understand that that (US withdrawal from USMCA) is unlikely given the commercial relationship with Canada, Mexico. It is very substantial. But I think of it (the review period) more as a piece of leverage to correct some things that may not have been going well (interview, 2 April 2021).

Referring back to the US negotiating objectives that were not included in USMCA, a Trump administration official argued that the review periods will provide an opportunity to obtain new concessions from Mexico and Canada:

> With the sixteen-year time frame, it wouldn't surprise me in some point in the future if the Americans go back and raise a lot of these issues again. We are going to get other chances to talk about some of these things (interview, 7 May 2021).

The review periods and sunset clause create an institutional mechanism for the US to progressively worsen the certainty of Mexico and Canada's access to the US market.

4.2.5. USMCA Auto Rules of Origin

Rules of origin (ROO) specify the share of the value of a product that should originate within the economic zone to be exported duty-free. USMCA introduced stricter rules of origin for the auto industry (USMCA Annex 4.B Appendix) which can hinder Mexico's (and to a lesser extent Canada's) access to the US market. USMCA increased NAFTA regional value content requirements for passenger vehicles and trucks from 60/62.5 per cent to 70/75, respectively. USMCA also added three unprecedented auto rules of origin. First, it extended the regional content requirement (RVCs) to 'core' parts in a vehicle, such as batteries, engines, and steering systems. For instance, an auto assembler has to ensure that its engine meets the 70 per cent rule of origin for the vehicle to qualify as originating in North America. Second, the agreement introduced the requirement that 70 per cent of a vehicle's steel must be sourced from North

America for the vehicle to qualify as originating in the region. Third, USMCA stipulated that 40/45 per cent of the value of passenger vehicles and trucks, respectively, must be produced in plants where direct production workers earn on average at least 16 US dollars per hour (Labour Value Content rule of origin).

The Labour Value Content (LVC) rule of origin contains a 10 per cent exception for high-wage technology expenditures and a 5 per cent exception for high-wage assembly which effectively reduces the requirement to 25/30 per cent for passenger vehicles/trucks, respectively. Those exceptions ensure that investments in Mexico are not undermined (cf. section 5.4.2.). Firms were allowed to ask for alternative staging regimes to have more time to comply. Whereas nearly all firms demanded additional time to meet the RVC increase (from 60/62.5 to 70/75 per cent for autos/trucks), only a few asked for additional time to meet the LVC requirements (USITC 2023: 35). By setting a high-wage requirement, the LVC can even reduce power asymmetries between MNCs and domestic suppliers as core firms in the global North typically squeeze the profits of their suppliers in the global South, thereby limiting the latter's ability to pay higher wages or upgrade production (Gereffi 2018; Milberg 2013).

The complexity of complying with four rules of origin, however, can hinder Mexican and Canadian auto manufacturing. Firms can decide to assemble in the US or to keep exporting but pay the 2.5 per cent US WTO Most Favoured Nation (MFN) tariff on passenger vehicles (this strategy is unviable for trucks given that the US MFN tariff is 25 per cent). Under NAFTA, already 23 per cent of goods in the transport sector imported from Mexico to the US did not comply with the rules of origin and were thus subject to the 2.5 per cent tariff (Freund 2017). The higher rules of origin are likely to exacerbate this trend and thereby undermine Canada and Mexico's preferential access to the US market given that more goods will be subject to the same 2.5 per cent tariff as non-USMCA members. Furthermore, the US's unconventional implementation of the auto rules of origin since 2020 (not allowing 'roll up') increased the

difficulty of complying.[6] The Biden administration kept Trump's protectionist interpretation despite a January 2023 ruling from a USMCA panel allowing 'roll-up', lending further credence to the argument that structural factors rather than Trump alone are leading to a long-term shift in US trade policy (McCarten 2023). Even if the US eventually complied with the USMCA panel ruling, the uncertainty already impacted firms' expectations and investment decisions. According to a Toyota representative:

> Even if it's going to be more expensive to comply (with roll-up provisions), we made a political decision to just do this. So we're doing it, Ford is doing it, GM is doing it. But some other companies are struggling. Only a few companies actually can meet the new rules with super core roll-up, including Toyota (interview, 9 September 2021).

On the one hand, this change in rules could be significant given that, in 2017, the transport sector accounted for a quarter of Mexico's exports to the US (Ibid.). On the other hand, the strict rules of origin constitute a North American industrial policy incentivising firms to produce in the region. Although NAFTA and USMCA reduce Mexico's policy space by banning local content requirements, the regional value content requirements are in effect local content requirements applied at the North American level. Furthermore, Mexico and Canada will increase their preferential access to the US market relative to competitors if the US imposes national security tariffs (Section 232) on passenger vehicles. In the case of Section 232 tariffs, imports from Mexico which do not comply with USMCA rules of origin would be exempted from the higher tariffs thanks to a side letter to USMCA specifying that 2.6 million passenger vehicles and 108 billion US dollars' worth of auto parts per year would be able to enter the US under the 2.5 per cent tariff (Canada obtained similar side-letters). This is much higher than the number of passenger vehicles that Mexico exported to the US in 2017, leaving room for export

[6] 'Roll up' enables a company to count as 100 per cent originating an auto part which passed the rule of origin threshold. For instance, under NAFTA, where the auto rule of origin for passenger vehicles was 62.5 per cent, if 65 per cent of the value of a 100 dollar car part was created in North America (thereby meeting the rule of origin), the auto assembler could count the value of the entire car part in the calculation of its rules of origin (100 dollars as opposed to 65).

growth (Deloitte, 2020: 40; Zayas, 2017; Tankersley 2018). The next section details policy space changes from NAFTA to USMCA.

4.3. Changes in Policy Space

This section focuses on Mexican policy space given that Canada is already a high-income economy. Through the different channels undermining market access certainty outlined above, the renegotiation of NAFTA challenged the logic of North-South PTAs whereby countries in the global South obtained *stable* preferential access to markets in the global North in exchange for relinquishing the use of activist trade and industrial policies (Chang 2002; Gallagher 2007; Shadlen 2008). This section analyses the extent to which the NAFTA renegotiation also altered Mexico's policy space for activist trade and industrial policies. It then details the reasons that led the Mexican government to embrace most of these changes. First, though, it considers the new USMCA state-to-state dispute settlement mechanism, which conditions enforcement of most policy space restrictions.

Loopholes in NAFTA that prevented the functioning of the state-to-state dispute settlement mechanism (DSM) are removed in USMCA (Vinopal 2019). The US had blocked the appointment of DSM roster members since the early 2000s to prevent Mexico from raising a dispute over US limitations on sugar imports. USMCA closed those loopholes by ensuring that roster members are appointed even if there is no consensus or if a country fails to designate its roster members (USMCA Chapter 31 Article 8.1). The easier recourse to arbitration reduced the Mexican government's policy space insofar as it increased the threat of legal action should Mexico implement industrial policies that breach USMCA provisions. As of December 2023, the US and Canada had requested the formation of two panels to examine whether López

Obrador's support of state-owned company PEMEX and its ban on imports of genetically modified corn were consistent with Mexico's USMCA commitments (Brookings 2023b)

The DSM also allows Mexico and Canada to legally challenge US protectionist policies. They did so in 2021 to contest the US strict interpretation of USMCA auto rules of origin. The panel ruled in Canada and Mexico's favour in January 2023, yet the US refused to comply with the panel decision as of December 2023 (Ibid.). Although Mexico and Canada have the right to retaliate, they have not done so which indicates that US *de facto* policy space is higher than its *de jure* policy space. By contrast, Canada and Mexico's *de facto* policy space is lower than their *de jure* policy space as they avoid creating tensions with the US. The USMCA review periods accentuate this power asymmetry as officials in both the Trump and Biden administrations have argued that they would ask for changes to USMCA to ensure the US interpretation of automotive rules of origin prevails (interviews, 23 October 2020, 7 May 2021; Lighthizer 2023). This contrast between *de facto* and *de jure* policy space is found in the application of many USMCA provisions, as detailed below.

4.3.1. Tariffs

USMCA contains few changes in tariff barriers given that nearly all tariffs had been reduced to zero under NAFTA. One notable addition is a ban on tariffs on digital products (Article 19.3). Another significant change is the increase in the *de minimis* threshold for customs duties in Mexico from 50 to 117 US dollars, at the US insistence, which enables purchases of 117 US dollars or less to be sent duty-free from the US and Canada to Mexico (Article 7.8.1). Low *de minimis* levels constitute a significant trade barrier to small online purchases, which have increased in importance and are dominated by US firms such as e-commerce platform Amazon. Mexico's higher *de minimis* threshold benefits consumers and strengthens North American ties

but also constitutes a loss of tariff revenue in a country with low fiscal resources (UNCTAD 2021: 35).

USMCA increased *de jure* policy space to impose tariffs for national security reasons, although those are more likely to be used by the US than by Mexico or Canada. Whereas NAFTA and WTO national security exemptions specifically refer to weapons, nuclear products, and war or other international emergencies as legitimate reasons for imposing national security tariffs, USMCA no longer specifies what is relevant to a country's 'protection of its own security interests' (Article 32.2). Although Mexico and Canada can contest US national security provisions at the WTO, this is largely irrelevant given the growing US preference for unilateralism. In 2022, the Biden administration refused to comply with multiple WTO dispute settlement rulings finding that the US national security tariffs on steel and aluminium imposed by the Trump administration were unjustified (the Biden administration then 'appealed into the void' given that the WTO Appellate Body is not operational) (Hirsch 2023). Although both Canada and Mexico were exempted from Section 232 tariffs on the automotive industry in side letters to USMCA, they remain vulnerable to US national security tariffs on other industries.

USMCA also introduced a provision aimed at dissuading a member from signing a trade agreement with a 'non-market economy' (Article 32.10), which is unprecedented. The article specifies that a USMCA member must inform other members of its decision to negotiate a trade agreement with a non-market economy, and provide them details of the negotiation process, as well as the full text of the agreement at least 30 days before it is signed. Should the USMCA member enter into a trade agreement with the non-market economy, other USMCA members have the right to expel that country from the USMCA. A 'non-market economy' is defined as a country:

> (a) that on the date of signature of this Agreement, a Party has determined to be a non-market economy for purposes of its trade remedy laws; and
> (b) with which no Party has signed a free trade agreement (USMCA Article 32.10.1).

This provision was requested by the US and aims to prevent Canada and Mexico from entering into a PTA with China (IUST 2020c). Although the provision does not *de jure* prevent Mexico or Canada from signing a PTA with China, which was the initial US proposal (Mckenna and Decloet 2018), the pressure exerted by the US *de facto* restricts their policy space to sign a PTA with China. The provision could also render problematic Canada and Mexico's membership of CPTPP should China succeed in becoming a member, and deter Canada and Mexico from joining RCEP, of which China is a member (Atkins 2021; IUST 2020c). Given that China is set to become the world's largest market, this provision may undermine in the long run Mexico's export-oriented development strategy. The impact of this provision on Mexican industrial policy is mixed: while tariffs on Chinese imports can promote domestic production, the lack of PTA with China can also prevent the Mexican government from diversifying its export destinations to reduce its dependence on the US.

4.3.2. Trade Remedies

Although USTR Lighthizer wished to eliminate the NAFTA antidumping and countervailing duties dispute settlement mechanism (AD/CVD DSM) and the global safeguard exclusion, which would have allowed the US to impose trade remedies unilaterally, those mechanisms are maintained in USMCA (Chapter 10 Section D and Article 2, respectively).[7] This limitation on US policy space to impose trade remedies is also a limitation on Mexican policy space for trade remedies. However, nowhere is the gap between *de jure* and *de facto* policy space more evident than in the use of trade remedies. For instance, while both the US and Mexico are entitled to

[7] The global safeguard exclusion prevents a USMCA member to impose tariffs against another USMCA member due to a surge in imports (unless specific conditions are met, such as the targeted country being one of the top five exporters of that product).

use 'zeroing' as a methodology to calculate AD/CVD,[8] only the US has used this accounting method as Mexican officials are worried about retaliation should they do the same (Mexican USMCA panellist, interview, 25 September 2020). The US even expanded its policy space to impose trade remedies by resorting to Section 301 tariffs, whereas Mexico stayed clear of unilaterally imposing trade remedies. Whereas the US disregarded NAFTA rules, Mexico faced the opposite situation: its *de facto* policy space to impose trade remedies is lower than its *de jure* policy space.

4.3.3. Technical Barriers

As countries committed to reducing their tariff barriers in the WTO and bilateral trade agreements, they increasingly resorted to non-tariff barriers, such as burdensome regulation, to protect domestic producers (Crivelli and Groeschl 2016; Li and Beghin 2012). The Trans-Pacific Partnership, which Trump rejected, addressed some of those technical barriers. Ironically, the USMCA contains many provisions that had already been negotiated in TPP, such as on sanitary and phytosanitary measures (chapter 9) and technical barriers to trade (chapter 11). USMCA also contains new chapters, such as on good regulatory practices (chapter 28) and digital trade (chapter 19), which also contain provisions from TPP. Those are described by negotiators in all three countries as efforts to modernise NAFTA to facilitate cross-border trade and investment. Although such requirements restrict policy space for infant industry protection, they also help Mexican firms operate in the US.

[8] AD/CVD are calculated by comparing the price of the imported product and that of the same product sold in the exporting country. Dumping occurs when the imported product is cheaper. Zeroing consists of not including in the calculation imported products that are more expensive than in the exporting country, which magnifies the size of the dumping.

The most novel restrictions on policy space are in the digital sector, which was not regulated under NAFTA. USMCA bans taxation of cross-border data flows (Article 19.3) as well as discriminatory or unnecessary restrictions on cross-border data flows (Article 19.11). The agreement also undermines technology transfer by prohibiting requirements that firms disclose computer source code and algorithms to access the national market (Article 19.16). Similarly, the ban on data localisation requirements (Article 19.12) restricts industrial policy space as requirements to store data on the national territory can be used to promote joint ventures and technology transfer (Mayer 2021). Furthermore, the data localisation ban does not guarantee US compliance given the bipartisan consensus in the US to consider data localisation a matter of national security, which opens the possibility of a Section 232 investigation. This would enable the US to overrule the USMCA provision and impose data localisation requirements.

Mexico's d*e facto* policy space with regard to technical barriers to trade is even more limited than its *de jure* policy space as the US government and business lobbies threaten to sue Mexico for alleged violations of USMCA. For instance, shortly after USMCA entered into force, the Trump administration claimed that the Mexican legal project of regulating social media platforms of systemic size constituted discrimination against US big tech companies because nearly all large social media companies are American (IUST 2021c). This interpretation is contested, but threats of litigation or retaliation were sufficient to discourage the Mexican government from engaging in regulation.

4.3.4. Intellectual Property

The US demanded further policy space restrictions in areas already regulated under NAFTA, such as intellectual property (IP) protection, state-owned enterprises, and foreign direct investment, with the objective of preventing 'unfair' trade practices. Concerning intellectual

property protection, the US demanded provisions that it had obtained in TPP negotiations before Trump withdrew from the agreement. The US obtained patent term extensions for delays of more than five years in granting a patent. Although the Trump administration successfully negotiated test data protection of ten years for biologic drugs, which would have further lengthened the duration of patent-holders monopoly rights, Democratic members of Congress demanded and obtained the withdrawal of those provisions, considered excessively anticompetitive, as a condition for their support of the new trade agreement (Akhtar and Fergusson 2020). US chief negotiator John Melle recalled:

> We had others (Democrats) who had very strong feelings about the pharmaceutical provisions which we had negotiated. Trying to correct that had been one of the big political issues largely with Republicans on the Trans-Pacific Partnership, having to do with the data exclusivity period for biologic drugs. That obviously got changed (interview, 16 December 2020).

Although Trump also criticised excessive intellectual property protection for pharmaceuticals during his presidential campaign, he yielded to business lobbies until Democrats in Congress demanded the change. Similarly, patent protection for new uses, methods, or processes of a known product was included in USMCA but removed in the amended agreement. Together, these changes signal an inflexion point in US trade policy, which had until then favoured the inclusion of ever-stronger IP provisions in trade agreements. It reflected growing opposition to high drug prices in the US, an issue seized by the Democratic Party.

The Mexican government did not consider the new IP provisions a burden on policy space but rather a logical change given its commitments in other trade agreements. According to Mexican chief negotiator Ken Smith Ramos:

> One of the most controversial issues in IPR that was actually taken away from the agreement was the issue of data protection for pharmaceutical products. It's quite controversial. It was controversial in the TPP, and, obviously, also in our agreement with the European Union, because it has to do with a new generation of medicines, basically biologic products that require much more time to develop and more of an

> investment. So there's a high liability and risk for innovators unless they get a certain level of data protection guarantees. So this was a big issue. Mexico in TPP had accepted eight years of data protection for biologics. In the USMCA negotiations, we accepted ten years.

Those provisions, initially accepted by Mexico, would have further undermined Mexican policy space for transferring foreign technologies to domestic firms given that they lengthen the process of technology diffusion. The Mexican government historically over-complied with IP regulations due to the weakness of its pharmaceutical industry and interest in exchanging this concession to obtain stable access to the US market (Shadlen 2017: 229-232). By contrast, some countries in the global South abstained from joining North-South PTAs to preserve their policy space (with varying degrees of success as other strategies were deployed by the global North to undermine WTO TRIPS flexibilities) (Deere-Birkbeck 2009).

Although US trade policy towards IP for pharmaceuticals changed, the US continued to demand and obtain stronger IP protection in other areas. USMCA increased minimum copyright protection from life plus 50 years or 50 years to life plus 70 years or 75 years (Article 20.62), and of industrial designs from 10 to 15 years (Article 20.55), which in effect increased the flow of royalties from Mexico to the United States (Gallagher 2007: 69). The agreement also introduced stricter protection of trademarks, as well as criminal penalties for certain infringements of IP protection, such as digital content theft (Article 20.84) and trade secret violation, including by state-owned enterprises (Articles 20.69 and 20.84).

4.3.5. State-owned Enterprises

In addition to criminalising trade secret violations by state-owned enterprises (SOEs), USMCA also expanded the definition of SOEs to include firms in which the government owns a minority but controlling stake (Article 22.1). SOEs are also precluded from providing ‘non-commercial’

assistance to other SOEs, except if those are at risk of bankruptcy (Article 22.6); and must conduct procurement in a non-discriminatory manner (Article 22.4). Although those provisions restrict Mexico's policy space, they were not considered particularly relevant by Mexican negotiators given that they were not used in Mexico under NAFTA (Mexican trade official, interview, 10 December 2020). Instead, those provisions were primarily targeted at the Chinese government, which had successfully argued in WTO panels that firms in which it owns a minority but controlling stake are not SOEs, and thus should be treated as private firms operating on a level playing field with foreign private firms (Ibid.; Trump administration official, interview, 30 September 2020). By contrast to NAFTA, which placed few restrictions on the use of SOEs (chapter 15), USMCA introduced strict restrictions on policy space for industrial policy using SOEs.

USMCA also locked in the trade liberalisation reforms in the energy sector introduced by former Mexican President Peña Nieto (Gantz, 2020: 109). Those provisions are particularly relevant given Mexican President López Obrador's support of state-owned oil company PEMEX and electricity company CFE. López Obrador sought to prioritise PEMEX and CFE over private sector firms in the allocation of contracts, which ran against Mexico's obligations in USMCA and other trade agreements (IUST 2021b). Although López Obrador contended that the USMCA provisions on energy (chapter 8) grant Mexico the power to change its constitution and domestic laws regarding its energy sector (Reuters 2020), such modifications run against another trade agreement signed by Mexico which locked in Mexico's energy liberalisation reforms: the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP), effective since 2018. Furthermore, Article 32.11 of USMCA specifies that Mexico can modify its commitments 'only to the extent consistent with the least restrictive measures […] in other trade and investment agreements that Mexico has ratified prior to entry into force of this Agreement', which includes CPTPP. Mexican policy space on SOEs is thus highly

restricted. The López Obrador government was aware of those provisions but did not have the bargaining power to remove them from USMCA (which would have also required removing them from CPTPP to regain policy space) (interview, Mexican negotiator, 5 April 2023).

4.3.6. Foreign Investment Regulation

USMCA weakens the Investor-State Dispute Settlement (ISDS) mechanism: only government contracts for certain high sunk-cost sectors, including energy, retain full access to ISDS, including against indirect expropriation (Annex 14-E.6). In other sectors, firms must exhaust national remedies first and do not have the right to launch an ISDS investigation for indirect expropriation (Article 14.D.3). The removal of ISDS does not considerably increase *de facto* policy space for most activities, such as automotive production, for which expropriation yields little benefits given that the adequate functioning of an auto plant depends on the brand and logistics of the automaker. By contrast, in other activities such as the construction of seaports, dams and airports, the loss of ISDS creates policy space for indirect expropriation and will increase uncertainty for foreign investors.

The weakening of ISDS was promoted for different reasons by US Congressional Democrats and USTR Robert Lighthizer. While Democrats wanted to eliminate ISDS to regain policy space for health and environmental regulation, Lighthizer hoped that the elimination of ISDS would reduce incentives for firms to offshore production to Mexico by increasing investment uncertainty (IUST 2017m). According to a Canadian negotiator:

> The US wasn't interested in ISDS. And I believe the public message was the same as the private message, which is that ISDS is an insurance policy for American companies who send their jobs overseas. The US position was more in the interest of causing American companies to think twice before moving operations south of the border because they would lose that protection (interview, 5 March 2021).

By removing protection against indirect expropriation, Lighthizer hoped to create uncertainty as firms could no longer require compensation for a loss of profit due to regulatory changes, such as changes in intellectual property law, services regulation, and environmental standards. This change also provided governments with greater policy space to regulate for health, environmental or other public good purposes, following the regulatory chill created by several ISDS rulings (Laurens et al. 2019).

Although NAFTA already banned most performance requirements on foreign investment, such as exporting requirements, USMCA went slightly further by banning technology transfer requirements, such as on using a particular technology or on the duration or royalty rate of a licence contract (Article 14.10). Those measures are aimed at setting a precedent against China's trade practices and were promptly accepted by Mexican negotiators, who did not consider those provisions problematic given that Mexico had abandoned the use of such performance requirements on FDI (interview, Smith Ramos, 16 October 2020). Although NAFTA and USMCA prohibit the use of local content requirements, they set regional value content requirements in the form of rules of origin, which are in effect local content requirements applied at the North American level. These can be used by countries to increase domestic value-added in production.

4.3.7. Financial Regulation

USMCA introduces new commitments to liberalise cross-border financial services, such as investment advice, electronic payment services, and portfolio management (USMCA chapter 17). The changes to the financial sector policy space remain minor given that Mexico had adhered to extensive financial liberalisation under NAFTA. One notable exception is USMCA provisions against currency manipulation (USMCA chapter 33). Those measures were not

directly aimed at Mexico, which had not resorted to currency manipulation during the NAFTA period, but rather at setting a precedent against China's past practices (Trump administration official, September 30, 2020). The Phase One trade agreement, signed between the US and China in 2020, largely replicated the provisions in USMCA chapter 33, including a commitment 'to refrain from competitive devaluations and the targeting of exchange rates for competitive purposes' (US-China Phase One Agreement, Article 5.1.4).

With regards to capital controls, USMCA slightly increased policy space compared to NAFTA by allowing the use of temporary safeguards for external financial difficulties (Article 32.4). Capital controls have been essential for many countries to prevent or reduce financial instability by restricting the inflow and outflow of short-term speculative investments (Gallagher 2011; Stiglitz 1996). While the IMF recognised the role of temporary capital controls in reducing financial instability following the 1997 East Asian financial crisis, the US continued until recently to demand the prohibition of capital controls as a condition for signing a PTA (Elliott 2019: 14-15). The slight increase in policy space in USMCA for preventing financial instability has little impact on industrial policy, however, given that capital controls remain prohibited in normal circumstances. Those were used by East Asian miracle economies such as South Korea and Taiwan, and currently by China, to channel finance into long-term productive activities, as well as to discipline firms (Amsden 1989).

4.3.8. Overview

Table 4 presents a summary of the changes to Mexico's space for industrial policy between NAFTA and USMCA. Except for a few changes, such as the weakening of ISDS, the new provisions in USMCA further restrict Mexico's policy space for activist trade and industrial

policies, although only slightly more than NAFTA. As the discussion on ISDS demonstrated, what matters is not degrees of policy space but the utility of certain policy instruments.

TABLE 4. CHANGES TO POLICY SPACE FROM NAFTA TO USMCA

Industrial policy tool	Relevant provisions in USMCA	Policy space
Tariffs	Increased *de minimis* level from 50 to 117 US dollars	-
	Ban of tariffs on digital products	-
Non-compliance	Fixing of loopholes and increased coverage (labour, environment, digital sector, technical barriers) of the state-to-state DSM*	-
Technical barriers	Regulatory harmonisation with the US	-
	Regulation of the digital sector: bans data tariffs, data localisation requirements, and requirements for firms to disclose computer source code and algorithms	-
	Locking in of energy sector liberalisation reforms	-
Intellectual property rights	Increased copyright protection from 50 to 70 years	-
	Increased industrial design protection from 10 to 15 years	-
	Test data protection for agricultural/chemical and pharmaceutical products of 10 and 5 years, respectively	-
	Patent term extensions for delays of more than 5 years in granting a patent	-
	Criminalisation of trade secret theft by SOEs and digital content theft.	-
	Stricter protection of trademarks	-
State-owned enterprises (SOEs)	Expansion of the definition of what constitutes an SOE	-
	Strict restrictions on the provision of 'non-commercial assistance' between SOEs, and discrimination against foreign firms in procurement contracts.	-
Foreign investment regulation	Weakening of Investor-State DSM (ISDS) to cover only certain high sunk-cost sectors	+
	Ban on requirements for foreign firms to use a specific technology or apply a given royalty rate	-
	Stricter rules of origin for the North American automotive industry	+
Financial regulation	Stricter provisions against currency manipulation	-
	Authorisation of temporary capital controls to mitigate financial instability.	+

DSM*: Dispute settlement mechanism; +: increase in policy space; -: decrease in policy space.

Mexican negotiators and officials interviewed considered activist trade and industrial policies to be a relic of the past, abandoned by Mexico since its membership of NAFTA in 1994. As such, they were either favourable to new restrictions on policy space or considered the new provisions inoffensive additions to the agreement aimed at setting precedents against China (Mexican chief negotiators Seade and Smith Ramos, interviews, 15 and 16 October 2020). For

instance, Juan Carlos Baker, Undersecretary of Foreign Trade in the Peña Nieto administration, was 'particularly proud' of the new restrictions on SOEs introduced in the CPTPP and USMCA, and argued that the loss of policy space for industrial policies will not 'impede or hinder development in Mexico in any way' (interview, 10 December 2020).

Even Jesús Seade, chief negotiator for President López Obrador, argued that 'I don't think industrial policy should be such that it allows you to break your commitments, including commitments in intellectual property' (interview, 15 October 2020). This attitude challenges the structuralist literature, which assumes that foregoing policy space will negatively impact economic development. The NAFTA renegotiation differed from the original, however, in that the utility to Mexico of regaining policy space was lower due to path dependence. Path dependence reduced the utility of regaining policy space in USMCA through two mechanisms: the lock-in of policy space restrictions in other PTAs signed by Mexico, and increasing returns to NAFTA which led Mexican negotiators to focus on preserving market access and seek regulatory harmonisation with the US.

First, Mexico's development strategy since NAFTA has been to forge deep trade agreements with the rest of the world to secure preferential market access. Many of the new policy space restrictions in USMCA had already been accepted by Mexico in other trade agreements. According to Kenneth Smith Ramos, Mexican chief negotiator in the Peña Nieto administration:

> Once we came into the NAFTA, we started moving away from the traditional industrial policy models that had been followed in Mexico, and I think that continues now in the USMCA. The big question here is what will do the current administration in Mexico, which comes in with these ideas of having more government intervention in the economy. What has happened in some of the policies that they are trying to take, in the energy sector for example, to favour the SOEs, etc., is that they are running into a brick wall, because a lot of these industrial policy tools are now incompatible with what we have been pursuing in trade agreements and the WTO for the last 30 years. The gamble, or the decision that Mexico has made over the last 25 years, of entering into these types of trade agreements where they emphasise not using tariffs as an economic development

> tool, or utilising these traditional tools of industrial policy, is because we did it in the past and it failed (interview, 16 October 2020).

This view was shared by Jesús Seade, Mexican chief negotiator for the López Obrador administration, who emphasised the need for a 'new industrial policy' that should not consist of 'interference in the price mechanism, subsidies, and certainly not breaching your commitments' (interview, 15 October 2020). As such, even President López Obrador, a long-standing critic of NAFTA and supporter of industrial policy, did not regain policy space for industrial policies. Even in energy, the one sector where his administration attempted to regain policy space, he was unable to do so due to the commitments already negotiated in USMCA and the precedent set by the provisions in CPTPP.

Second, increasing returns to NAFTA led Mexican negotiators to prioritise preserving their access to the US market, which entailed advocating to maintain NAFTA commitments. Seade argued that for Mexico to breach its commitments would only incentivise further US unilateralism. The priority for Mexico during the negotiations was to maintain access to the US market, which entailed advocating for maintaining NAFTA commitments. This view was shared by Mexican negotiators in the Peña Nieto administration, who considered that the priority for Mexico was 'maintaining certainty' and 'maintaining openness, which implied that Mexico would maintain its commitments' under NAFTA' (interview, 20 November 2020, translated from Spanish). 'The intention was not to go backwards in any area, but rather to keep integrating' (Ibid.).

25 years of economic integration under NAFTA also increased the need for Mexican cooperation with the US. Between 1993 and 2019, the share of trade in Mexican GDP increased from 28 to 78 per cent, of which approximately 80 per cent is with the US (World Bank 2023). Mexico's integrationist strategy requires regulatory harmonisation with the US and Canada, which entails constraints on policy space. As supply chains are organised regionally rather than

nationally, Mexico benefits from facilitating regional trade and investment. While Mexico can implement some industrial policies on its own, the most powerful levers of structural change are at the regional level, such as the USMCA rules of origin. According to Juan Carlos Baker, Undersecretary of Foreign Trade in the Peña Nieto administration:

> As an OEM now has to comply with many new requirements, they will necessarily structure their supply chains down to the level of tier 2, or even maybe tier 3 suppliers, to be in Mexico. So that could probably be way more influential in terms of shaping industrial policy than any government-driven program (interview, 10 December 2020).

USMCA's strict rules of origin constitute an industrial policy for Mexico (in effect a local content requirement at the regional level). Being part of USMCA also enabled Mexico and Canada to benefit from the 7500 US dollars tax credit for electric vehicles as part of the Biden administration's Inflation Reduction Act. Half of the tax credit is conditioned on the extraction of critical minerals in the US or in a country with which the US has an FTA, or if the critical minerals were recycled in North America. The other half is conditioned on at least 50 per cent of the battery value being assembled in North America (Reinsch, Chauhan, and Duncan 2022). Although some of USMCA's stricter provisions can promote Mexico's structural transformation, others, such as USMCA's excessive intellectual property protections, undermine economic upgrading in Mexico; a point also recognised by free trade advocates (Lester and Manak 2019).

4.4. Conclusion

The renegotiation of NAFTA indicated a worsening of the market-access-policy space trade-off characteristic of North-South PTAs. Following the development-oriented typology of US trade policies developed in Chapter Three, Trump sowed the seeds of a *power-based* trade policy during the renegotiation by increasing uncertainty over access to the US market and

further restricting policy space. Yet by signing USMCA, Trump largely preserved his predecessors' *restraining* trade policy: USMCA maintained NAFTA's zero tariffs and even improved the enforceability of the trade agreement by fixing the state-to-state dispute settlement mechanism. The reasons for continuity between NAFTA and USMCA, despite the Trump administration's radical negotiating objectives, are examined in Part II (Process of Institutional Change), consisting of the next three chapters. These chapters demonstrate that path dependence constrained Trump to preserve a restraining trade policy towards Mexico and Canada, despite his objective of implementing a power-based one.

Path dependence also played an important role in determining the Mexican government's negotiating position. Left-wing President López Obrador had a long record of opposing NAFTA and campaigned in 2018 to implement industrial policies incompatible with Mexico's PTA commitments, such as support to state-owned enterprises and the energy sector. During the NAFTA renegotiation, President López Obrador agreed to all the provisions negotiated by his predecessor, except for the inclusion of a symbolic energy chapter reaffirming Mexico's sovereignty (Mexico's obligations in terms of energy liberalisation are maintained by USMCA Article 32.11, cf. section 4.3.5). Path dependence reduced Mexico's utility of regaining policy space in USMCA through two mechanisms: the lock-in of policy space restrictions in other PTAs signed by Mexico, and increasing returns to NAFTA which led Mexican negotiators to focus on preserving market access and seek regulatory harmonisation with the US. These two mechanisms are illustrated in the theoretical framework outlined in Chapter One.

The blackmailing and market access uncertainty created by the Trump administration during the NAFTA renegotiation demonstrated the vulnerability of Mexico's development strategy since 1994, which relied on stable access to the US market. Although market access certainty was restored with USMCA, the USMCA review periods and sunset clause create institutional opportunities for the US to revive market access uncertainty in the future to gain concessions

in terms of reductions in Mexico's market access or further policy space restrictions. The first review period in 2026 will determine whether US trade policy towards Mexico and Canada becomes *power-based* or remains *restraining*. Even if US trade policy remains restraining, it will continue to undermine structural economic change in Mexico given that certain policy space constraints, in particular excessive intellectual property protection, impede technology transfer and have been decried by both neoclassical and structural economists as anti-developmental (Bhagwati 2004; Lester and Zhu 2019; Chang and Andreoni 2020). The conclusion provides reflections on the policies which the US and Mexico could implement to promote the latter's economic catch-up.

PART II – PROCESS OF INSTITUTIONAL CHANGE

Chapter 5. Trump’s thwarted Negotiating Agenda

> *If you sort of go down a road that is like “Lighthizer was sort of playing mind games with these people. And he was sort of throwing all kinds of things out there to scare people or terrify people”. I mean, none of that's true. […] We were pretty much on a two-year clock, we thought if we didn't have a deal by the end of 2018, it was going to be very, very difficult to get anything done. And especially with the turnover in Mexico and having a new president come in, and you got to start all over. So we were under very great pressure to move very, very quickly. And in that context, you don't have time for posturing or poison pills or all that type of stuff. You're really trying very, very hard to get a deal.*
>
> Trump administration official, interview, 7 May 2021

5.1. Introduction

The Trump administration failed to achieve its initial negotiating objectives. The renegotiated NAFTA does not contain any of the US negotiating objectives deemed unacceptable by Mexico and Canada, such as voluntary export restraints, the removal of constraints on the use of trade remedies, and dollar-for-dollar government procurement. Other US demands were significantly weakened, such as a 50 per cent US-specific rule of origin in the auto industry (replaced by a lower high-wage requirement) and a five-year sunset clause (replaced by a revision period every six years and a sixteen-year sunset clause difficult to activate). In the case of the state-to-state dispute settlement mechanism, the Mexican and Canadian views prevailed as the mechanism was fixed to prevent a state from blocking the appointment of roster members. This chapter identifies ten key objectives of the Trump administration considered unacceptable by the Mexican and Canadian governments. It then demonstrates that none were included in USMCA in their original form and half were included in a significantly weakened form.

The chapter provides a detailed analysis of the negotiation process, starting with an examination of Trump's threats to withdraw the US from NAFTA. Trump did not withdraw the US from NAFTA to gain further leverage in the negotiations, despite little progress in achieving his initial negotiating objectives. After outlining negotiations over those ten objectives, the chapter demonstrates that the Trump administration was committed to those objectives rather than bluffing. The findings inform the next chapter, which explains this outcome by analysing the impact of path dependence on US-Mexico and US-Canada power asymmetries using the theoretical framework developed in Chapter One.

5.2. 10 Objectives and a Threat

Many of the Trump administration's negotiating objectives were unprecedented in trade negotiations and considered unacceptable by Mexican and Canadian negotiators, led by Chrystia Freeland and Ildefonso Guajardo, respectively. There are numerous lists and references in the media to those objectives, often under the label 'red line' or 'poison pills', the latter term coined by the US business sector (Expansión 2018; Morales 2020). The identification of the ten negotiating objectives considered unacceptable by the Mexican and Canadian governments is built on interviews with Mexican and Canadian negotiators. The list does not include the US demand to backtrack on NAFTA's cross-border liberalisation of trucking services given that this measure was never implemented under NAFTA. USMCA preserves the NAFTA rule but allows the US International Trade Commission to stop issuing licences to Mexican truckers should it detect 'material harm' (Fisher 2021; Russell 2014). According to Mexican chief negotiator Smith Ramos, 'it really doesn't change the present situation […], it's just political messaging from the United States to its own unions without any real impact' (interview, 16 October 2020).

Table 5 provides an overview of ten key US negotiating objectives identified as red lines by the Mexican and Canadian governments. Of the ten, none are included in their original form in USMCA and five are in a significantly weakened form, such that they no longer reflect the original US proposal. Canada and Mexico also successfully conditioned the signing of USMCA on the removal of US tariffs on steel and aluminium, which were replaced by *de facto* voluntary export restraints aimed at preventing arbitrage. The negotiating objectives and negotiation process are detailed in section 5.4.

TABLE 5. 10 NEGOTIATING OBJECTIVES OF THE TRUMP ADMINISTRATION CONSIDERED UNACCEPTABLE BY THE MEXICAN OR CANADIAN GOVERNMENTS.

Trump administration's negotiating objectives	Mexico's position	Canada's position	Objective attained?
1. Force Mexico to impose VERs to reduce the US trade deficit.	No voluntary export restraints (VERs).	NA	**No:** weak VER on steel and aluminium for other reasons than the deficit.
2. Obtain 50 per cent US-specific ROO in the auto industry.	No US-specific rules of origin (ROO), no wage requirement	No US-specific rules of origin (ROO), but wage requirement okay.	**Partly**: No US-specific ROO, 40-45% high-wage ROO (in effect 25-30% due to exceptions).
3. Include a five-year sunset clause.	No sunset clause.	No sunset clause.	**Partly:** 6-year review; 16-year sunset clause.
4. Eliminate Investor-State Dispute Settlement (ISDS).	Maintain NAFTA rules.	Not a red line.	**Partly**: ISDS weakened between US-Mexico and eliminated between US-Canada.
5. De facto eliminate State-to-State DSM*.	Improve state-to-state DSM.	Improve state-to-state DSM.	**No:** DSM is improved.
6. Eliminate AD/CVD DSM* and facilitate trade remedies on agriculture.	Maintain NAFTA rules	Maintain NAFTA rules.	**No:** AD/CVD DSM and NAFTA rules are maintained.
7. Facilitate the imposition of safeguards.	Maintain NAFTA rules.	Maintain NAFTA rules.	**No:** NAFTA rules are preserved.
8. Severely restrict access to the US government procurement market.	Maintain NAFTA rules.	Maintain NAFTA rules.	**Partly:** NAFTA rules are only kept between Mexico and the US.
9. Increase access to Canada's dairy market.	NA	Maintain NAFTA rules.	**Partly:** US access reaches 3.6% of the Canadian dairy market.
10. Eliminate Canada's cultural exemption.	NA	Maintain NAFTA rules.	**No:** NAFTA rules are preserved.

*DSM: Dispute Settlement Mechanism; AD/CVD: Anti-Dumping Countervailing Duty; VER: Voluntary Export Restraint; ISDS: Investor-State Dispute Settlement; ROO: Rules of Origin; NA: Not applicable

US chief negotiator John Melle argued that USMCA led to significant US victories, such as stricter rules of origin in the auto industry and the inclusion of a sunset clause (interview, 16 December 2020). However, while the US undeniably obtained concessions during the renegotiation, the agreement has more similarities with NAFTA than with Trump and Lighthizer's original vision. A five-year sunset clause and the elimination of all dispute settlement mechanisms would have severely undermined the market access certainty provided by USMCA. The imposition of voluntary export restraints to reduce the US trade deficit, a 50 per cent US-specific rule of origin in the auto industry, severe restrictions on Mexico and Canada's access to the US government procurement market, and new trade remedies for agricultural products would have openly challenged the logic that trade negotiations seek to liberalise trade. The absence of such provisions in USMCA explains why analysts have described the trade agreement as a NAFTA 2.0 rather than a paradigm change (Anderson 2020: 155; Gagné and Rioux 2022; Manak 2022).

Although central to the NAFTA renegotiation and ground-breaking, USMCA labour standards are not analysed here given that both the US and Mexico changed their negotiating objectives over time. The Trump administration was initially opposed to the inclusion of dispute settlement mechanisms in USMCA, preferring to enforce USMCA labour provisions through unilateral actions. Following the Democratic Party's victory in the 2018 mid-term House of Representatives elections, however, USTR Lighthizer agreed to pursue the Democratic objective of enforcing labour standards through the state-to-state DSM and the creation of a Rapid Response Labour Mechanism. In Mexico, the election of left-wing candidate López Obrador as President in 2018 also changed the Mexican government's position in favour of stronger labour provisions. President López Obrador used USMCA labour provisions to lock in his labour reform, as discussed in Chapter Seven. As such, certain USMCA labour provisions were no longer considered unacceptable by the Mexican government.

It is important to distinguish between the Trump administration's policy target (overarching objective), policy instruments (negotiating objectives), and tactics. The overarching objective of the Trump administration during the NAFTA renegotiation was the reduction of the US trade deficit with Mexico and the reshoring of manufacturing production to the US (Lighthizer 2023; IUST 2017v; USTR 2017b, 2017a). To meet this policy target, the Trump administration pursued protectionist negotiating objectives. In terms of achieving the policy target of reducing the US trade deficit with Mexico, the Trump administration was unsuccessful: the US trade deficit in goods and services with Mexico nearly doubled from 71.1 billion US dollars in 2017 to 131.1 billion in 2022 (US Bureau of Economic Analysis 2023; USTR 2023b).

Although not an objective but a negotiating tactic, a US withdrawal from NAFTA to gain leverage in the negotiations was considered by Mexican and Canadian negotiators as the most harmful policy given its economic consequences. Trump repeatedly threatened to withdraw the US from NAFTA unless Mexico and Canada conceded to major US negotiating demands. This disruptive strategy was aimed at 'breaking history' given the path dependence created by NAFTA (Kushner 2022). Given that Trump sought to negotiate a new trade agreement in only six months, his strategy consisted of withdrawing the US from NAFTA to exert pressure on Mexico and Canada to quickly make concessions. By contrast, the Mexican and Canadian governments implemented a status-quo tactic by communicating on the costs of breaking path dependence and attempting to preserve NAFTA rules.

5.3. The NAFTA Withdrawal Threat

To obtain concessions from the Mexican and Canadian governments, Trump repeatedly threatened to withdraw the US from NAFTA by presidential decree. A private conversation between Trump and Gary Cohn, his chief economic adviser, reported by Woodward (2018:

274), confirms Trump's commitment to withdrawing the US from NAFTA: 'The only way to get a good deal is to blow up the old deal. When I blow it up, in that six months, they'll come running back to the table'. Furthermore, Gary Cohn and White House staff secretary Rob Porter later admitted to removing from Trump's desk executive orders to withdraw the US from NAFTA that the President had requested (Ibid: 233). Trump was initially committed to withdrawing the US from NAFTA.

The closest that Trump came to withdrawing the US from NAFTA occurred on 25 April 2017, four months before the start of negotiations. Trump planned to notify Congress of his intention to withdraw to mark the hundredth day of his Presidency (Ibid.: 155-8). His team was divided, however, and upon hearing the news Commerce Secretary Wilbur Ross and Agriculture Secretary Sonny Perdue urged him to reconsider, while chief strategist Stephen Bannon and trade adviser Peter Navarro sided with the President. As the news erupted, hundreds of business executives lobbied the administration to ensure Trump would not sign the executive order. Agricultural groups were most vehement in opposing a withdrawal, arguing that doing so would enable Mexico to reimpose tariffs on US agricultural products (IUST 2017a; Parker et al. 2017). Accounts of the meeting stress that the key element that changed Trump's mind was a map, brought by Perdue from a meeting with US agricultural business groups, of the US states and counties hardest hit by a US withdrawal, of which many had voted for Trump in 2016 (Ibid.; Parker et al. 2017). The economic costs of a NAFTA withdrawal (and political repercussions for the Republican Party in the midterm elections) were determinant in changing Trump's mind.

The role of US lobbies in dissuading Trump from triggering the withdrawal process is also clear from a media interview with Kenneth Smith Ramos, Mexican chief trade negotiator under President Peña Nieto, when asked whether Trump was likely to withdraw from NAFTA:

> At the beginning of the negotiations, the US administration felt like this was a win-win strategy in which the US would either make Canada and Mexico accept radical changes

> to the NAFTA or it would pull out of the agreement without any cost. But what we saw throughout the negotiation was a very strong movement within the US private sector – starting with the American Farm Bureau, following up with all of the industrial manufacturing sectors – in showing that if the US unilaterally pulled out of NAFTA, at least in the case of Mexico they would lose their main export market for over 30 states in the US (IUST 2019b).[9]

Indeed, as negotiations progressed, US business groups organised to dissuade Trump from withdrawing from NAFTA, informing him of the economic costs of doing so, as they had done on 25 April 2017. Hundreds of business groups repeatedly urged Trump to maintain NAFTA (IUST 2017h, 2017b). The US Chamber of Commerce argued that a US withdrawal would hurt states that had voted for Trump in 2016 (IUST 2017c), while US agricultural groups strongly lobbied Congress to block any attempt by Trump to unilaterally withdraw (IUST 2017a). Even US labour unions supported a renegotiated deal over no deal, given that NAFTA had already reshaped production structures in North America (interviews with labour union representatives, 15, 17 March and 2 April 2021; Byrd 2019).

Congressional members from both parties responded to Trump's withdrawal threats by indicating that they opposed a US withdrawal from NAFTA and would pass legislation to block Trump's attempt to do so unilaterally. Republican representatives in Congress, who controlled both the House and the Senate, pressured Trump not to withdraw (IUST 2017q) and joined with the US business sector in informing him that a US withdrawal would undermine prospects for Republican candidates during the 2018 mid-term elections (IUST 2018b). Republican Senator Hatch also echoed the views of other members of Congress in arguing that Congress would implement 'veto-proof' legislation to prevent the executive from unilaterally terminating NAFTA (IUST 2018g). Although most Democrats voted against NAFTA in 1993, they campaigned to preserve the agreement. Richard Neal, the top-ranking Democrat in the House

[9] This is an exaggeration. In 2018, Mexico was the first export market to 7 US states, second export market to 20 US states, and third export market to 3 US states (cf. Figure 7).

Ways and Means Committee, argued that Congress would block an attempt by the executive to unilaterally withdraw the US from NAFTA (Allen-Ebrahimian 2017).

It is unclear whether Congress would have succeeded in preventing Trump from unilaterally withdrawing the US from NAFTA. On the one hand, Trump was 'very likely' to succeed in terminating NAFTA given that the trade agreement did not specify that Congress must give authorisation for a withdrawal and that NAFTA had foreign policy implications, which fall under the President's power (Hufbauer 2017). On the other hand, it is likely that a NAFTA withdrawal by executive decree would not have removed many NAFTA provisions passed by Congress in the NAFTA Implementation Act, especially if Congress passed 'veto-proof' legislation to ensure that outcome as suggested by Republican Senator Hatch (Ibid.; IUST 2018g; Riley 2019). Although the Trump administration preferred not to start a legal battle with Congress, it was committed to attempting to withdraw the US from NAFTA by executive decree should the negotiations yield no progress. A Trump administration official recalled:

> If we had been unable to get a deal that he found acceptable, I don't have any doubt that he would have tried to pull out of NAFTA. I don't think that was ever a plough or a trick or anything. His view was, and he said this many, many, times, the best outcome is an improved deal, the second-best outcome is we pull out of NAFTA. Staying in NAFTA, we are not going to do that. I don't think there is any chance on earth that the President was going to run for re-election in 2020 and still be under the old NAFTA. He had promised the voters over and over and over that he was going to get out of it and that he was going to change it. He was going to keep that promise (interview, 12 May 2021).

Similarly, Mexican chief negotiator Smith Ramos argued that Mexico's concessions in the auto industry were key to persuading Trump not to withdraw the US from NAFTA (interview, 16 October 2020). The concessions obtained, however, are much weaker than the Trump administration's initial objective.

5.4. The Negotiating Objectives

This section details the negotiation process over the first four US negotiating objectives (voluntary export restraints, auto rules of origin, sunset clause, and ISDS). It ends with a summary of the negotiation process over objectives 5-10.

5.4.1 Force Mexico to Impose Voluntary Export Restraints

US Trade Representative (USTR) Lighthizer demanded the inclusion of voluntary export restraints (VERs) in USMCA that would tie the trade agreement to the reduction of the US bilateral trade deficit with Mexico. This measure is not included in USMCA. Referring back to the WTO's ban of VERs under Article 11b of the Agreement on Safeguards, USMCA Article 2.11 prohibits the use of VERs. Mexican chief negotiator Smith Ramos recalled:

> You will not find the one chapter that supposedly was the only thing that Trump wanted, which is a chapter that allows for trade barriers to be imposed if there is a trade deficit or if the trade deficit grows. They did propose at the beginning for autos and other successful sectors like agriculture and textiles these triggers: that if the deficit goes up by a certain percentage, then Mexico automatically imposes voluntary export restraints (interview, 16 October 2020).

Interviews with White House staff indicate that Trump and US Trade Representative (USTR) Lighthizer were both determined to create mechanisms to force the reduction of the US trade deficit. This is also clear from Woodward's (2018: 274) account of the Trump administration. Trump identified reducing the US trade deficit as the central objective of the negotiations, while Robert Lighthizer developed the idea of VERs as a means to do so. As Deputy USTR in Ronald Reagan's administration, Lighthizer built his reputation by imposing VERs on Japan to reduce the US trade deficit.

Congressional representatives did not strongly oppose the use of VERs. According to a Democrat trade official:

> Most Republicans are (pro) free trade, so if there would have been any pushback (against VERs), it would have been from free trade Republicans, but they were scared to push back against Trump because President Trump is a Republican […] Voluntary export restraints in trade agreements, Democrats are generally ok with that. So no, there was not a lot of pushback on the Hill (interview, 12 May 2021).

As to the illegality of VERs in the WTO, it was seen as largely 'irrelevant' by Congressional representatives (Ibid.). The irrelevance of the WTO's ban on VERs in the eyes of US Congressional Representatives is confirmed by a Trump administration official:

> I don't think that anybody was all that concerned about the WTO. […]. In America, if you are a member of Congress, it is very difficult to come out and say 'Well I don't think that we should make our trade policy. I think the WTO should make our trade policy and we Americans should just do what Geneva tells us to do (interview, 7 May 2021).

While Congress was not strongly opposed to VERs, one should expect that firms exporting from Mexico to the US lobbied strongly against those measures. However, news of the Trump administration's proposals for VERs did not even reach US firms. John Murphy, who directed the US Chamber of Commerce's lobbying efforts on trade policy, did not have to lobby strongly against VERs:

> I do recall a sense in Washington that Lighthizer would seek voluntary export restraints on various products. During the negotiations, reports on this were vague, but of course, when Lighthizer was Deputy USTR in the Reagan administration, he led the charge for VERs on Japanese autos. In the event, we never saw VERs in the true sense (interview, 17 May 2021).

The author's review of over 2000 articles on the NAFTA renegotiaton published by the specialist newspaper *Inside US Trade* (IUSTR) between 2016-2020 confirms that VERs did not receive much media coverage during the negotiations, except for steel (IUST 2018j). The reason for the lack of pushback from US firms is that, as stressed by Mexican chief negotiator Smith Ramos, US proposals to include VERs were tabled at the beginning of the negotiations and

soon abandoned, leaving little time for US firms to lobby against them (interview, 16 October 2020). The Mexican and Canadian governments refused to consider imposing VERs, arguing that those were outlawed by the WTO. Given this unwavering opposition, Lighthizer focused instead on indirect mechanisms to reduce the US trade deficit, such as auto industry rules of origin.

Although VERs tied to the reduction of the US trade deficit are not included in USMCA, Lighthizer succeeded in including a soft version of a VER for steel and aluminium. In May 2018, the US agreed to eliminate its national security tariffs on Mexican and Canadian steel and aluminium in exchange for both countries eliminating their retaliatory measures. A joint statement by all three countries specified that each can impose tariffs of 25 and 10 per cent on steel and aluminium, respectively, when imports 'surge meaningfully beyond historic volumes of trade' (Hufbauer and Jung 2019). According to a Trump administration official, this measure sought to prevent arbitrage given that steel and aluminium tariffs remained in place for imports from other countries (interview, 30 September 2020). Without this provision, Mexico or Canada could import steel or aluminium duty-free and then sell it with a 10/25 per cent mark-up in the US market. This is precisely what the Trump administration accused Canada of doing in August 2020, leading to a brief reimposition of tariffs on aluminium. The Canadian government retaliated and, by September 2020, both countries found a compromise to eliminate tariffs again. Although the measure was officially aimed at preventing arbitrage, it was decried as disguised protectionism by the Mexican and Canadian governments.

5.4.2. Obtain 50 per cent US-specific Auto Industry Rules of Origin

In another attempt to reduce the US trade deficit with Mexico, the Trump administration demanded a 50 per cent US-specific rule of origin in the auto industry for both original

equipment manufacturers (OEMs) and auto parts producers (Trump administration official, interview, 7 May 2021; IUST 2017n). The measure was aimed at forcing auto firms operating in Mexico to re-shore their production to the US. Given that most of the US trade deficit with Mexico was attributable to autos, this industry was the focus of Trump and Lighthizer's efforts (Lighthizer 2020, 2023). During his presidential campaign, Trump singled out the loss of auto manufacturing jobs to Mexico. Officials in his administration approved this negotiating stance, as '9 out of the last 11 North American auto plants were built in Mexico' (Ibid.; interview, 30 September 2020). US-specific content would force firms to re-shore auto plants to the US.

While the US asked for other changes to the auto rules of origin, the demand for a US-specific rule of origin was unacceptable to Mexico and Canada because it undermined the logic of a regional free trade agreement. The proposal was not included in USMCA but replaced by a Labour Value Content (LVC) requirement that 40/45 per cent of the value of passenger vehicles and trucks, respectively, must be produced in plants where direct production workers earn on average at least 16 US dollars per hour (the requirement only applies to OEMs, and not to suppliers as originally requested by USTR). Although the 16-dollar figure is not annexed to inflation, wages in Mexico are much lower and that figure is likely to be adjusted for inflation during renegotiations.

In its form, the shift from a US-specific auto ROO to a labour value content rule was a significant weakening of the US proposal given that it maintained the norm of regional requirements in PTAs instead of establishing a national requirement. In terms of substance, the 40/45 per cent high wage requirement was also a significant step back from the 50 per cent US-specific rule of origin. Of the 40 per cent high-wage requirement for passenger vehicles, 10 per cent can be deducted for high-wage technology expenditures (R&D and IT) and 5 per cent for high-wage assembly expenditures (engine, transmission or battery assembly plants), which in effect reduces the requirement to 25 per cent (a similar system applies to trucks, reducing the

requirement from 45 to 30 per cent). According to government officials and auto industry representatives interviewed in all three countries, these changes ensured that plants would not be re-shored from Mexico to the US (interviews, 16 November 2020, 8 and 16 February, 9 September 2021). A Mexican negotiator recalled:

> Lowering the requirement from 50 per cent to 40 per cent essentially gets where the market was at that point. By leaving that at 40 per cent, there wouldn't be any need to shut down plants in Mexico or do any sudden shifts in production from Mexico to any of the other two countries […]. The computation towards that 40 per cent includes a lot of things, so it is not that difficult to get to that 40 per cent (interview, 7 April 2021).

According to a Trump administration official, 'what we expect is that the (LVC) rules actually lock-in the kind of existing divide and then there's a slow transition to have a little bit more made in the United States and or Canada' (interview, 10 March 2021).

While Republicans in Congress tended to oppose stricter rules of origin for the auto industry, Democrats were more sympathetic to Trump's objective. As one Congressional Democrat official argued, Trump's approach to rules of origin 'grew out of Democratic criticism of the TPP (Trans-Pacific Partnership)' (interview, 23 October 2020). Nevertheless, the Trump administration's initial proposals on autos, including the 50 per cent US specific rule of origin, were met with bipartisan opposition in Congress. This was due to auto industry groups lobbying against USTR's proposal, warning that it would render the North American auto industry uncompetitive (IUST 2017l). Several House members sent a letter to USTR Lighthizer warning that the proposal 'would eliminate the competitive advantages provided to the US auto industry under the current NAFTA rules' (Ibid.). According to Mexican chief negotiator Smith Ramos:

> The US government's position was so divergent from what its own industry wanted that it took six months for a real proposal from the US to be put on the table. We started in August 2017 and it wasn't until the end of January 2018 […] that the US put a full-text proposal on the table. And what did they want in the beginning? It was absurd. They wanted regional value content to go above 90 per cent, they wanted to impose salaries in the auto sector in Mexico from the trade agreement, which was impossible as well,

> they wanted to have within the rules of origin context the obligation that 50 per cent of the vehicle had to come from the US, not Canada or Mexico, just the US. All that we rejected and the three productive sectors of the three countries rejected (interview, 16 October 2020).

Despite pushback from Mexican and Canadian negotiators, the US Congress and the auto sector, Lighthizer remained committed to a 50 per cent US-specific rule of origin. Representatives of the auto industry confirmed that Lighthizer was not very responsive to their demands for meetings and to 'do no harm' (IUST 2017k). USTR initially only spoke to its domestic OEMs (Ford, GM, Chrysler), leading foreign OEMs to lobby Congress and governors instead (interviews, 16 November 2020, 9 September 2021). According to a Mexican official interviewed:

> The US auto industry initially pushed back on everything. They were hoping to discard all these changes. But when they realised that some changes were inevitable, they started working on making sure that the negotiating sides had accurate information. So instead of 50 per cent, make it 40 per cent. That was an input from the auto industry. Regional content rules were also calibrated not to the US initial demands but to a point that was provided by the auto industry, to make sure that the agreement did not create damage to the industry (interview, 7 April 2021).

Although pressure from the US auto industry moderated some of Lighthizer's proposals, he did not abandon his proposal for a US-specific rule of origin until a compromise with Canada was reached in March 2018.

From October 2017 to March 2018, Canada and Mexico jointly opposed Lighthizer's proposal for US-specific rules of origin (IUST 2017f, 2017g). Canadian and Mexican negotiators even refused to make a counteroffer, arguing that the US proposal was unacceptable (Flavio Volpe, President of Canadian auto parts association, and Mexican official, interviews, 8 February and 7 April 2021). Their opposition was successful in that, by late March 2018, Lighthizer offered to abandon the US-specific content proposal in exchange for a 15 dollar high-wage regional rule of origin (IUST 2018u). This 'worked to Canada's advantage' given Canada's high wages,

and thus exerted pressure on Canada-Mexico cooperation (IUST 2018g; US chief negotiator Melle, interview, 16 December 2020). A Canadian negotiator recalled that their interests on this issue could be aligned with the US:

> All of the issues that were put on the table by the US that we viewed as not realistic, we still sort of viewed them as anchored in some sort of policy goal. And in the case of autos, what we wanted to try and figure out was a bit more about what the underlying US concern was. And in a lot of ways, it was pretty easy, because it's the same concern that we have in our auto sector: our auto sector is good, and it's strong, but it has been subject to a bit of leakage towards cheaper inputs, if you will, and labour down in Mexico. And so we definitely had conversations with the US about the importance of making sure that whatever outcome we arrive at reflects a shared perspective on balancing the playing field within North America, and in particular, guarding the integrity of the Canada-US auto industry (interview, 5 March 2021).

The US strategy of dividing Mexico and Canada proved successful as, while Mexico argued that the US proposal remained unacceptable, the Canadian government sided with the US, forcing Mexico to concede. A Canadian negotiator recalled that 'Mexico was furious with Canada in advancing this because they hoped that Canada would hold the line with them against linking wages with rules of origin' (interview, 2 November 2020).

By May 2018, the pressure on Mexico increased even more as the US Commerce Department launched a Section 232 investigation to impose national security tariffs on auto imports (IUST 2018c). Similarly, the threat of Section 232 tariffs incentivised North American auto firms to find a compromise. According to an auto industry representative:

> On a 40,000-dollar car, you've (USTR) got 800 dollars' worth of leverage. Once you get beyond that, companies would just say "Okay, I'll just pay the 2.5 per cent tariff." That was early on in the negotiations. Frankly, it didn't really go very far. Then the USTR introduced the notion of Section 232 tariffs on vehicles […]. At that point, things changed and the leverage changed from the negotiators on the Mexican and Canadian side to USTR, meaning the threat of Section 232 tariffs on automobiles made it a lot more difficult and challenging for Canada and Mexico, and frankly all the automotive companies, because I think we were fairly aligned in positions with Canada and Mexico at the time (interview, 16 November 2020).

Shortly after the threat of Section 232 tariffs, the Mexican government agreed to a 16 US dollar wage requirement for 40 to 45 per cent of the value of autos originating in North America.

5.4.3 Include a Five-year Sunset Clause

The proposal of a five-year sunset clause in USMCA was conceived by US Trade Representative (USTR) Robert Lighthizer and received strong support from President Trump (IUST 2017r). It served several purposes. First, a sunset clause would increase a president's power in future negotiations by facilitating the process of withdrawal. Lighthizer's idea was that, by refusing to sign a renewed trade agreement, a president would be able to force a withdrawal, by contrast to the situation under NAFTA in which Congress could undermine an attempt by the President to do so. Second, a five-year sunset clause would contribute to Trump's agenda of reshoring industrial production to the US. With a sunset clause, firms have to consider the risk of the trade agreement not being renewed when deciding whether or not to invest in Mexico and Canada. Third, a sunset clause would increase US leverage over Mexico and Canada in future trade negotiations as the threat of a unilateral withdrawal from the US President would be more credible. In USMCA, the US proposal is weakened to a sixteen-year sunset clause. Withdrawing through this clause is difficult, however, given that a country must state its intention to withdraw eleven years in a row (from the sixth to the sixteenth year) for the clause to enter into force, which implies that at least three US governments support a withdrawal.

The Trump administration's commitment to the five-year sunset clause can be inferred from Trump and USTR Lighthizer's efforts until the last days of the negotiations to include it in the trade agreement (IUST 2018q), but also from Lighthizer's belief in the need to create mechanisms to re-shore production to the US (Lighthizer 2020, 2023). For Lighthizer, the

market access certainty provided by trade agreements constituted in effect a subsidy for US firms to offshore production (Ibid.). In a public statement in October 2017, he argued that firms should 'calculate that (risk) into (their) investments'(IUST 2017i).

Republicans in Congress and US business groups both opposed the inclusion of a five-year sunset clause in the agreement, arguing that it would undermine the benefits of the trade agreement by creating uncertainty. For instance, Republican senators Portman and Roberts, members of the Senate Finance Committee, positioned themselves against a sunset clause from the start of the negotiations (IUST 2017p). Similarly, US firms criticised a five-year sunset clause as counterproductive, and big business associations such as the US Chamber of Commerce lobbied the government to remove that objective from the negotiations (IUST 2017b). Democrats, however, were less concerned about the sunset clause (Congressional Democrat official, interview, 23 October 2020), while US labour unions supported its inclusion in the agreement. According to US chief negotiator John Melle, domestic pressure was partly responsible for the adoption of a weaker sunset clause in the trade agreement (interview, 16 December 2020, cf. quote at beginning of chapter). Until the end of the negotiations, however, Lighthizer was still pushing for a five-year sunset clause, telling House Republicans that he did not intend to abandon this objective (IUST 2018e). Although pressure from US firms and Republicans in Congress weakened Lighthizer's position, he remained committed to achieving this negotiating objective.

The determinant factor in preventing the inclusion of a five-year sunset clause was Canada and Mexico's cooperation against the US proposal. From the start, both countries positioned themselves firmly against a sunset clause (IUST 2017i). Mexico made counteroffers, suggesting a five-year review mechanism to allow countries to update the agreement, but objected to a sunset clause in case the review period failed (IUST 2017o, 2018s). Following the shift from trilateral to bilateral talks as a result of US pressure, Canada also resisted Trump's blackmail to

include a sunset clause. In May 2018, Trump conditioned his meeting with Canadian Prime Minister Trudeau on Canada accepting a five-year sunset clause to the agreement, which Trudeau refused (IUST 2018q). Towards the end of the negotiations, Trump suggested that he would accept a longer-term sunset clause (IUST 2018r). Yet a few weeks before the end of the negotiations, Mexico and Canada were still resisting US demands for a five-year sunset clause (IUST 2018l).

In the endgame, Mexico agreed in bilateral talks with the US to abandon its demands on retaining the antidumping and countervailing duty dispute settlement mechanism (NAFTA chapter 19), while the US conceded to replace the sunset clause with a clause to revise the agreement every six years (Mexican chief negotiator Ramos, interview, 16 October 2020; Forbes 2018). Mexican negotiators were hoping that Canada would be able to retain chapter 19, however, and then demand equal treatment, which is what occurred: NAFTA chapter 19 is preserved as USMCA chapter 10. (Ibid.; cf. section 5.3.7). Along with pressure from US lobbies and Congress, cooperation between Mexico and Canada prevented the inclusion of a five-year sunset in USMCA (but did not prevent a sixteen-year sunset clause).

5.4.4. Eliminate the Investor-State Dispute Settlement Mechanism

Just as for the five-year sunset clause, Lighthizer proposed to eliminate the NAFTA Investor-State Dispute Settlement (ISDS) mechanism to increase the risk of investing in Mexico, and thereby incentivise firms to invest in the US instead (IUST 2017b). USMCA contains a weakened ISDS mechanism between the United States and Mexico. NAFTA ISDS provisions including protection against indirect expropriation are kept for certain high-sunk cost sectors in energy and infrastructure. In other sectors, ISDS no longer protects against indirect expropriation. Although the weakening of ISDS was a setback compared to Mexico's initial

objective of maintaining full ISDS coverage, it did not considerably alter investment risk in Mexico. The Mexican government was concerned with preserving certainty for investments in its energy sector, which had just been liberalised by President Peña Nieto (IUST 2018o). In industries most at risk of expropriation, such as energy and infrastructure, USMCA maintained NAFTA ISDS provisions. In other sectors, expropriation risks are much lower than they were when NAFTA entered into force in 1994. As remarked by a Mexican negotiator, 'there was no ISDS case for the auto industry during the NAFTA period, which shows that it was not needed anyway' (interview, 20 November 2020). Indeed, the US auto industry did not consider the preservation of ISDS a priority in the negotiations (IUST 2018o).

Lighthizer was initially committed to eliminating ISDS between Mexico and the US. He considered ISDS an infringement on US national sovereignty and hoped that its elimination would encourage firms to invest in the US instead of Mexico. According to a Trump administration official, Lighthizer believed ISDS hindered the US comparative advantage in the rule of law by guaranteeing secure property rights to firms that offshore production to Mexico (interview, 30 September 2020). Similarly, Trump towards the end of the negotiations characterised the elimination of ISDS as a second sunset clause, suggesting their similar purpose as mechanisms to increase the uncertainty associated with offshoring production to Mexico (IUST 2018r).

The US Congress was divided on retaining ISDS. Republicans opposed Trump's objective as contrary to US firms' interests, while Democrats endorsed the proposal. Republicans had long been advocating for investment protection for US multinationals abroad, and many continued to do so during Trump's presidency. In March 2018, Republican Orin Hatch, chairman of the Senate Finance Committee, and Republican Kevin Brady, chairman of the House Ways and Means Committee, informed Lighthizer that Republicans may vote against the new trade agreement if it does not contain ISDS (IUST 2018f). By contrast, Democrats called for the

removal of ISDS to regain policy space for environmental and social policies (IUST 2017d, 2017e).

US business groups lobbied to retain ISDS, although the oil and gas industries were more committed to this objective than others. From the very start of the negotiations, major US industry groups called for the preservation of ISDS (IUST 2017j). The Presidents of the US Chamber of Commerce, the US National Association of Manufacturers, and the US Business Roundtable all conditioned their support of a new trade agreement to the inclusion of ISDS (IUST 2017t). To reduce opposition from US businesses, Lighthizer proposed that each country be able to opt into ISDS rather than eliminating ISDS (with the clear intention of opting out the US from ISDS). As such, a few months after the start of the negotiations, the US business sector had already succeeded in weakening Lighthizer's proposal from eliminating ISDS to allowing Mexico to opt in ISDS while the US would opt out.

Mexican negotiators announced that they would not opt-in ISDS if the US opted out, however, which led a coalition of US business groups to oppose Lighthizer's proposal (IUST 2017b). The US energy sector was most concerned with the removal of ISDS. The American Petroleum Institute (API) in particular lobbied strongly to preserve ISDS in Mexico to guarantee continued access to Mexico's newly opened energy market (IUST 2018n). Following talks with the US energy sector, the Trump administration changed its position to advocate for an ISDS that covered only certain sectors, such as energy and infrastructure. A Trump administration official interviewed explained the necessity of ISDS for high sunk-cost sectors by arguing that expropriation of an energy plant is easier and more lucrative for a government than expropriation of an auto plant (interview, 30 September 2020). In the case of an oil refinery, for instance, the ability to change suppliers more easily and to export to other countries than the US facilitates expropriation. By contrast, operating an auto plant in Mexico requires control of a complex supply chain controlled by an OEM and access to the US market, both of which can

be easily removed through retaliatory measures by the expropriated firm or the US government. Pressure from US energy firms in particular led to the shift in USTR's position from eliminating ISDS to narrowing down its scope to cover industries most at risk of expropriation. US chief negotiator John Melle confirmed this analysis, stressing the role of US firms in changing the Trump administration's position on this issue (interview, 16 December 2020).

Mexico and Canada did not provide strong or unified resistance to the US proposal of eliminating ISDS. While the Peña Nieto government focused on preserving certainty for foreign investments in its energy sector, the Trudeau government was confident in the investment certainty provided by Canada's long tradition of maintaining the rule of law. Furthermore, Canada had lost 314 million US dollars in ISDS claims under NAFTA, and Canadian civil society groups were lobbying against ISDS for having a 'chilling effect' on regulation in the public interest (IUST 2018k). By February 2021, Canada accepted the elimination of ISDS in the hope that the US would agree to retain the NAFTA antidumping and countervailing duties dispute settlement mechanism (IUST 2018n). Mexican negotiators could have maintained the NAFTA ISDS provisions by accepting the opt-in/opt-out US proposal but chose a more limited ISDS mechanism given the low cost of no coverage for certain industries, such as autos (interview, 20 November 2020).

5.4.5. Summary of Objectives 5-10

Objective 5: Eliminate NAFTA State-to-State DSM

In addition to ISDS, the Trump administration also sought to eliminate the NAFTA state-to-state dispute settlement mechanism. The state-to-state DSM had been dysfunctional since 2000 when the US blocked the appointment of judges to a dispute settlement panel on sugar. In the NAFTA renegotiation, the Trump administration attempted to further weaken the state-to-state

DSM by proposing that its decisions be non-binding, such that the US could ignore a ruling it considered 'clearly erroneous' (IUST 2017u). This proposal *de facto* amounted to eliminating the state-to-state DSM, given that its main purpose is to provide enforceable resolutions of trade disputes. At the first signing of USMCA, in September 2018, the DSM remained in its NAFTA form as the Trump administration rejected proposals to remove loopholes enabling a country to block the appointment of roster members. After winning control of the House in the 2018 mid-term elections, however, Democrats in Congress successfully conditioned passage of USMCA on rendering the state-to-state DSM functional, leading to the removal of the loopholes which had prevented the DSM from functioning for two decades.

Objective 6: Eliminate NAFTA Antidumping and Countervailing Duties DSM and Facilitate Agricultural Trade Remedies

Despite the Trump administration's efforts to eliminate the antidumping and countervailing duties (AD-CVD) dispute settlement mechanism (NAFTA chapter 19) (IUST 2017d), USMCA maintained it (USMCA chapter 10). The Trump administration also demanded more policy space to impose trade remedies on agricultural products. Mexican chief negotiator Smith Ramos recalled that the US demanded shortening the period analysed for trade remedy procedures from a year to the months during which 'US demand and Mexican exports are highest' (IUST 2020b). US proposals on this issue were also not included in the USMCA.

Canada maintained its historical stance by arguing that the preservation of the trade remedies DSM was a red line, leading the Trump administration to ultimately abandon this negotiating objective (IUST 2017m, 2018p). This is revealing of the importance of US-Canada economic integration given the bipartisan opposition to the trade remedies DSM in the US Congress. Although the Mexican government supported the Canadian position, it let the Canadians negotiate alone to focus on countering US demands to facilitate the imposition of trade remedies

on seasonal products. As a result, at the end of US-Mexico bilateral negotiations, the trade remedies DSM had been removed from their bilateral draft agreement. It was only once Canada achieved a deal with the US that the trade remedies DSM became part of the agreement (Mexican and Canadian negotiators, 16 October 2020, 19 and 20 April 2023). Meanwhile, the Mexican government had succeeded in resisting US proposals to facilitate the imposition of agricultural trade remedies. It received support from the US agricultural sector given that the proposal was 'supported by agricultural interests in Florida and to some degree Georgia but opposed by farmers and ranchers everywhere else' due to the risks of retaliation by Mexico (interview, John Murphy, US Chamber of Commerce, 19 February 2021; IUST 2018c, 2019a). This objective is not included in USMCA, despite the Trump administration's efforts until the last days of the negotiations (interview, Jesús Seade, 15 October 2020).

Objective 7: Eliminate the NAFTA Global Safeguard Exclusion

The Trump administration strove to eliminate the NAFTA global safeguard exclusion, which protects NAFTA members against safeguards imposed by another member if certain conditions are met (USTR, 2017b; interview, 25 September 2020). This change is also not included in USMCA as the Mexican government successfully rejected it in bilateral negotiations with the US, despite receiving little support from the US business community or Congress (IUST 2018h, 2018t). Canada supported Mexico's position but was less invested in the outcome given that USTR wanted to use safeguards to reduce imports of seasonal agricultural products from Mexico. Although a Mexican official in the Peña Nieto administration argued that Lighthizer knew he would not obtain these provisions (interview, 7 April 2021), the highly competitive nature of elections in Florida and Georgia incentivised the Trump administration to press Mexico for concessions until the very end of the negotiations (interview, Jesús Seade, 15 October 2020). The preservation of the safeguard exclusion was a major victory for Mexico

given that the US frequently imposes safeguards. Only a few months after the USMCA was signed, USTR Lighthizer demanded that the US International Trade Commission (ITC) conduct an expedited review to impose safeguards on imports of blueberries, which Mexico is a key exporter (Spak, de Rosenzweig, and Dilley 2020).

Objective 8: Dollar-for-Dollar Government Procurement Access

The Trump administration's negotiating objective for government procurement was to 'ensure reciprocity in market access opportunities for US goods, services, and suppliers in Canada and Mexico' (USTR, Nov 2017). Under this 'dollar-for-dollar' proposal, the US would cap access to its government procurement market to the level of the Mexican and Canadian procurement markets (IUST 2018t). Given the small size of the Mexican and Canadian procurement markets, this proposal amounted to removing Mexico and Canada's market access to most US procurement contracts. The US did not achieve this objective in its negotiations with Mexico, as USMCA maintains NAFTA government procurement regulations between the US and Mexico. Although Canada successfully resisted the US 'dollar for dollar' proposition, it did not obtain the maintenance of NAFTA provisions as the USMCA government procurement chapter does not cover US-Canada relations, which became regulated through the WTO Government Procurement Agreement (WTO GPA). Procurement between Canada and Mexico is regulated under the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP).

The objective of reducing Mexican access to the US government procurement market to the size of the Mexican procurement market was mocked by Mexican negotiators, who pointed to the fact that US firms had obtained more government procurement contracts in Mexico than vice-versa (interview with Mexican official, 7 April 2021). The US Chamber of Commerce described the proposal as a 'disaster' and lobbied for its abandonment, which eventually occurred (IUST 2018a). Certain career staff in USTR were also perplexed that this proposal

remained on the negotiating table for so long (interview, 25 January 2021; IUST 2018i). In this case, the Trump administration was less committed to imposing this objective on Mexico, given that the proposal targeted Canada. Although USTR Lighthizer pursued this objective in his negotiations with Mexican counterparts, he knew it was unlikely he would obtain it and sought to trade it for a concession elsewhere (interviews with US and Mexican officials, 25 January 2021 and 7 April 2021).

Objective 9: Increase Access to Canada's Dairy Market

The Trump administration's objectives also included 'eliminating remaining Canadian tariffs on imports of U.S. dairy, poultry, and egg products' and Canada's practices of 'cross-subsidization, price discrimination, and price undercutting' for dairy products (USTR 2017b: 3-4). Since the 1970s, Canada's supply management of these products entailed small quotas on imports, after which imports would face high tariffs, up to 315.5 per cent in the case of certain dairy products (Greene 2019). In 2017, the Canadian government also introduced a new classification for skimmed milk (Class 7) which led to a sharp decline in US exports of ultra-filtered milk to Canada (Dufour and Hurdle 2022). USMCA maintained Canada's supply side management but increased quotas for US exports of dairy, poultry and eggs.

The Trump administration's efforts to eliminate Canadian tariffs on dairy, poultry and eggs as well as eliminate Canada's discriminatory policies were met with bipartisan support in the US Congress and were pushed by the US agricultural sector (IUST 2018m). The Canadian government refused to concede on this objective until the very last days of the negotiations. Once a US-Mexico bilateral agreement was reached in September 2018, however, the risk of being left out led the Canadian government to agree to higher quotas for dairy, poultry and eggs. Although a concession, this is far from the US government's initial proposal. In the dairy sector, which was the most politically sensitive, only an estimated 3.6 per cent of Canada's market is

liberalised (Lobosco 2018). This reflects concessions made by Canada in its recent PTAs, CETA and CPTPP, where it provided access to 1.4 and 3.1 per cent of its market, respectively (Dufour and Hurdle 2022). A Canadian negotiator interviewed expressed confidence that the language they included would protect their dairy industry, which proved accurate in November 2023 as the US lost a state-to-state dispute over the allocation of Canada's dairy quotas (interview, 11 August 2023; Brookings 2023b).

Objective 10: Eliminate NAFTA's Cultural Exemption Provision

According to Mexican chief negotiator Jesús Seade, USTR Lighthizer had a 'resolute plan' to eliminate the NAFTA cultural exemption, which enabled Canada to protect its cultural industry from US and Mexican competition (IUST 2018l; 2018p). This had always been the US negotiating position since the exception was first granted in the Canada-US Free Trade Agreement (CUSFTA). Just as in CUSFTA and NAFTA, maintaining the cultural exemption was a red line for the Canadian government. Canada implements quotas and local content requirements to ensure the production and diffusion of Canadian books, music, films, radio and television programmes, among others. This provision was politically sensitive in Canada given the fear that Canadian culture would be dominated by imported American cultural productions, and the need to maintain a harmony between French and English cultures.

Canada succeeded in maintaining the cultural exemption in USMCA. As a result, the Mexican government demanded its own cultural exemption, albeit a more limited one given its concern for protecting Mexican cultural exports, notably of its film, television and music industries. Mexico obtained a limited carveout to promote cultural diversity, such as work in indigenous languages (Ibid.). As a whole, however, the scope of Mexico's cultural exemptions has narrowed (Gagné 2022: 257). USMCA Article 32.6.4 preserves the retaliatory clause in NAFTA, which enables Mexico and the US to retaliate in response to Canadian cultural

exemptions. This clause led the Canadian government to exercise restraint during the NAFTA period, although the US never retaliated against Canada's cultural exemptions (Ibid.: 248).

5.5. Was the Trump Administration Bluffing?

The Trump administration may have demanded the radical negotiating objectives discussed above to obtain more modest concessions, in which case the non-inclusion or weakening of the ten objectives should not be considered a thwarted negotiating agenda but a successful 'bluff'. During negotiations, countries sometimes 'open with high demands' or include demands of little interest in the hope that they can exchange them for real, more modest objectives (Jones 2013: 84-88; Ortiz Mena 2006). Beyond the analysis above, which demonstrated that the Trump administration was committed to its negotiating objectives, it is worth analysing the Trump administration's strategy from a holistic viewpoint given that negotiators often prioritise some objectives over others. This section draws on interview evidence from US, Mexican, and Canadian negotiators.

While Trump was unfamiliar with the details of trade policy (Woodward 2018), he was committed to certain negotiating objectives and appointed trade negotiators who had the skills to obtain them. Trump was not alone in proposing radical change but supported by members of his government, including USTR Lighthizer and economic adviser Peter Navarro. According to Mexican chief negotiator Smith Ramos, Trump was not bluffing:

> A lot of people throughout the negotiation and even today, they asked me, well, you know, he (Trump) must have been bluffing, right? Because the cost of the US pulling out of NAFTA would have been huge, not just because of their relationship with Mexico, but also the relationship with Canada. And what we have seen so far, I think it's proven true, what I kept saying, what I'm still saying today, is that Trump doesn't bluff (interview, 16 October 2020).

Juan Carlos Baker, chief of staff to the Mexican Minister of Economy and Undersecretary of Foreign Trade, also stressed that the Trump administration was not bluffing: 'Mexico took the US position very seriously, we did not believe it was a bluff, we did not believe it was a lie' (interview, 10 December 2020, translated from Spanish).

Canadian negotiators interviewed diverge on whether Trump and his administration were bluffing. According to one Canadian negotiator:

> They (US negotiators) might have been trying to, in classical negotiating terms, anchor us on certain concepts: "Here's this horrible idea, Oh, here's another idea that's less horrible, so you must like it?" That might work if this was the first time we'd ever been in a negotiation, but it wasn't. I think they're more sophisticated than that. I don't think that's what they were really doing (interview, 5 March 2021).

By contrast, another Canadian negotiator interviewed gives more weight to the interpretation that Trump was bluffing:

> Some of them (US negotiating objectives) were just so audacious or ridiculous to begin with that we looked at them more as strategies to create a headline, to create a little bit of shock and awe around what the US was trying to do, and less so as something that they were really thinking was a reasonable outcome. Perhaps it was what they viewed as the first step on the path towards the outcome that they wanted to get at. But I would say that, at least my perspective, from the beginning, the US probably realized that they would never succeed in getting a US-specific content requirement in rules of origin for autos (interview, 5 March 2021).

Interviews with Trump administration officials lend more credence to the interpretation that Trump was not bluffing than to the interpretation above. Indeed, Canadian negotiators' dismissal of US negotiating objectives as bluff and unrealistic led to growing frustration from the Trump administration, eventually leading it to favour a deal with Mexico excluding Canada. According to a Trump administration official:

> The Mexicans, very politically savvy, very pragmatic. The Canadians were really difficult to deal with. Their view from the beginning, their strategy was: "We're gonna go to governors and Congress to say we shouldn't renegotiate this." And so they just

> never did any good-faith negotiations. It wasn't until the Mexicans came through with a deal, and then Canadians were left out in the cold, that they realized that we were moving forward and that we weren't messing around (interview, 10 March 2021).

This view was shared by many US negotiators interviewed, as illustrated by the quote at the beginning of his chapter. Jared Kushner, Trump's advisor and son-in-law, also argued in his memoirs that Trump was committed to withdrawing from NAFTA.

> Negotiating a trade deal is like a game of chicken, with real consequences. The other side has to believe you are going to jump off a cliff. We succeeded because Trump was absolutely prepared to terminate NAFTA – and Mexico and Canada knew it (Kushner 2022: 197).

Kushner played a key role in ensuring that Canada was included in the final trade agreement, advising PM Trudeau that Canadian negotiators needed to make concessions or Trump would proceed with a bilateral deal with Mexico (Kushner 2022: 193-200).

Although Trump administration officials were initially committed to their radical negotiating objectives, they had to change strategy once they realised certain objectives could not be met. Interview respondents stressed the importance of distinguishing US negotiators' position at the beginning of the negotiations and later on. USTR Lighthizer significantly moderated his stance as the negotiations progressed due to his conversations with members of Congress, the US business sector, negotiating counterparts, and other stakeholders. A Trump administration official recalled:

> Early on, both of them (Lighthizer and Navarro) were fairly hawkish. But I think Navarro certainly was more hawkish than Lighthizer. And I'd also say that as his tenure wore on Lighthizer softened pretty significantly. He was nowhere near as hard line in 2020 as he was in 2017 (interview, 25 January 2021).

Despite this evolution, the Trump administration continued to pressure Mexico and Canada to accept some of its radical negotiating objectives until the end of the negotiations. Lighthizer

demanded limits on Mexican agricultural imports during negotiations with the Peña Nieto government, but also until the last days of negotiations over the amendments to USMCA (Jesús Seade, interview 15 October 2020). Referring to the dollar-for-dollar government procurement objective, Trump administration officials interviewed also believed it was a fair demand. For instance:

> I still think the (US) position on government procurement was a very realistic and very strong proposal that made a lot of sense. Why should we give Canadians, say, more access to our market than we have to their market? And they would say, "Well, your market is a lot bigger than ours". And we would say, "We should be able to make as many sales in Canada as you can make here". And I don't see that as a poison pill or trap or anything. You look right now, President Biden's out all the time talking about Buy America and saying "If the American taxpayer spends money, those jobs should go to Americans, that stuff should be made here in the United States" (interview, 7 May 2021).

Although some objectives were more prioritised than others, such as US-specific auto rules of origin and eliminating all dispute settlement mechanisms, even those were not met in the negotiations (Lighthizer 2023; Smith Ramos, interview, 16 October 2020). It is hard to argue that Trump himself wanted the modest changes found in USMCA. US chief negotiator John Melle recalled that 'Trump came in with one of his longest public policy views: that the NAFTA was a terrible agreement and that tariffs were good' (interview, 16 December 2020). Trump's rhetoric on the campaign trail and actions during the first months of his presidency indicated that he was committed to achieving those radical negotiating objectives. In the first few months, the US Congress and businesses had not yet organised to persuade him not to withdraw from NAFTA. During this period, Trump's chief economic adviser Gary Cohn and White House staff secretary Rob Porter played a key role by removing from Trump's desk executive orders to withdraw the US from NAFTA that he had requested (Woodward 2018: 233).

5.6. Conclusion

The Trump administration demanded radical changes to NAFTA during the renegotiation and threatened to withdraw the US from NAFTA by executive decree if Mexico and Canada did not concede. Of the ten US objectives considered unacceptable by Mexican and Canadian negotiators, half are not included in USMCA and the remaining half are severely weakened. Despite this thwarted negotiating agenda, President Trump did not act on his threat to withdraw the US unilaterally from NAFTA and signed USMCA. His policy target was to reduce the US trade deficit with Mexico, which he aimed to achieve through the increased uncertainty caused by the NAFTA renegotiation and the new provisions in USMCA. Between 2017 and 2022, however, the US trade deficit in goods and services with Mexico nearly doubled from 71.1 billion US dollars to 131.1 billion (US Bureau of Economic Analysis 2023; USTR 2023b).

Drawing on this analysis, the next chapter examines the reasons for the thwarted negotiating agenda of the Trump administration. Given that the Trump administration was not 'bluffing' but committed to its negotiating objectives, it identifies a power paradox: the US could not leverage its large power asymmetry with Mexico and Canada to impose its negotiating objectives. The chapter applies the theoretical framework developed in Chapter One to analyse how 25 years of NAFTA shaped the preferences and power of actors during the renegotiation process.

Chapter 6. Power and Path Dependence

> *All of those 'poison pills' (a term used by the US business sector to label certain US negotiating objectives) were perhaps not only poisonous to Mexico or to Canada but to important sectors in the US economy. It is important to look at how the evolution of those issues occurred both within the domestic context and within the negotiations themselves as well. The five-year sunset clause, there was a lot of opposition in the US to that, in the business community as well. The concern there was the uncertainty that that creates […] There was a large segment in all three countries that did not want the agreement to expire or to be renegotiated. We even had Democratic members of the House who had voted against the agreement saying they hated the NAFTA but "You can't terminate it".*
>
> John Melle, US chief negotiator, interview, 16 December 2020

6.1. Introduction

Negotiations in the early 1990s over the North American Free Trade Agreement (NAFTA) were characterised by power asymmetry between the US and Mexico (less so with Canada, which had already signed a PTA with the US, CUSFTA, in 1989). At the time, the US economy was more than ten times the size of Mexico's and had three times higher labour productivity (Blecker 2019). Between 1994 and 2016, asymmetries between the United States and Mexico due to differences in market size and productivity increased (Ibid.: 160; Figure 7). Furthermore, beyond economic divergence, the power asymmetry was magnified by the sharp increase in Mexico's dependence on trade with the US (Figure 8). The acute power asymmetry between Mexico and the US became apparent following Trump's election as he verbally abused Mexicans and threatened to withdraw the US from NAFTA unless Mexico agreed to unilateral

concessions, by contrast to the Mexican government's strategy of not responding to his comments to avoid further confrontation.

Despite the large US-Mexico power asymmetry, the Trump administration failed to impose its initial negotiating objectives, which raises a power paradox. The previous chapter demonstrated that the Trump administration did not impose any of its ten negotiating objectives in their original form despite its commitment to do so. While US business groups and Republicans in Congress had always been in favour of NAFTA, US labour unions and Congressional Democrats' opposition to a US withdrawal from or significant alteration of NAFTA contrasted with their position in the 1990s. Drawing on this puzzle, this chapter analyses the reasons for continuity over change between NAFTA and USMCA.

Path dependence is the main explanation for the power paradox: *economic integration under NAFTA and the nature of the US political system* raised disruption costs. First, 25 years of North American economic integration undermined the US government's ability to make radical changes to NAFTA as export interests rose to defend the status quo. Second, three characteristics of the US political system increased disruption costs: Congress' constitutional authority over trade policy, the competitiveness of Congressional seats (in swing states and districts), and business lobbies' influence on political representatives. The concluding chapter evaluates the generalisability of this finding to other trade renegotiations, as well as provides policy reflections.

6.2. The Power Paradox

Dahl's (1957: 202-3) classic definition of power, 'A has power over B to the extent that he can get B to do something that B would not otherwise do' provides an intuitive framework to

analyse the power paradox: the Trump administration did not succeed in getting the Mexican and Canadian governments to accept its radical negotiating objectives. This definition of power, however, is to some degree tautological ('get' refers to ability or power) and unable to distinguish between an actor that prevails without effort and one that prevails 'by a hair with tremendous effort' (Rubin and Zartman 2000: 7-10). Following Habeeb's (1988: 15) definition, power is defined as 'the way in which actor A uses its *resources* in a process with actor B so as to bring about changes that cause *preferred outcomes*'.

A power paradox contrasts an actor's *actual* power (obtention of preferred outcomes) with its *potential* to influence an outcome (use of its resources or capabilities) (Knorr 1975). Knorr (1975: 9) refers to the first as 'actualised power' and to the second as 'putative power'. In their analysis of relations of dependence (understood as asymmetric interdependence) between countries, Keohane and Nye (1989: 11) focus on putative power. A less dependent actor has more putative power because it can use its resources to inflict a greater cost on the other actor. The conversion of putative power into actualised power, however, is not automatic but depends on a variety of factors. A power paradox can occur when a large gap exists between an actor's putative and actualised power. This is precisely what occurred during the renegotiation of NAFTA: the US had greater putative power over Mexico and Canada, yet the Trump administration had limited success in transforming it into actualised power. The rest of this section demonstrates the power paradox by showing the large asymmetry in putative power between the US and Mexico/Canada during the renegotiation, which arguably increased since NAFTA.

NAFTA was negotiated in the context of important power asymmetries between the US, Mexico and Canada. Differences in market size 'meant that a negotiator for the United States could say to counterparts in Mexico and Canada: "You want access to our $7 trillion market, and you offer in exchange access to your $250 and $500 billion markets? You are going to have

to pay for that access, and here is what it is going to cost you…" (Cameron and Tomlin, 2000: 15). Although Canada also faced power asymmetries during the NAFTA negotiation, it benefited from having already signed a PTA with the US in 1989 (CUSFTA). By contrast, Mexico lacked this alternative and also suffered from asymmetries in productivity: Mexican output per worker in 1993 was approximately 40 per cent of US output per worker (Blecker, 2019: 160).

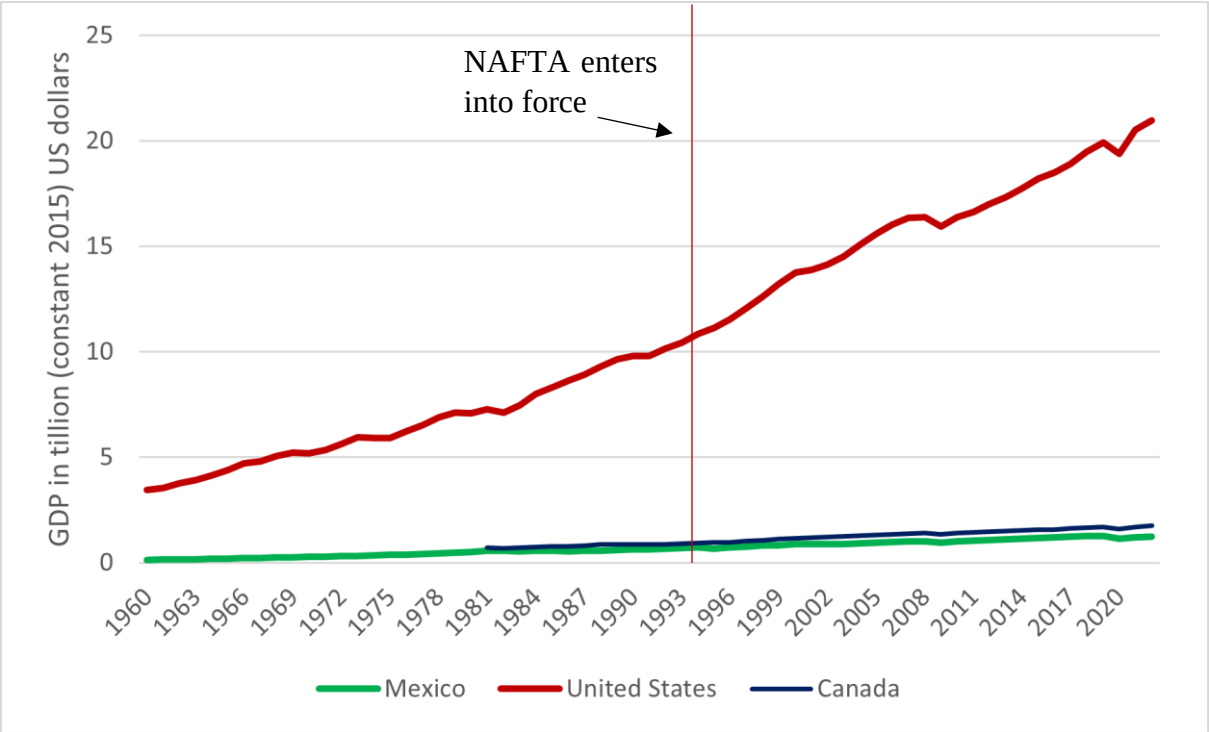
In addition to asymmetries in market size (and productivity in the case of Mexico), Mexico and Canada also suffered from asymmetric economic interdependence with the US, which occurs when one country is more economically dependent on the other than vice-versa (Hirschman, 1945; Keohane and Nye, 1977). In 1993, Mexico and Canada sent 83 and 81 per cent of their total exports to the US, respectively, whereas only 9 per cent of US exports were sent to Mexico and 22 per cent to Canada (WITS 2023). Asymmetric economic interdependence is a source of power for the less dependent country and vulnerability for the most dependent country (Hirschman 1945; Knorr and Trager 1977). Drawing on Keohane and Nye's (1977: 12) distinction between sensitivity and vulnerability interdependence, Mexico and Canada's dependence on the US was not only a problem of sensitivity (high share of total exports sent to the US) but also of vulnerability (no clear alternative export market). This is due to 'all countries being ready to sell and none ready to buy' (Hirschman, 1945: 32).

Although many proponents of NAFTA argued that the agreement would promote economic convergence between the United States and Mexico and thereby reduce the power asymmetries between the two countries, the opposite happened (Blecker, 2019; Hufbauer and Schott, 1992: 58-62; Mayer 1998; cf. Chapter Two). Mexican labour productivity (output per worker) as a percentage of US labour productivity decreased from 40 per cent in 1993 to 33 per cent in 2014, while real wages of Mexican production workers were lower in 2016 than in 1994 (Blecker, 2019: 160-1). Between 1994 and 2017, US GDP per capita at purchasing power parity (PPP)

increased from 4.5 to 6.5 times Mexico's GDP per capita PPP (from $27694 to $59907 for the US, from $5976 to $9434 for Mexico).

Market size is the most important bargaining chip in trade negotiations. Figure 7 shows the divergence in economic size between Mexico, Canada and the US since the signing of NAFTA, measured in terms of GDP in constant 2015 US dollars (the dollar being the currency predominantly used in international transactions). Divergence in economic size between the US and its neighbours is natural given that the US had a population of 332 million in 2021, compared to 126 million in Mexico (2.5 times) and 38 million in Canada (9 times). The economic divergence between the US and Mexico was exacerbated by the depreciation of the Mexican peso: between 1994 and 2019, the value of the US dollar increased sixfold from 3 to 19 pesos (World Bank 2021a). The peso's depreciation is a constituent part of the asymmetric relation between the US and Mexico given that the dollar is used in their transactions.

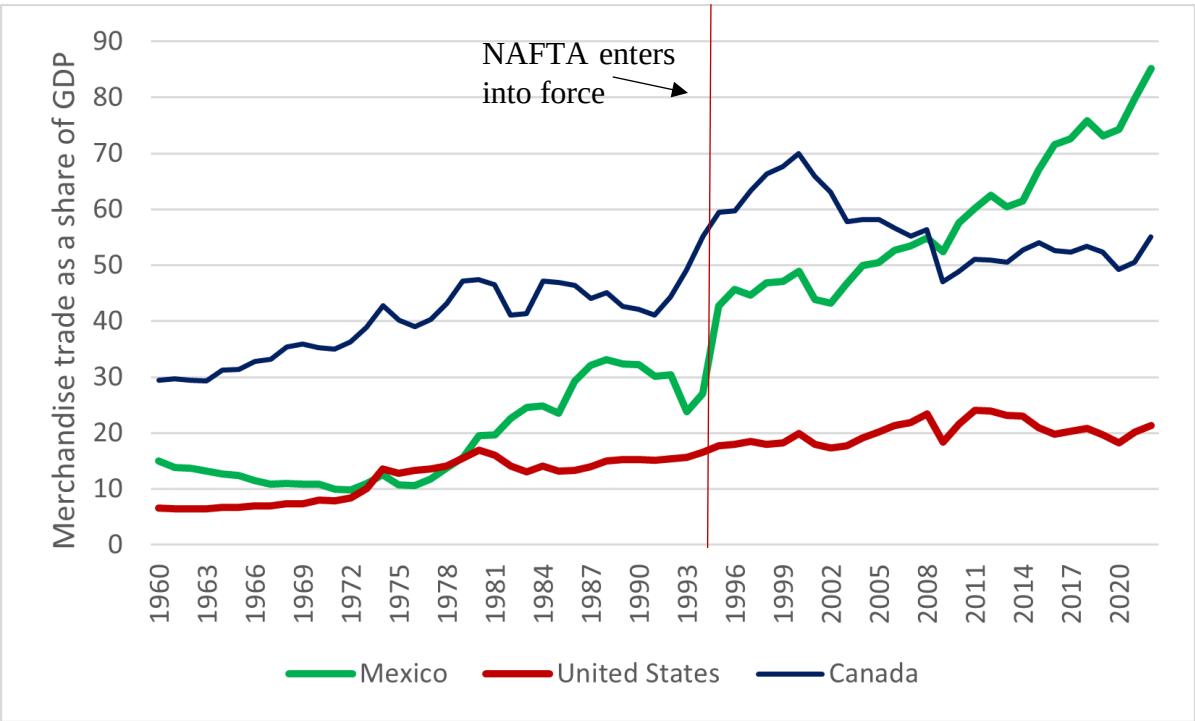
FIGURE 7: MEXICAN, CANADIAN AND US GDP IN CONSTANT 2015 US DOLLARS (1960-2022)



Source: Author's own, based on data from World Bank (2023).

Beyond economic divergence, the power asymmetry between the US and Mexico was magnified by the much higher increase in Mexico's dependence on trade with the US than vice versa. Between 1993 and 2019, the share of merchandise trade in Mexican GDP increased from 28 to 78 per cent (Figure 8). By contrast, the share of merchandise trade in the US GDP only increased from 20 to 26 per cent during the same period (and in Canada from 49 to 52 per cent). Although this metric overstates dependence on trade given that it double counts exports and imports of intermediate goods (the metric does not capture value-added), it is a good proxy of the sharp increase in Mexico's dependence on trade. The US remained Mexico and Canada's foremost trading partner during NAFTA, purchasing 78 per cent and 75 per cent of their exports in 2019, respectively, while US exports to Canada decreased from 22 to 18 per cent since 1993 and US exports to Mexico increased from 9 to 16 per cent (WITS 2023).

FIGURE 8. TRADE IN GOODS AS A SHARE OF MEXICAN, CANADIAN AND US GDP (1970-2022)



Source: Author's own, based on data from World Bank (2023).

In sum, US power asymmetry with Mexico and Canada increased between 1993 and 2019 in terms of market size. In the case of Mexico, power asymmetry with the US also increased due

to its lower rate of productivity growth and a large increase in dependence on trade. Although Mexico faced a more stable macroeconomic outlook in 2017 than in the 1990s given its prudent fiscal and monetary policies since the 1995 financial crisis, its negotiating position was not considerably improved given the macroeconomic instability which would have resulted from a US withdrawal from NAFTA. Given the power asymmetry with its negotiating counterparts, in particular Mexico, the Trump administration's failure to impose its negotiating objectives during the NAFTA renegotiation raises a power paradox.

6.3. Theories of Power Paradoxes

Power asymmetry is a relational approach: Mexico is not considered 'small' or 'weak' in itself but rather when contrasted with the US (Long 2022; Ojeda 1976; Womack 2016). Aside from its relation with its northern neighbour, the Mexican economy is not 'small' but represents the fourteenth highest GDP in the world in 2022, ahead of Spain and Indonesia and behind South Korea. With a population of 126 million in 2021, Mexico is far from the World Bank's 1.5 million people threshold for a 'small state', which explains why it does not endure many of the constraints typically faced by small states in international trade negotiations, such as weak negotiating capacity and the lack of communication with civil society and the private sector (Jones, Deere-Birkbeck, and Woods 2010).

On the contrary, as discussed in more detail below, the Mexican government entered the NAFTA renegotiation with a highly skilled negotiating team which was strengthened by the experience of negotiating Mexico's numerous PTAs since NAFTA. Mexican negotiators also benefited from close coordination with the private sector and civil society thanks to the 'Cuarto de Junto' and 'Cuarto de Inteligencia' which regrouped business interests and civil society actors, respectively.

Many theories have been developed to explain power paradoxes in international relations (Habeeb 1988; Rubin and Zartman 2000). Some focus on the international system, such as the weak state entering a coalition with other states to defend its interests against the strong state (Krasner 1985, 1990; Bilal, Tussie, and de Lombaerde 2013) or its greater commitment to the negotiating outcome (Keohane and Nye 1977). Some theories of power paradoxes focus on domestic politics, such as the weak state finding allies in the strong state or benefiting from time constraints in the strong state (Ibid.; Jones 2013: 63-64; Cameron and Tomlin 2000; Manger 2009; Bilal, Tussie, and de Lombaerde 2013; Odell 2000). Some theories emphasise the role of ideas, such as how persuasion and poverty narratives can be successfully used by negotiators in weaker countries to obtain concessions during negotiations (Corbett, Xu, and Weller 2022; Narlikar 2020; Panke 2010). Table 7 outlines six explanations that were raised by interviewees and academics to explain the power paradox in the NAFTA renegotiation, drawing on international, domestic, and ideational level explanations.[10] The rest of the section argues that, of the six, three are plausible explanations for the power paradox.

[10] This classification simplifies reality. Some schools, such as constructivist International Relations scholars, focus on ideas in the international system. For clarity, only a few key academic sources are cited for each theory.

TABLE 6. EXPLANATIONS OF POWER PARADOXES IN INTERNATIONAL TRADE NEGOTIATIONS

Theory	Evidence in the NAFTA renegotiation
International level	
A. **Intergovernmental coalition** between weak states to resist the strong state's demands (Krasner 1985; Bilal et al. 2013).	Mexico and Canada cooperated to some extent during the negotiations against certain US demands.
B. **Weak state's greater commitment**, leading it to negotiate more arduously (Keohane and Nye 1977/2012: 16).	The Mexican and Canadian governments defined 'red lines' that they were committed to defending (Bahri and Lugo 2020; Gagné and Rioux 2022).
Domestic level	
C. **Transnational alliance** between the weak state and organisations in the strong state (Keohane and Nye 1977; Odell 2000; Jones 2013: 63-64; Bilal et al. 2013), some of which can be veto players.	The US Congress challenged a withdrawal from NAFTA by presidential decree (Janusch 2018). US bureaucracy, business and labour unions developed ties with Mexican counterparts (Aspinwall 2009; Macdonald 2023; Nolan García 2011)
D. **Time constraints faced by the strong state and not the weak state** (Cameron and Tomlin 2000; Manger 2009).	President Trump wanted a trade agreement fast (Anderson 2020: 159), **but** so did President Peña Nieto.
Ideational level	
E. Adherence to **norms that benefit the weak state** by leaders in the strong state, such as the non-removable nature of trade agreements or promoting development (Narlikar 2020; Corbett et al. 2022).	The Mexican government obtained US support for the implementation of its labour reform (Bensusán and Middlebrook 2020), **but** President Trump reappropriated the poverty narrative to stress NAFTA's adjustment costs in the US.
F. **Excess of confidence by the strong state** leading to mistakes, such as investing too few resources or appointing incompetent negotiators.	Trump was confident he would 'win' and incompetent on details of trade policy (Woodward 2018), **but** surrounded by skilled advisors and negotiators.

Source: Author's own.

Shortly before President Salinas decided to negotiate a PTA with the US, neorealist scholar Krasner (1985, 1990) contended that trade agreements between unequal trading partners were unlikely. Power asymmetries would undermine cooperation as weak states attempt to reduce their vulnerability from strong states by forming coalitions, while strong states strive to maintain existing power asymmetries. Krasner considered the Mexico-US relation to epitomise such power asymmetries, pointing as evidence to Mexico's historic rejection of the General Agreement on Tariffs and Trade (GATT) and adherence to non-alignment (Krasner 1985: 55). Mexico entered the GATT in 1986, however, which weakened this argument. Nevertheless,

Krasner (1990: 45-50) argued that a bilateral trade agreement between the US and Mexico remained unlikely, in part because weaker states prefer multilateralism to conduct trade negotiations to reduce power asymmetries by forming coalitions. In addition, Krasner contended that power asymmetries would undermine cooperation because the strong state would prefer to act unilaterally, while the weak state would be worried that its vulnerability would lead to an unfavourable implementation of the trade agreement in practice (Ibid.). Thirty years later, Trump's unilateral decision to renegotiate NAFTA and Mexico's increased dependence on the US economy vindicated Krasner's concerns. His analysis does not explain, however, why Mexico signed NAFTA nor why the Trump administration failed to force Mexico and Canada into adopting many of its negotiating objectives despite the US power asymmetry with its neighbours. The rest of this section assesses the relevance of the theories of power paradoxes A-F in the NAFTA renegotiation.

Despite Krasner's failure to predict NAFTA, his insight that a weak state can mitigate asymmetric relations with a strong state by cooperating with other states could explain some outcomes of the NAFTA renegotiation (theory A). Admittedly, NAFTA is not the ideal application for this theory given that it would predict weak states to form alliances during multilateral negotiations at the WTO rather than to engage in bilateral talks with a strong state (Bilal, Tussie, and de Lombaerde 2013). In the context of NAFTA, however, the trilateral nature of the agreement rendered cooperation possible, albeit limited by quantity (Canada and Mexico could only cooperate with each other) and quality (the two countries had different levels of development and thus different economic interests).

Following the signing of NAFTA in 1992, scholars turned to the neoliberal school of international relations to explain the formation of reciprocal trade agreements between unequal trading partners. Keohane and Nye (1977) and Keohane (1990) argued that both strong and weak states have motives to cooperate. Strong states may need to cooperate with weak states to

increase their control, such as the US with Mexico to promote peace and stability in its southern border (Ibid.: 69-70). Weak states are often more concerned over the negotiating outcome than large ones, which can lead them to commit more resources and negotiate more arduously, such as Canada in its relationship with the US (Keohane and Nye 1977; Bacharacb and Lawler 1986: 172-3). Theory B (weak state's greater commitment) is a plausible explanation of the power paradox as Mexican and Canadian negotiators identified 'red lines' they were unwilling to compromise on (Bahri and Lugo 2020: 5).

The theories outlined above mostly fail to integrate the role of domestic politics in determining the formation of trade agreements and the bargaining power of each negotiating country (Keohane and Nye 1987: 753). Powerful states are often more internally divided than smaller states, which can undermine power asymmetries as smaller states form alliances with domestic interest groups in the large country (Ibid.; Odell 2000; Bilal, Tussie, and de Lombaerde 2013; Jones 2013: 63-64). This explanation was less applicable to Mexico during the original negotiation given that it was also domestically divided over NAFTA (Cameron and Tomlin 2000). During the NAFTA renegotiation, however, there was widespread support in Mexico for keeping NAFTA. By contrast, the US was internally divided, with the Trump administration demanding radical change but opposed by Republicans in Congress and the business sector.

Time constraints faced by the strong state but not the weak state can mitigate power asymmetries (Manger 2009; Cameron and Tomlin 2000). During the original NAFTA negotiations, time constraints faced by the Mexican government accentuated power asymmetries with the US. Mexico's fragile economic situation in 1990 rendered the Mexican government impatient to conclude a trade agreement with the US in the hope that NAFTA would stabilise the economy and attract foreign investment (Cameron and Tomlin 2000). By contrast, the US and Canadian governments were more patient (except for the last months of the negotiations in the case of the US due to President Bush Sr.'s re-election campaign), which

allowed them to press for further concessions (Ibid.). Anderson (2020: 159) argues that the time constraints self-imposed by Trump prevented him from obtaining more significant concessions during the NAFTA renegotiation. Trump wanted a renegotiated deal before the November 2018 US midterm elections. Mexican negotiators were also under time constraints, however, given that they sought to regain market access uncertainty fast and feared that the newly elected President López Obrador would undermine the agreement. It is no coincidence that USMCA was signed on 30 November 2018, the day before López Obrador took office. More importantly, timing does not explain why Trump decided not to withdraw the US from NAFTA, which would have increased the pressure on Mexico and Canada to make concessions rapidly (theory D is implausible).

Ideas can also explain power paradoxes in trade negotiations. Corbett, Xu, and Weller (2022) and Narlikar (2020), for instance, stress how poverty narratives have been successfully used by countries in the global South to obtain concessions in the UN and the WTO, such as a greater voice in negotiation processes, the inclusion of development in trade negotiation objectives, and special and differential status to promote development policies. The US implementation bill for USMCA contains financial support for Mexico's labour reform which could fit into this category. However, the funding resulted from demands from the Democratic Party rather than the Trump administration, which preferred using unilateral sanctions to enforce USMCA labour provisions. Furthermore, Trump's approach to international trade reappropriated the poverty narrative by blaming trade with Mexico for declining wages and job losses in the US (Narlikar 2020: 150). Mexican negotiators during the NAFTA renegotiation could not appeal to the poverty narrative to obtain concessions from the US but rather were asked by US negotiators to make concessions to alleviate economic distress in the US (theory E is implausible).

A power paradox can also be explained by an excess of confidence from the powerful country, leading it to make mistakes such as investing too few resources in the negotiation and

appointing incompetent negotiators. The outcome of the NAFTA renegotiation could be explained by Trump's lack of expertise on trade policy and overconfidence (Woodward 2018), as well as the widely documented chaos in the Trump White House (Ibid.; Wolff 2018). Aside from Trump's threats of withdrawal, however, the negotiations over NAFTA were delegated to a team of experienced negotiators at the Office of the United States Trade Representative (USTR), most notably Robert Lighthizer and career professional John Melle, who were praised for their skill and leadership by both Republicans and Democrats. Both received the support of hundreds of professionals at USTR and inputs from different US government agencies, which renders implausible that the US failed to meet its negotiating objectives due to incompetence (theory F).

The plausible explanations for the power paradox during the NAFTA renegotiation are: an intergovernmental coalition between weak states to resist the strong state's demands (theory A), the weak state's greater commitment to the negotiating outcome (theory B), and a transnational alliance between the weak state and organisations in the strong state (theory C). The next section analyses the relevance of those three explanations.

6.4. Explaining the Power Paradox

6.4.1. Overview

Table 6 summarises the reasons for the non-inclusion or weakening of the Trump administration's ten negotiating objectives based on the negotiation process detailed in Chapter Five. A transnational alliance between Mexico, Canada and actors within the US (theory C) is at least partly responsible for the abandonment or weakening of six of the ten US negotiating objectives, which were considered unacceptable not only by the Mexican and Canadian governments but also by large parts of the US business sector and Congress. Mexico-Canada

cooperation (theory A) helped undermine five of the ten US negotiating objectives, while greater commitment from Mexico or Canada alone (theory B) accounts for the weakening or abandonment of three US negotiating objectives.

TABLE 7. REASONS FOR THE NON-INCLUSION OR WEAKENING OF US NEGOTIATING OBJECTIVES

Trump administration objectives	Transnational alliance	Intergovernmental coalition (Mex-Can)	Greater Mex/Can commitment
Dollar-for-dollar govt procurement	**X***		
Eliminate State-State DSM	**X**		
Eliminate Investor-State DSM	**X**		
50% US-specific auto rules of origin	**X**	**X**	
(Five-year) sunset clause	**X**	**X**	
Voluntary export restraints	**X****	**X**	
Facilitate trade remedies	**X**	**X**	
Facilitate the use of safeguards		**X**	**X (Mexico)**
Eliminate Canada's cultural exemption			**X (Canada)**
Open Canada's dairy market			**X (Canada)**
Total	**7**	**5**	**3**

*This objective was primarily targeting Canada. The Mexican government obtained the support of US business groups to eventually remove that objective in bilateral negotiations.
**US firms were opposed but did not need to lobby as this proposal was quickly abandoned due to joint opposition by Mexico and Canada.

Although contributing to the explanation of the power paradox in half of the ten cases, Mexico-Canada cooperation (theory A) should not be overstated given that it was informal, often unintentional, and broke down when national interests diverged. When the Canadian and Mexican governments had diverging interests, they did not hesitate to cooperate with the US instead. Canada sided with the US over a high-wage content for auto rules of origin (cf. section 5.4.2.), while Mexico agreed to a bilateral agreement with the US in August 2018 forcing the

Canadian government to make last-minute concessions. The following quote from a Canadian negotiator reflects the views of other US and Mexican negotiators interviewed:

> I think it is rare to agree on a particular strategy in terms of you do this and I'll do that. It's more about where your priorities lie. At the end of the day, one of the things that I've learned, I won't say I learned strictly in this negotiation: the process is always a very strong reminder that while you may share a lot of interests with another negotiating partner, at the end of the day, when push comes to shove, each country looks out for its own national interest (interview, 5 March 2021).

Similarly, US chief negotiator John Melle recalled that they implemented a successful divide-and-conquer strategy in the negotiations:

> Throughout the negotiations, they (Mexico and Canada) were each trying to determine where they could be allies and work more effectively together to advance a common position with the United States. But also what happened is we divided them and we did a deal with Mexico first and then Canada had to come in on a very short notice and get what it could. […] Mexico had to decide how to play, with or against Canada, in this whole procedure. As always what happens is they stay allies up to a certain point and then one of them throws the other under the bus (interview, 16 December 2020).

Some of the achievements classified as Mexico-Canada cooperation in the analysis were unintentional given that the US chose to negotiate bilaterally with Mexico and Canada during most of 2018. For instance, Canada successfully resisted the elimination of the AD-CVD DSM alone in last-minute bilateral negotiations with the US, given that the Mexican government had agreed to forego this mechanism in its bilateral negotiations in the hope that Canada would rescue it (cf. section 5.4.5.). Similarly, Mexico successfully resisted alone the inclusion of agricultural trade remedies and the elimination of the safeguard exemption (although Canada voiced its support). Mexico-Canada cooperation was weak, limited to areas where they shared common interests, and often unplanned.

Similarly, the greater commitment of Mexican and Canadian negotiators (theory B) should not be overstated given that it relied to be successful on a transnational alliance with domestic actors

in the US (theory C). Mexican and Canadian negotiators informed or pressured domestic US interests in Congress and the business sector to be effective. Since the original NAFTA negotiations, Mexican negotiators had created a 'Cuarto de Junto', literally 'room next door', to help negotiators communicate with the business sector. In addition to shaping the Mexican government's negotiating position, this Cuarto de Junto was used to inform businesses of the proposals tabled by the US government, including US businesses which struggled to access the Trump administration:

> We have the mirror of that structure (negotiating team structure) within the private sector. For each chapter, for each lead, you will have another lead in the private sector that will be your contact point and your channel of communication. That I think is very, very important, because not only information goes very quickly, but it is something that is very effective in terms of having answers and having information (Mexican negotiator, interview, 9 October 2020).

In addition to the 'Cuarto de Junto', Mexican negotiators benefited from the 'Cuarto de Inteligencia' or 'intelligence room' composed of experts in different aspects of trade negotiations. Those were often academics and legal experts who advised the government on drafts of the text and negotiating priorities. This unit produced research which was sent to US lobby groups and political representatives to demonstrate the costs of undermining NAFTA:

> The 'Cuarto de Inteligencia', the intelligence and research unit, looked at all the data and drafted very convincing, persuasive reports with numbers to show US constituencies, US governors, saying "Look, this is what your state is going to lose if Trump manages to go back on NAFTA in USMCA negotiations". So it was more sophisticated than lobbying I think because it was massively backed by organized research and investigation (Mexican academic, interview, 9 October 2020).

Together, the 'Cuarto de Junto' and 'Cuarto de Inteligencia' helped Mexican negotiators inform actors in the US of the importance of preserving US-Mexico economic integration. In addition to engaging with business groups, Mexican negotiators also talked to other actors, including 'political actors, congressmen, organizations, the Latino community, everybody that is an ally

for Mexico', thereby increasing the avenues to influence the Trump administration (Mexican negotiator, interview, 9 October 2020). Canadian negotiators also used this strategy, albeit to the point that US negotiators became irritated by this tactic (cf. section 5.5).

Drawing on the theoretical framework in Chapter One, the next two sections analyse how Mexico and Canada's transnational alliance with domestic groups in the US (theory C) explains the power paradox, focusing on the preferences of US actors and the role of US political institutions.

6.4.2. Preferences of Domestic Groups

In the early 1990s, passing NAFTA was 'the most epic trade policy battle in Congress since the end of World War II' (Irwin 2017: 641). Although most US business interests supported the agreement, it was met with fierce opposition from certain industries (e.g. sugar, fruits), labour unions, and environmental groups (Mayer 1998). The AFL-CIO, the US largest trade union, argued that NAFTA would be 'a disaster for millions of working people in the United States, Canada, and Mexico' (Ibid.: 224). Key Congressional Democrats opposed the agreement, such as House Majority Leader Richard Gephardt and Chief Whip David Bonior (Ibid.: 201, 229). Undecided Congressional Democrats feared that voicing their support for NAFTA would undermine their re-election prospects, especially since organised labour threatened to campaign against them should they do so (Irwin, 2017: 639-40). Two months before the vote in Congress, polls predicted that NAFTA would be defeated, forcing President Clinton and US business groups to campaign arduously to persuade enough members of Congress to support the agreement. In November 1993, the House of Representatives passed NAFTA by a vote of 234-200 thanks to the support of Republicans who voted 132-43 in favour, while most Democrats

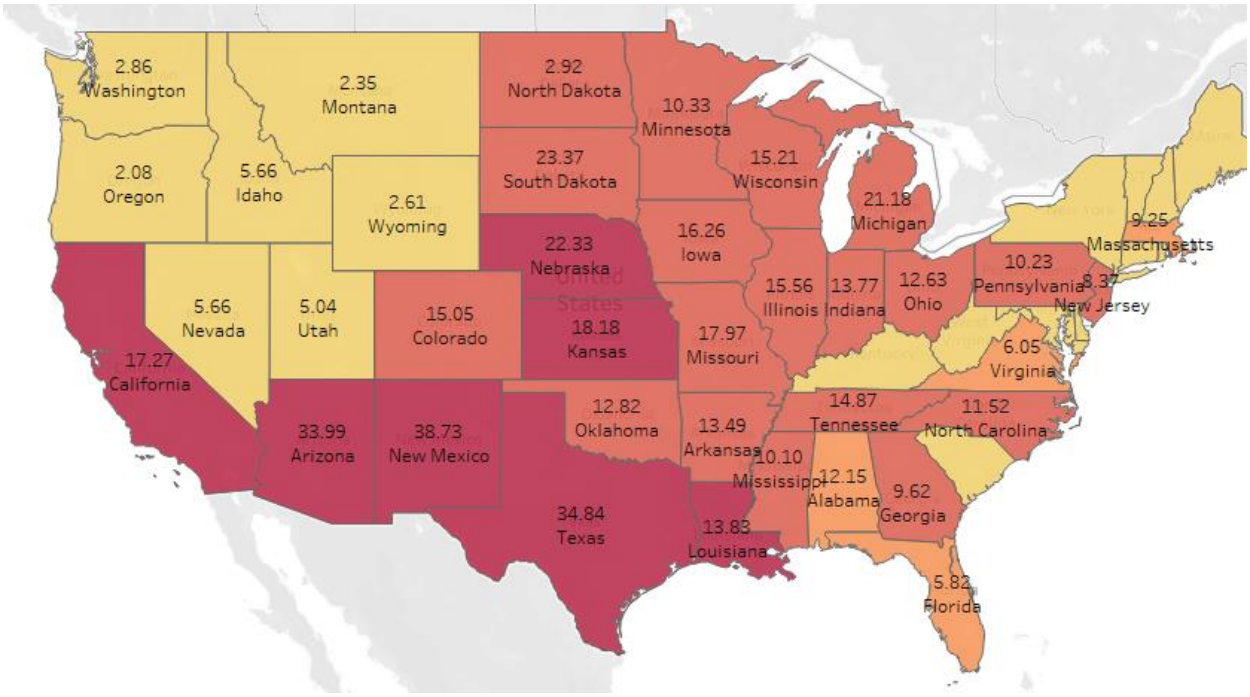
voted against the agreement (156-102). The Senate passed NAFTA by a vote of 61-38, with Republicans voting 34-10 in favour and Democrats 28-27 against (Ibid.: 642-3).

By contrast to NAFTA's difficult passage through Congress in 1993, the 2017-19 renegotiation process was characterised by bipartisan opposition to a US withdrawal from NAFTA. In December 2019, following the inclusion of stricter labour enforcement mechanisms, USMCA was overwhelmingly approved by Congress, with the House voting 385-41 and the Senate 89-10. Such levels of support in Congress for a trade agreement had not been seen since the US-Jordan PTA in 2001 (Congressional Research Service 2021; Irwin 2017: 677-9). Many US labour unions, including the AFL-CIO, endorsed the amended USMCA, breaking with twenty years of opposition to new PTAs. Even amongst the US public, divided over NAFTA in 1993, polls conducted in 2017 revealed that only ten per cent approved Trump's decision to renegotiate NAFTA and six per cent believed that the US should withdraw from the trade agreement (IUST 2017n). Even for Trump, no agreement was worse than a renegotiated agreement, although better than keeping NAFTA (Woodward 2018: 274). While US business groups' support for NAFTA in 2016 was not surprising (they had already lobbied for the agreement in the early 1990s), US labour unions and Congressional Democrats' opposition to a withdrawal from NAFTA and some of Trump's protectionist negotiating objectives contrasted with their rejection of NAFTA in the 1990s.

To understand the evolution of US labour unions and Congressional Democrats' views on the necessity of a trade agreement with Mexico, it is important to analyse the evolution of US trade with Mexico since NAFTA. Between 1993 and 2019, the share of total US exports sent to Mexico increased from 9 to 16 per cent (WITS 2023). In 2018, Mexico was the first export market for seven US states, including all states on the southern border, and the second export market for twenty US states (Figure 9 below). As the share of US exports sent to Mexico increased, so did the costs of a US withdrawal from or significant alteration of NAFTA (IUST

2017k). Although US-Mexico relations were characterised by asymmetric interdependence, the costs to the US of withdrawing from NAFTA had increased since 1994. US business groups reminded politicians of this evolution by lobbying strongly for the preservation of the trade agreement and demanding that the Trump administration 'do no harm'.

FIGURE 9. SHARE OF US STATES' EXPORTS SENT TO MEXICO (2018)



Source: Author's own, based on data from the US International Trade Administration (2022).
Note: Mexico is the first/second/third export destination for states coloured in red/dark orange/light orange, respectively. The number in each state indicates the share of the state's exports sent to Mexico.

Many US states and MNCs had much to lose from reduced access to the Mexican market. As detailed by Milner (1988: 21), greater integration in the world economy incentivises export-dependent multinationals to resist protectionism for three reasons: retaliation from trading partners, higher cost of imported inputs, and the benefits accrued to less export-dependent domestic competitors. Fear of retaliation and more costly imported inputs were key concerns of the US industry during the NAFTA renegotiation. For the US agricultural sector in particular,

fear of retaliation was predominant as the opening of the Mexican economy following NAFTA created an important export market. Regarding the Trump administration's proposal to facilitate the imposition of agricultural trade remedies, an industry representative recalled that they opposed this mechanism because of the risk of retaliation:

> They (Mexico) sounded the alarm with us about what kind of harm this would do to them […]. There would have been a lot of domestic pressure for them to do something to make it hurt for US agriculture, in response, and we didn't want that, we didn't want the threat to the markets. And so we pushed back. We provided a lot of information. We brought industry letters. And then we had a lot of conversations with USTR officials (interview, 8 December 2021).

US firms also resisted protectionism because it would have increased the costs of imported inputs. The US would have suffered economically from reductions in Mexico's access to the US market given the importance of interindustry trade. In 2015, half of total US imports from Canada and Mexico were intermediate goods, by contrast to 37 and 28 per cent in the case of imports from the EU and China, respectively (Parilla 2023). In Michigan, the heart of the US auto industry, 61 per cent of intermediate goods imports were provided by NAFTA partners (Ibid.). Between 1993 and 2019, the share of US imports coming from Mexico doubled from 7 to 14 per cent, while the share of US imports coming from Canada declined from 19 to 12 per cent during the same period, in part due to the share of US imports coming from China tripling from 6 to 18 per cent (WITS 2023). In Mexico and Canada, Chinese imports increasingly replaced US imports, which fell from 74 to 45 per cent and 67 to 51 per cent, respectively, during the same period. Despite the China shock, NAFTA shaped production networks such that a US withdrawal would have been costly for regionally integrated industries. The paramount example is the automotive industry, where cars cross the US border up to eight times during production as they integrate materials and parts produced by Canada and Mexico (Wilson 2011: 1). The share of US value-added in vehicles imported from Mexico is estimated at over a third, whereas the share of Chinese value-added in vehicles imported by the US from

Mexico is only five to six per cent (American Automotive Policy Council 2017; Flatness and Rasmussen 2017; Koopman et al. 2010).

Respondents interviewed, whether Mexican, Canadian, or American negotiators or lobbyists, concur on the preponderant role of North American economic integration in the non-adoption of many of the Trump administration's negotiating objectives. Referring to a map similar to Figure 9, a Mexican negotiator commented:

> I wanted to show you this map to show how Mexico is important to the US. Of course, this was not the case 25 years ago because Mexico was a closed economy. But now, after 25 years of having this free trade agreement, Mexico has become increasingly important to some of the most important US stakeholders (interview, 11 November 2020).

Similarly, US chief negotiator John Melle highlighted the role of the US business sector in weakening some of the Trump administration's most radical objectives, including gaining leverage by withdrawing from NAFTA, imposing a 50 per cent US-specific auto rule of origin, and including a five-year sunset clause in the agreement:

> All of those 'poison pills' (a term used by the US business sector to label certain US negotiating objectives) were perhaps not only poisonous to Mexico or to Canada but to important sectors in the US economy. It is important to look at how the evolution of those issues occurred both within the domestic context and within the negotiations themselves as well. The five-year sunset clause, there was a lot of opposition in the US to that, in the business community as well. The concern there was the uncertainty that that creates […] There was a large segment in all three countries that did not want the agreement to expire or to be renegotiated. *We even had Democratic members of the House who had voted against the agreement saying they hated the NAFTA but "You can't terminate it"* (interview, 16 December 2020, emphasis added).

Long-standing opponents of NAFTA, such as Democrat House Representatives Bill Pascrell (NJ) and Lloyd Doggett (TX), argued that a US withdrawal would cause more harm than good (Palmer 2017). By joining Republicans in their opposition to a US withdrawal from NAFTA, Democrats unified Congress against Trump's strategy of withdrawing the US from NAFTA by

executive decree to gain leverage in the negotiations. Juan Carlos Baker, Undersecretary of Foreign Trade, stressed that Congress and the US business sector could not support Trump's radical negotiating objectives given the costs of disrupting North American economic integration:

> We knew that such a radical position could not be supported by the US Congress or by the US business sector. Mexico did not make much effort: the most extreme ideas, the poison pills, were not taken care of by Mexico, they were taken care of by domestic stakeholders in the US. From this perspective, it would have been a mistake for Mexico to try to negotiate these issues or to offer something in exchange for these issues not being included because the weight of reality in the US was going to change that. So Mexico just tried to accommodate what we could to provide some face-saving for the US, but at the end of the day, we knew that some of these issues were not going to fly in any possible circumstance (interview, 10 December 2020).

As US businesses increased trade and investment with Mexico following NAFTA, stronger coalitions emerged to maintain the trade agreement. For the US agricultural sector, represented in part by the American Farm Bureau, NAFTA led to a boost in exports to Mexico of meat and grains (at the expense of Mexican corn farmers in particular), while Mexico increased its exports of seasonal and fresh products to the US (at the expense of US fruit producers, such as in Florida). Each country specialised in its comparative advantage: the US in capital-intensive agriculture and Mexico in labour-intensive agriculture. Although seasonal growers in the US remained politically influential given their concentration in swing states such as Florida, their concerns were dwarfed in US agricultural business groups by the increased value of agricultural exports to Mexico. The stronger weight of US export interests since NAFTA prevailed over protectionist interests, even in the politically sensitive agricultural sector. Mexican small firms faced similar problems during the trade liberalisation reforms leading to NAFTA as industry associations tended to represent the interests of large firms (Shadlen 2004: 15-16, 99-100).

Twenty-five years of North American economic integration under NAFTA also changed the preferences of US labour unions, which had largely rejected NAFTA in the 1990s and criticised

it since then. US labour unions supported a renegotiated deal over no deal given that NAFTA had already reshaped production structures in North America (interviews with labour union representatives, 15, 17 March and 2 April 2021; Byrd, 2019). According to a labour union representative:

> For President Trump to proceed with withdrawal from NAFTA would return us to an even worse situation probably than had existed under NAFTA, with massive investments by US companies in Mexico, and no or limited access to US exports. This was not a situation where there was a new negotiation of an agreement, but rather a secondary negotiation of an existing agreement. That was important to remember (interview, 15 March 2021).

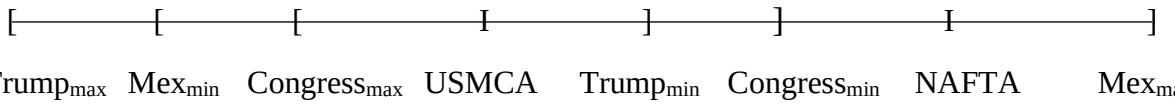
Another US labour union representative stressed that beyond the opposition the Trump administration faced due to the economic costs of disrupting NAFTA, Trump also had to deal with institutional barriers which undermined his capacity to alter the agreement:

> First of all, it's very complicated to try to unwind it. You have all these commitments and tariff reductions and things that have already happened, how do you just reimpose? Sometimes you need to change your laws, it's not easy. But then also, obviously, every business and communities that rely on this sort of business, they are going to argue, hardly, very aggressively, that completely eliminating this (NAFTA) will just cause complete economic havoc. I'm not saying I agree in all those instances, but that's a strong political case to make (interview, 17 March 2021).

The economic costs to the US of withdrawing from or significantly altering NAFTA increased over time. Economic integration created increasing returns to preserving NAFTA. This impacted the preferences of US domestic actors, who reduced the Trump administration's Level II (domestic) win-set size. Figure 10 represents the possible negotiating outcomes, where $Trump_{max}$ represents the best outcome for the Trump administration and $Mex_{max\ is}$ the best outcome for the Mexican government (it can also represent the best outcome for the Canadian government). Although the Trump administration could have obtained an agreement between Mex_{min} and $Trump_{min}$, the preferences of domestic actors, in particular, Congress, forced it to

find an agreement between $Congress_{max}$ and $Trump_{min}$, to the advantage of Mexican and Canadian negotiators.

FIGURE 10. WIN-SETS DURING THE NAFTA RENEGOTIATION



A difficult ratification process typically gives the executive a bargaining advantage as it can obtain new concessions by arguing that those are necessary for the agreement to be approved by domestic veto players (Putnam 1988; Milner and Rosendorff 1997). When the preferences of the legislature are closer to those of the trading partner than the executive, however, a difficult ratification process becomes a disadvantage for the executive. The US Congress obtained concessions from the Trump administration, such as improving the state-to-state dispute settlement mechanism, which benefited Mexico and Canada. Congress's role in influencing US negotiators' win-set size leads to the analysis of how US political institutions contributed to path dependence.

6.4.3. Political Institutions

Three characteristics of the US political system increased the costs to the Trump administration of withdrawing from or severely disrupting NAFTA: Congress' constitutional authority over trade policy, the risk of losing seats in Congress due to the costs of economic disruption, and business lobbies' influence on political representatives. These three factors reflect three characteristics of a democracy: separation of powers, electoral competition, and the strength of civil society. Together, these factors undermined radical change by restricting the executive's power, increasing the risk of losing elections (due to the impact of economic disruptions), and

allowing civil society to infuse cost aversion in the executive's agenda (the US democracy provides a particularly strong voice to business groups due to their importance in funding political parties).

First, the US Congress has constitutional authority over trade policy, which constrains the President's powers to act unilaterally. Trump would have faced a legal challenge over his authority to withdraw the US from NAFTA by executive decree if he had attempted to do so. While precedents in US law would have probably allowed the President to do so, the legal challenge would have dragged the process over months or years (Trachtman 2017). If the Supreme Court decided that the US President could not withdraw from NAFTA without authorisation from Congress, Trump's bargaining power would have been undermined. A Trump administration official recalled:

> We chose not to withdraw because it was going to open a whole can of worms that we didn't really want to get into. I think our assessment was that we probably would win that case. There was a whole legal discussion on our ability to withdraw from agreements more broadly. And there was a Supreme Court case a while back that basically said 'In the absence of Congress saying that Congress has to approve a withdrawal, then the President can do it'. And in our implementing language on NAFTA, there was nothing saying that Congress had to approve the withdrawal. We just had to give thirty days of notice or something along those lines.[11] So we probably would have won that. But there was certainly a very real possibility that we would have been told that no, actually you can't withdraw. One that's a bad vote politically, although I don't think that was ever too much of a concern. But two, I think that being able to say "Oh, we're gonna withdraw" was a good bargaining chip. And if courts tell you "Oh, no, you can't do that" it sort of takes away the negotiating piece that you've got in your back pocket (interview, 25 January 2021).

Even if the Supreme Court had authorised the US President to withdraw from NAFTA by executive decree, it is unlikely that withdrawing would have returned North American relations to WTO rules given that trade agreements are passed in the US through a Congressional implementation bill rather than ratification (Bradley 2018: 1634-5; Trachtman 2017). To

[11] NAFTA Chapter 22 Article 5 requires Parties to notify other members six months in advance that it will withdraw from the agreement.

remove the implementation bill, the President would have likely required Congressional support.

Although Trump could probably side-line Congress to withdraw from NAFTA (even though this would not automatically remove the implementation bill), passing USMCA required support from both chambers of Congress. As such, the Trump administration had to make concessions to Democratic and Republican representatives in Congress, such as abandoning its objectives of including a five-year sunset clause, eliminating ISDS, and obtaining US-specific rules of origin for autos. When the Democratic Party won control of the House of Representatives in the 2018 mid-terms, the Trump administration had to find new compromises including ensuring the good functioning of the state-to-state DSM and removing certain intellectual property provisions. Those changes improved the outcome for Canadian and Mexican negotiators.

Faced with the veto power of Congress, Trump sought to undermine the legislature by threatening to unilaterally withdraw from NAFTA, which would have left Congress with the choice between no agreement or USMCA instead of NAFTA or USMCA. The inclusion of a sunset clause in USMCA also sought to change the balance of power with Congress by increasing the executive's power to withdraw unilaterally: by not signing the renewal of USMCA, the President would be able to force a withdrawal. Even a withdrawal using the sunset clause, however, is likely to be challenged in court. According to a Republican official in Congress:

> We pushed really hard to put a clause in there to require Congress to have to vote on this (sunset clause) and USTR was firmly opposed […] If and when this is ever triggered, and the withdrawal starts, that process starts, there will be a lawsuit in the United States. There are strong feelings on both sides of this. And I can tell you from sitting in the room trying to negotiate with congressional Democrats and the administration at the time on this, there is the strong belief that this is constitutionally within the purview of Congress and Congress only. Then there's the point of view that this is part of the President's constitutional authority to set trade policy and share that

> with Congress through powers Congress has delegated to the President. And it was a question that was very unsettled. And litigation was already being studied and planned for just when the President was talking about potential NAFTA withdrawal (interview, 29 August 2022).

Even though Congress did not succeed in including a clause in USMCA requiring a vote from Congress for the sunset clause to take effect, Congress could still challenge a withdrawal by executive decree in courts. Congress also included language in the USMCA implementation bill specifying that the executive must inform the public and conduct consultations before the sunset clause takes effect (Ibid.).

Second, the electoral competitiveness of Congressional seats undermined President Trump's willingness to cause trade disruptions given that they would jeopardise Republicans' prospects in the upcoming 2018 mid-term and 2020 presidential elections. Several econometric studies demonstrated that Trump's trade wars led to the Republican Party's electoral loss in the 2018 midterm House elections (Blanchard, Bown, and Chor 2019; Chyzh and Urbatsch 2021; Fetzer and Schwarz 2021; Hinojosa Ojeda and Telles 2021). Early on in the Trump presidency, Secretary of Agriculture Sonny Perdue dissuaded Trump from withdrawing unilaterally from NAFTA by showing him a map of the US states which would be hardest hit by this decision, which were mostly Republican. The political importance of the agriculture sector impacted negotiations on other sectors, such as autos. According to an auto industry representative:

> The agriculture sector was critical to the success of all of this. The other interesting thing about the agricultural sector in the United States is that it tends to be represented by Republican politicians. They were critical to the success of this renegotiation. They were not going to let it disappear. They were getting hammered by China. They were really upset with the demise of TPP. And so to lose NAFTA would have just been a bridge too far for them. The agriculture sector in the United States really should be credited with a lot of the success in keeping the train on the tracks throughout the process (interview, 1 September 2021).

According to a Democratic Party official, ‘some of the free trade Republicans are free trade Republicans because of agricultural issues’ (interview, 12 May 2021).

The electoral competitiveness of Congressional seats enabled US trading partners to magnify the costs of economic disruption through strategic trade retaliation (Lake and Nie 2023). Mexico and Canada, but also China and the European Union, retaliated against US steel and aluminium tariffs by targeting exports from Republican-controlled states with representatives influential in Congress. As a result of Mexican and Canadian retaliatory tariffs, for instance, the influential Senator Grassley from Iowa alongside other members of Congress pressured Trump to remove the national security (section 232) tariffs on Mexico and Canada:

> He (Sen. Grassley) threatened withdrawing his support for USMCA in a Wall Street Journal op-ed in the spring of 2019 if the President didn't remove the 232 steel and aluminium tariffs on Canada and Mexico. As a result of those 232 steel and aluminium tariffs, Canada and Mexico were retaliating and their top targets for the retaliation was the agricultural sector. That was really hitting Iowa hard. That kind of a public threat by Senator Grassley, in a publication like the Wall Street Journal, it got the President's attention. And within a month, those 232 steel and aluminium tariffs were taken off Canada and Mexico. So there were definitely a lot of key agriculture players between members of the administration itself, members of Congress, and then key players in the sector, that were making that known to the President (interview with Congressional Republican official, 29 August 2022).

As in many other US states, Canada and Mexico were the top two trading partners of Iowa, which led to strong opposition to Trump’s threat of withdrawing the US from NAFTA (Ibid.).

Third, the influence of business groups in the US increased the costs to the US President of disrupting North American economic integration. Breaking from past practices, the Trump administration sought to gain autonomy from such influence by distancing itself from businesses. USTR Lighthizer initially refused to meet with some of the auto representatives. A Trump administration official stressed the novelty and risk of Trump’s approach:

> The (US) Chamber of Commerce has basically bankrolled the Republican Party for decades. And so it was a huge, huge political risk for Trump to break and sort of go

> against the Chamber because the Republican Party has really always been this pro-business party in the US. The Chamber opposed a lot of what he was doing on trade, not just USMCA. When he was throwing tariffs on China, I think they were freaking out, and it was very bold of him to break with the Chamber (interview, 25 January 2021).

The term 'poison pill' was coined by the President of the US Chamber of Commerce, Tom Donohue, to describe US objectives considered unacceptable, which included a five-year sunset clause, the elimination of ISDS, and higher auto industry rules of origin (this term was later adopted by Mexican and Canadian negotiators) (Hackbarth 2017). His plea to preserve NAFTA provisions was echoed early on in the negotiations by other large US business groups, such as the Business Roundtable, the National Association of Manufacturers, the Coalition of Service Industries, and the American Farm Bureau (Palmer 2017). Similarly, over 300 state and local chambers of commerce demanded that the Trump administration 'do no harm' in the NAFTA negotiations (IUST 2017k). US firms had increased their exports to Mexico (e.g. US agriculture), invested in Mexican supply chains (e.g. auto industry) and distribution networks (e.g. financial services) in the belief that NAFTA would be maintained, and as such did not want to lose value from those investments.

Faced with the lower receptiveness of the Trump administration, businesses focused their lobbying efforts on other political representatives: members of the House, Senate, and governors. They targeted influential politicians within the Trump administration and Republican Party who helped weaken or remove some of Trump's initial objectives, such as Agriculture Secretary Sonny Perdue lobbying on behalf of agricultural businesses and Republican Party representatives against a withdrawal from NAFTA. This strategy was also actively used by the auto sector. A representative from Toyota recalled:

> We have plants in Indiana, Kentucky, and right away you've got Mike Pence from Indiana, Mitch McConnell is from Kentucky, John Cornyn is from Texas and Ted Cruz is from Texas. So we've got facilities in all three states. We've also got Alabama, Mississippi. So because we weren't that successful with the USTR, a lot of our lobbying

> efforts were with governors of key states, congressmen and senators, because we were trying to push back against some of the USTR's demands, but using them as leverage […] If it (the USMCA) threatens jobs in, for instance, the state of Kentucky or the state of Indiana, then it's imperative for state governors or congressmen or senators to make sure they're not disadvantaging the operations that are in their states. That was reasonably successful. Lobbying helped moderate some of the USTR's demands. I think they would have continued to be much stronger if we hadn't pushed back from the state level (interview, 16 November 2020).

The importance of lobbies in US politics increased the costs for Trump of creating economic disruption, alongside separation of powers (Congress's constitutional authority over trade) and electoral competitiveness (trade disruption undermining the electoral prospects of Republicans, which was magnified by strategic retaliation from Mexico and Canada).

6.5. Conclusion

The renegotiation of NAFTA was characterised by a power paradox: despite the large US power asymmetry with Mexico and Canada, the Trump administration was not able to impose any of its initial negotiating objectives (half are included in USMCA in a significantly weakened form). This paradox is explained by the role of path dependence in creating domestic constraints on President Trump's power. First, 25 years of economic integration under NAFTA increased the costs of trade disruption for many US actors. US labour unions and Democrats joined the US business sector in arguing that a withdrawal from NAFTA would be counterproductive, in contrast to their resolute opposition to NAFTA in the 1990s. This echoes US trade policy in the 'competitive' period of the 1970s-80s (cf. Chapter Three), where US integration in the world economy post-WWII created path dependence, leading US multinationals to resist protectionism despite similar import competition pressures than in the 1920s (Milner 1988). Second, three democratic institutions restrained the President's power to alter NAFTA: separation of powers (Congress's constitutional authority over trade), electoral competitiveness

(trade disruption undermined Republicans' election prospects in swing states), and the strength of civil society (business lobbies' influence on US politics). The veto power of the US Congress was reinforced by the latter two democratic institutions as the electorate and businesses voiced their preferences by voting and lobbying. Even a US President, the world's most powerful figure, could not significantly alter NAFTA or trigger the withdrawal process given the costs of breaking path dependence.

Mexico and Canada were also affected by path dependence as a result of NAFTA. In Canada, labour unions and the Liberal party sought to preserve NAFTA, whereas they had led opposition to trade liberalisation in the 1980s and 1990s, influenced by the nationalist economic policies of Justin Trudeau's father, Pierre. In Mexico, preferences of domestic actors also changed as the Mexican economy became much more dependent on trade with the US. While President López Obrador initially opposed NAFTA in the 1990s and 2000s, by the time of his 2018 presidential campaign he acknowledged that the costs of withdrawing from NAFTA were too important (Cunningham 2018). Just as in the US, NAFTA changed the structure of the Mexican economy by weakening import-competing sectors and strengthening export interests, which lobbied to preserve NAFTA (Shadlen 2017). One negative consequence, in so far as it undermined the use of industrial policies to promote technological upgrading, is that the Mexican government 'over-complied' with NAFTA intellectual property rights regulations (Ibid.: 229-232). Second, political institutions changed as Mexico pursued a strategy of negotiating PTAs with the global North, including with the EU and Japan, leading to multiple commitments to restrict its policy space. The next chapter argues that Mexico's negotiating stance also evolved on labour standards, as the Peña Nieto government sought to include provisions negotiated in previous PTAs while President López Obrador used USMCA to lock in his ambitious labour reform.

Chapter 7. USMCA Labour Standards

> *It was clear to us from the work we had done in the CPTPP, the Trans-Pacific Partnership, that we wanted to have a change. We were okay with modifying the approach to labour issues in NAFTA because it would reflect the reforms and the changes that have gone on in Mexico relatively recently.*
>
> Kenneth Smith Ramos, Mexican chief negotiator, Peña Nieto administration, interview, 16 October 2020

> *The strong (labour) obligations created by USMCA were something that the President told me directly and very clearly: that is fine. It will only help us come forward, roll out the labour reform. So that is not a problem. If there are cases, let them come, and if there is merit, we will address it because it is part of the labour reform. That was something that was very much part of his agenda politically for twenty years or so. He was unhappy with the very archaic labour regime we had for decades and decades in Mexico.*
>
> Jesús Seade, Mexican chief negotiator, López Obrador administration, interview, 15 October 2020

7.1. Introduction

USMCA contains labour provisions unprecedented for a trade agreement, including Annex 23-A overhauling a hundred years of Mexican labour relations, a comprehensive labour chapter subject to novel provisions, and a high-wage rule of origin (Labour Value Content) in the automotive sector. By contrast to previous US trade agreements, it also includes footnotes that facilitate its enforcement through the state-to-state dispute settlement mechanism and a unique factory-specific Rapid Response Mechanism (RRM) aimed at addressing in a few months violations of workers' rights to freedom of association and collective bargaining. The US implementation bill dedicated 180 million dollars over four years to help Mexico enforce its

labour laws, created an independent body in charge of monitoring progress, and financed five labour attachés in Mexico.

Drawing on interviews and the USMCA text, this chapter analyses the negotiation process to explain the inclusion of those ground-breaking provisions. Of particular interest is the Mexican government's support for labour and environmental standards in USMCA, by contrast to its opposition in the original NAFTA negotiation and negotiations over a Free Trade Ara of the Americas in the early 2000s (Deere-Birkbeck and Esty 2002). Both the Peña Nieto and López Obrador administrations were supportive of higher labour standards during the renegotiation. While the Peña Nieto government wanted to update NAFTA to include Mexico's labour commitments in other PTAs, the López Obrador government accepted unprecedented provisions to lock in the implementation of its labour reforms, just as NAFTA had been used by President Salinas de Gortari in the 1990s to lock in trade liberalisation reforms (Cameron and Tomlin 2000).

In the United States, the inclusion of labour standards was pursued for protectionist reasons by the Trump administration, Congressional Democrats, and US labour unions. The Trump administration included a footnote in USMCA which rendered the Rapid Response Mechanism nearly unenforceable in the US, while the Labour Value Content rule of origin was set at 16 dollars per hour in an attempt to dissuade firms from offshoring to Mexico. Although Republicans in Congress opposed the unprecedented labour provisions in USMCA, they relented given the responsiveness of their voting base to Trump's agenda. As to the Canadian government, despite initially pushing for stronger labour standards, it prioritised other issues once the Trump administration conditioned labour standards on obtaining concessions in other areas.

The chapter concludes by analysing the effects of USMCA labour standards on Mexico's access to the US market and labour conditions. Until USMCA, the empirical literature concluded that

labour standards did not reduce the global South's market access to the global North and had no or weak developmental effects (Raess 2022; cf. literature review below). During their first three years (July 2020-June 2023), USMCA labour standards did not reduce Mexico's access to the US market while contributing to limited improvements in labour conditions (freedom of association, collective bargaining, minimum wage). This outcome can be traced to three characteristics of USMCA's design. First, the US supported the implementation of Mexico's labour reform through financial assistance and a commitment to raise issues through the Rapid Response Mechanism. Second, the López Obrador government addressed cases brought by the US through the RRM. Third, successful lobbying from the auto industry ensured that the LVC rule did not cause a reshoring of production to the US (cf. section 5.4.2.).

7.2. From NAFTA to USMCA

7.2.1 The Trade-Labour Nexus

The passage of NAFTA through the US Congress, followed by the creation of the WTO, placed labour rights and standards at the forefront of trade policy debates in the 1990s (Luce 2005). Although the US had already conditioned market access on labour standards since the 1980s under the WTO Generalised System of Preferences (Murillo and Schrank 2005; Raess 2022), NAFTA was the first trade agreement to contain labour standards. The North American Agreement on Labour Cooperation (NAALC) was included as a side agreement to NAFTA to obtain votes from Congressional Democrats. Following the precedent set by the NAALC, US President Bill Clinton argued in 1996 for the inclusion of a 'social clause' at the WTO, which was rejected by most governments in the global South and contributed to the collapse of the 1999 Ministerial Conference in Seattle (Polaski 2022: 204-5).

The literature on labour standards from this period mostly focused on whether labour standards should be included in trade agreements (Bhagwati 1995; Brown 2001; Charnovitz 1992; Freeman and Elliott 2003; Kabeer 2000; E. Lee 1997; Maskus 1997). Economists, governments in the global South and multinationals were largely opposed to a trade-labour nexus, although some saw it as an opportunity to improve consumer perception of products made in the global South (Polaski 2022: 207-8). Neoclassical economist Bhagwati (1995), who was at the forefront of the opposition to a trade-labour nexus, argued that it would undermine the global South's comparative advantage in low-wage labour, and hence its prospects for economic development. By contrast, advocates of a trade-labour linkage contended that, in addition to protecting labour rights, labour standards in PTAs can prevent a race to the bottom by sanctioning countries that lower their labour standards to gain a competitive advantage (social dumping) (Charnovitz 1992; E. Lee 1997; Qureshi and Weiss 1998; Addo 2015).

The empirical literature is not conclusive on the existence of such a race to the bottom between North and South, while there is some evidence of a South-South race to the bottom (Davies and Vadlamannati 2013; Guasti and Koenig-Archibugi 2022; Rodrik 1997; Singh and Zammit 2004). In the South, labour standards can reduce the capacity of multinationals to squeeze the profits and wages of their suppliers. This logic in global supply chains has been associated with countries such as Mexico witnessing economic upgrading without social upgrading (Gereffi, Humphrey, and Sturgeon 2005; Milberg 2013). Labour standards can also promote economic upgrading in the global South by forcing firms to increase their productivity to remain competitive (Amsden 2001; Brown 2013; Gereffi 2018). In 1970s Singapore, for instance, the government repeatedly increased the minimum wage, which ultimately led to FDI inflows targeting sectors with more value-added (Ibid.; Lim 1983).

The literature progressively shifted away from the debate over the inclusion of labour standards in trade agreements for two reasons. First, labour standards were included in PTAs, although

they remained outside the WTO's agenda (Compa 2022: 274-5; Smith et al. 2021: 3, 26). By 2019, 91 trade agreements contained labour provisions, and since 2015 over half of new PTAs signed contain labour provisions (Ibid.: 3, 34). This change occurred as the US, followed by the EU, adopted a strategy of requiring the inclusion of labour standards in their PTAs, given opposition in the WTO. The US and EU succeeded in mainstreaming the trade-labour nexus as labour standards can now be found in North-North, North-South and South-South PTAs involving countries such as Chile, Canada, New Zealand, South Korea, Japan, China, Mexico, Peru, and South Africa (Postnikov 2022: 253; Smith et al. 2021: 36-7).

Second, labour standards in PTAs never led to trade sanctions, which undermined the argument that they would be used as a protectionist tool. While the EU did not favour enforcement through sanctions, the US did but was never able to implement them (Postnikov 2022: 215-16). As part of the 'May 10' 2007 agreement, the US, following pressure from House Democrats, required that labour chapters in PTAs be fully enforceable through the state-to-state dispute settlement mechanism (DSM). The DSM only applied to federal/national laws and to violations which occur 'in a manner affecting trade or investment between the parties' and 'through a sustained or recurring course of action or inaction', however, which placed a high burden of proof. By 2020, when USMCA entered into force, US-Guatemala was the only case in 25 years that had proceeded to a DSM panel (Polaski 2022: 215). After eight years, the panel ruled in 2017 that, although labour rights violations occurred in Guatemala, no sanction could be imposed as there was no proof that the violations occurred 'in a manner affecting trade or investment', which was interpreted as requiring the demonstration that lower labour standards enabled firms to export their goods at lower prices (Compa and Brooks 2019: 243-244).

Logically given the lack of sanctions, the few empirical analyses conducted so far find that labour standards in North-South PTAs do not reduce exports from the global South, and can even increase them through reputational effects (Raess 2022). A recent study using a more

precise database (LABPTA) finds that PTAs with strongly institutionalised cooperation mechanisms on labour increase exports from the global South, while PTAs with strong enforcement mechanisms have no impact on exports (Carrère, Olarreaga, and Raess 2022). Although the data so far suggests that labour standards have no protectionist effect and can even increase exports from the global South, the unprecedented labour provisions in USMCA create more effective opportunities for protectionism.

Given the lack of enforcement through sanctions, the literature has focused on assessing the extent to which labour standards in PTAs led to improvements in labour conditions. Labour standards are implemented with a different mix of pre-ratification conditionality, post-ratification conditionality, and promotional measures (ILO 2013). The US historically preferred conditional measures, whether conditioning ratification of a PTA on changes in the trading partner's labour laws or by including enforceable dispute settlement mechanisms (Ibid.; Postnikov 2022: 249). The EU adopted a more promotional approach to enforcement in the form of expert panels without sanctions for non-compliance (Smith et al. 2021). The US approach has been found more effective during the pre-ratification phase as entry into force of the PTA is conditioned upon the passage of labour reforms (A. Evans 2021; Kim 2012; Postnikov 2019, 2022: 251-2).

Beyond differences between EU and US labour standards, most quantitative and qualitative studies find no significant effect of labour provisions in PTAs on labour standards (real wages, occupational safety, gender wage gap, working hours…) but some effect on intermediate outcomes such as labour market monitoring (Aissi et al. 2016; Harrison et al. 2019; Kamata 2016; Marx, Lein, and Brando 2016; Orbie, Putte, and Martens 2017; Posso 2017; Roozendaal 2017). PTAs not involving the US or EU, although severely under-researched, have weaker labour standards and are thus less likely to be effective (Smith et al. 2021: 36-7; Raess and Sari 2018). Recent quantitative research using the more precise LABPTA database, however, found

that PTAs which ensure strong institutional cooperation on freedom of association and collective bargaining improve compliance, while strong enforcement mechanisms have no effect (Raess 2022; Raess and Sari 2018). For instance, the North American Agreement on Labour Cooperation (NAALC), although limited, helped stakeholders identify shortcomings and create the transnational labour communities necessary to demand and obtain significant regulatory changes during the NAFTA renegotiation (Compa 2022; Kay 2011). Labour rights violations remained pervasive in Mexico, however, generating a list of US grievances which would inform the drafting of the USMCA labour chapter (Compa and Brooks 2019).

7.2.2. USMCA Labour Provisions

The unprecedented labour provisions in USMCA are bringing to the fore the debate on the developmental effects of labour standards in PTAs (De la Cruz 2022). By contrast to the side agreement in NAFTA, labour provisions in USMCA are included in a labour chapter (chapter 23), reflecting the evolution of labour standards in US PTAs since 1994. Articles 23.2 and 23.3 include commitments to enforce ILO core principles in national legislation (with still no requirement to ratify ILO core conventions given the US reluctance to do so). The chapter also comprises novel commitments for US PTAs, such as the prohibition to import goods made by forced labour, including from third countries (Article 23.6), protection against gender discrimination (Article 23.9) and violence in the workplace (Article 23.7), as well as measures to guarantee the rights of migrant workers (Article 23.8) (Compa and Brooks 2019: 229, 232). Also unprecedented for a PTA is a footnote to Article 23.3 on labour rights precising that ‘the right to strike is linked to the right to freedom of association, which cannot be realized without protecting the right to strike’. This footnote places the signatory governments on the side of unions in a long-standing dispute at the ILO (Vogt 2019; Compa 2022: 287).

The labour chapter is subject to the USMCA state-to-state dispute settlement mechanism (DSM). Whereas the DSM was not operational under NAFTA as loopholes enabled countries to block the appointment of roster members, it became operational following amendments negotiated in 2019 which closed those loopholes. Compared to previous US PTAs with the exception of NAFTA (which only required labour violations to be 'trade-related'), bringing cases is also made easier by a footnote to Article 23.3 which loosens the interpretation of 'in a manner affecting trade or investment' to include most activities:

> For greater certainty, a failure is "in a manner affecting trade or investment between the Parties" if it involves:
>
> i. a person or industry that produces a good or supplies a service trade between the parties or has an investment in the territory of a Member State that has failed to comply with an obligation; or
> ii. a person or industry that produces a good or supplies a service that competes in the territory of a Member State with a good or service of another Member State.

The amended USMCA also adds another footnote to Article 23.3 placing the burden of proof on the responding government:

> For purposes of dispute settlement, a panel shall presume that a failure is in a manner affecting trade or investment between the Parties, unless the responding Party demonstrates otherwise (USMCA Article 23.3 footnote 5).

Together, these changes aim to facilitate the launch of cases and to prevent a new 'US-Guatemala' panel resolution by considerably reducing the level of evidence needed to prove that a labour rights violation affects trade or investment. In the case of violence against workers, the amended USMCA adds that it is no longer necessary to demonstrate that violations are 'sustained or recurring' to bring a dispute settlement case, such that a single incident can lead to a case (USMCA Protocol of Amendment, Article 23.7).

The USMCA pushed pre-ratification conditionality further than any other PTA by requiring Mexico to overhaul a century of labour relations. Since the end of the Mexican Revolution in

1917, labour unions in Mexico were typically controlled by the government or by the firms themselves. These 'protection unions', which restrained freedom of association and collective bargaining, were used to repress wages and working conditions as part of Mexico's national development strategy of competing internationally based on low wages (Otis 2012; Tilly 2014). In USMCA Annex 23-A, Mexico agreed to implement a list of labour reforms aimed at guaranteeing freedom of association and collective bargaining. Clause 3 specifies that the legislation must be adopted before January 1, 2019, and that 'it is further understood that entry into force of this Agreement may be delayed until such legislation becomes effective'. The reforms include eliminating the tripartite labour boards, which regrouped government, business and mostly 'protection union' representatives, to ensure that labour representation disputes can be arbitrated by the judicial system. To ensure workers have a chance to replace the protection unions, Annex 23-A also requires new trade union elections by secret ballot in all Mexican states. The López Obrador government passed the reforms in 2019 and set itself a four-year timeframe to implement them, ending in April 2023. In addition, Mexico had to demonstrate to the US Congress that it provided sufficient funding to its Ministry of Justice to enforce those labour reforms. Annex 23-A is subject to the state-to-state DSM.

USMCA Annex 31-A adds an unprecedented DSM, the Rapid Response Mechanism (RRM), aimed at addressing violations of worker rights to freedom of association or collective bargaining at 'covered facilities' in 'priority sectors' (all sectors except agriculture) within a few months. Following a complaint, the responding government has 45 days to respond, after which the complaining government can demand the creation of a panel constituted of labour law experts. If the panel finds a violation has occurred, sanctions range from the removal of preferential tariffs for goods produced in the factory (first violation) to the removal of preferential tariffs for all the company's goods (second violation) to the blocking of goods at the border (third violation). Should a panel find that there has been a labour rights violation, the

complaining government can apply sanctions with retroactive effect, which means that it can claim tariffs on the goods imported from that factory since the day the panel request was submitted (Compa 2022: 290). If a state-to-state dispute settlement panel finds a labour rights violation, that issue can then be brought to the RRM for two years or until the conclusion of the next review period, whichever is later, thereby widely increasing the RRM's mandate (Article 31-A.12). Given the removal of the 'sustained and recurring' violation requirement for bringing dispute settlements on violence in the workplace, this issue would be the easiest to add to the RRM's mandate.

Under the RRM, the complaining government can suspend the final settlement of customs accounts from the targeted factory as soon as it requests the formation of a panel (Article 31-A.4.3). Given that the RRM has limited resources, which constrains panels to investigate only a few cases at a time, a 'flood of cases' could lead to major delays in panel formation, in which case trade uncertainty could be maintained for long periods without proof of labour rights violations. A Democrat trade official argued that 'the moment you know there is a problem, you suspend liquidation of customs entries' and that this mechanism would also be used if panels become delayed (interview, 23 October 2020). Consistent with this statement, the Biden administration has used this provision in all the RRM cases it submitted to signal the possibility of trade sanctions (Compa 2022: 291; USTR 2023). The risk of the RRM mechanism being used for solely protectionist reasons is mitigated by Article 31-A.11, however, authorising a country to raise a state-to-state DSM procedure over abuses of the RRM. If the panel finds that the responding government has not used the RRM 'in good faith', the complaining government can choose to prevent the responding country from using the RRM for two years.

Finally, USMCA broke with the traditional approach to labour standards in PTAs by including the auto rule of origin (Labour Value Content) that 40/45 per cent of the value of a car/truck be produced by direct production workers earning on average 16 dollars per hour (cf. section

5.4.2.). USMCA labour provisions are a major break with previous PTAs. Table 8 compares USMCA labour standards with those in NAFTA and the Trans-Pacific Partnership (TPP). The TPP, signed in 2016 by President Obama, contained the most ambitious labour standards in a US PTA before President Trump withdrew the US from the agreement on his first day in office.

TABLE 8. EVOLUTION OF LABOUR STANDARDS IN US TRADE AGREEMENTS

	NAFTA (1994)	TPP (2016)	USMCA (2020)
Scope	Side agreement (NAALC)	Chapter 19 and US labour side agreements with Vietnam, Brunei, and Malaysia	Chapter 23 and Annex 31-A (Rapid Response Labour Mechanism)
	Refers to 11 labour rights	Refers to ILO Declaration	Refers to ILO Declaration
	No extraterritoriality	Discourage all imports of goods made from forced labour	Prohibit all imports of goods made from forced labour
	No conditionality	Passage of the agreement conditioned on labour reforms in Vietnam	Passage of the agreement conditioned on labour reforms in Mexico
	No wage requirement	No wage requirement	Wage requirement in auto rules of origin
Institutions	Commission for Labour Cooperation with Council and Secretariat	Labour Council	Labour Council
	National Administrative Office	Labour Cooperation	Labour Cooperation
	Evaluation Committee of Experts	Labour Dialogue	Labour Dialogue
	Arbitral Panel	Committee of Experts (side agreement)	Rapid-Response Labour Mechanism (RRM)
		Government review (side agreement)	Interagency Labour Committee for Monitoring and Enforcement (implementation bill)
		ILO assistance (side agreement)	Independent Mexico Labour Expert Board (implementation bill)
Enforcement	Not covered by state-to-state DSM; labour-specific panel.	Covered by state-to-state DSM	Covered by state-to-state DSM and RRM
	Rules related to child labour, minimum wage, health and safety	All labour rules (including side agreements)	All labour rules for state-to-state, collective bargaining and freedom of association for RRM.
	Sanctions up to 0.07% of total trade.	Trade sanctions or compensation of up to 50% of the benefits the panel has determined	Trade sanctions. In the case of RRM, up to denial of entry of goods at the border
	Violations must be 'trade-related'	Violations must be 'in a manner affecting trade or investment'	Violations must be 'in a manner affecting trade or investment', but footnotes loosen the requirement and reverse the burden of proof

Source: Author's own.

USMCA's unprecedented labour provisions can be used for both protectionist and developmental purposes. The next section argues that the US government included those provisions for protectionist purposes, while the López Obrador government accepted them to lock in its labour reform.

7.3. The Renegotiation

7.3.1 Protectionist US Intentions

The provisions in USMCA and the testimony of interview respondents both point to protectionism as the main driver of the US negotiating strategy on labour standards. At the start of the negotiations, the Trump administration was not interested in pushing for stronger labour standards in the trade agreement. Mexican chief negotiator Kenneth Smith Ramos recalled that, initially, Mexico and Canada were most active in designing a labour chapter subject to dispute settlement:

> The US in reality took sort of a backseat to the discussion, which over the first few rounds was basically with Canada. Canada itself had a lot of disagreements with the United States, because Canada felt, as we did, that this should not just be something that focuses on a country in particular: this notion that when you talk about labour rights, it all has to be about Mexico. I mean, that's completely false. Canada has quite a few issues with the US in terms of their enforcement of labour laws, the fact that some states call themselves 'right-to-work states' and have more lax provisions. There's quite a bit of de-unionization in the United States, companies moving to the southern states rather than traditional Midwest, unionized states. Enforcement in the agricultural sector of labour laws in the US is terrible. And that's something that Mexico has dealt with with the US quite a bit, with all the migrant workers that we have working there (interview, 16 October 2020).

Mexican negotiators demanded better enforcement of labour laws in the US, especially for migrant workers employed in the agricultural sector. The Canadian government proposed ambitious negotiating objectives on labour rights, including concerns over de-unionisation in

the US, especially in 'right to work' states which prevent employees from negotiating contracts requiring all workers to unionise (Canadian negotiators, interviews, 5 March 2021). The Trump administration conditioned acceptance of certain demands on Canada making concessions in other issues, however, leading Canadian negotiators to abandon some of their proposals (Canadian diplomat, interview, 21 October 2020). Most notably, the Canadian government renounced its priority to include a chapter on indigenous peoples' rights, although it obtained a provision guaranteeing the right to adopt or maintain measures 'to fulfil its legal obligations to indigenous peoples' (USMCA Article 32.5).

Although USTR Robert Lighthizer and his staff regularly met with US labour union representatives to hear their concerns over NAFTA, Trump's lack of interest in labour standards was evident in his domestic policies which weakened the power of unions. A US labour union representative interviewed highlighted some of those policies, as well as Trump's appointment of anti-union personalities to the National Labour Relations Board (NLRB), the US independent federal agency tasked with enforcing labour law:

> The reason why we get into trade policy is not just for the sake of trade policy, it's for a broader goal of trying to have better jobs in the US and have a stronger middle class. And so we look at trade as one mechanism. Then you look at something like tax law, you look at labour laws, and one of the problems that we had was while there was some receptivity, an alignment on trade with the previous (Trump) administration, they were completely on the opposite side on everything else […] And if we're talking about trying to raise wages here, we had an NLRB that was extremely hostile to workers. I think it would be hard-pressed to find more than one or two decisions that were favourable to workers from the NLRB, that were mostly Trump nominees (interview, 17 March 2021).

Instead of improving labour standards in Mexico, the main objective of the Trump administration was to bring back manufacturing jobs to the US. To do so, USTR Lighthizer initially favoured openly protectionist negotiating objectives such as voluntary export restraints and US-specific rules of origin for the auto industry. As highlighted by a Canadian negotiator:

> The Trump administration's approach was not to enhance labour standards in Mexico. Their objective was to make it as hard as possible for Mexico, and in some cases maybe Canada, to participate in or benefit from economic activity involving the US (interview, 5 March 2021).

Once it became clear that his initial demands would not be accepted, the Trump administration resorted to labour standards as a means to increase the costs of producing in Mexico. According to a Trump administration official:

> We're going to level the playing field by making sure that there are unions in Mexico to raise the cost of doing business. So then, when you're a US manufacturer, you think: "Well, I could go to the United States or Mexico. Mexico used to be low wage, but now they have unions so wages are increasing, might as well stay in the United States." That was our calculation. We want people to get good wages and we want wages to rise in Mexico, which with unions would help (interview, 10 March 2021).

Similarly, a Congressional Democrat argued that NAFTA made workers on both sides of the US-Mexico border worse off as Mexican workers could not enforce their labour rights, leading to factories moving to Mexico to benefit from repressed wages (interview, 23 October 2020). Although both Democrats and Republicans pushed for labour standards for protectionist motives, they also considered the likely developmental effects of such provisions in Mexico.

The Labour Value Content (LVC) automotive rule of origin, however, was included for purely protectionist motives. It requires that at least 40/45 per cent of the value of an auto/truck has to be produced by direct production workers earning on average at least 16 dollars per hour. According to a US negotiator, the rule was specifically designed to prevent offshoring to Mexico:

> That's going to be the big thing that will keep production in the United States, or even cause future production facilities to be built in the United States that otherwise would likely have gone to Mexico or to Canada […] What a lot of Mexican manufacturers might choose to do is say: "Look, we're going to be the part of your production that is not high value. We're going to make ball bearings and pay people 4 dollars an hour because 4 dollars an hour is sufficient in Mexico for our employees, they're willing to

> accept that number. And yes, we will meet the LVC. […] But we don't have to be the high-value labour country" (interview, 14 October 2021).

By imposing an average wage five to eight times higher than average wages in Mexican auto factories, the Trump administration sought to ensure that the high-value content in automobiles would be produced in the US (Menck and Swiecki 2016: 32). A US union leader also argued that the LVC was included in USMCA to bring back jobs to the US rather than improve labour conditions in Mexico:

> They (US negotiators) wanted to use some more blunt instruments like that (LVC) because, in all candour, labour rights can help bring back jobs by levelling the playing field, but it will be a long process, even if it succeeds (interview, 2 April 2021).

Democrats supported the LVC for the same reasons. Many Democrats had already criticised the Trans-Pacific Partnership (TPP), negotiated under Obama, for its weak rules of origin in the auto industry, which would have facilitated offshoring. Although the Trump administration had an unconventional approach to rules of origin, Democrats were 'sympathetic' to the goals of the LVC and also found NAFTA to be 'out of balance' (Democrat trade official, interview, 23 October 2020). A negotiator in the Trump administration similarly argued that their objectives were closer to those of Congressional Democrats than representatives of the Republican Party:

> When you talk about the House Ways and Means Committee on the Republican side, very free trade fundamentalists, open borders at all costs. And then on the Democratic side, Katherine Tai, for example, more pragmatic, actually viewed trade more like we did (interview, 10 March 2021).

Katherine Tai, who played a key role in negotiating the USMCA amendments as chief trade counsel for the US House Committee on Ways and Means, became USTR in the Biden administration. Congressional Democrats diverged with the Trump administration, however, in wanting an operational dispute settlement mechanism to address labour rights violations. Canadian and Mexican negotiators were also favourable from the start for fixing the dispute

settlement system, while USTR Lighthizer preferred to maintain the DSM dysfunctional and incentivise enforcement through unilateral sanctions. To push back against members of the US Congress demanding an operational DSM, Robert Lighthizer argued that he could use US Section 301 tariffs (against 'unfair' trade practices) to unilaterally sanction labour rights violations in Mexico (Rodriguez 2019). Although USTR had never taken this approach before, it had been recommended by the AFL-CIO as early as 2004 to mitigate 'unfair' competition from China (Luce 2005: 6).

During the renegotiation of USMCA following the Democratic Party's victory in the 2018 House midterm elections, the Trump administration continued to oppose the fixing of the dispute settlement mechanism. It ultimately accepted, however, to obtain Congressional Democrats' support for USMCA, which was necessary given that they controlled the House of Representatives. According to Jesús Seade, Mexican chief negotiator for President López Obrador:

> The Democrats wanted something horrible, which was inspectors, the Republicans (Trump administration) wanted something horrible, which was no proper dispute resolution system. We found a way to put those two together […] and what resulted was that they first proposed to have a proper dispute resolution system for labour issues (interview, 15 October 2020).

The Trump administration ultimately agreed to fix the dispute settlement system so that it covered all trade issues, including the labour chapter (cf. section 5.4.5).

The labour chapter itself was also subject to amendments as Democrats conditioned the passage of USMCA in Congress on adding provisions, including some which impact the working of the state-to-state DSM and can serve protectionist interests. Footnotes to Article 23.3 facilitate the imposition of trade sanctions for labour rights violations by loosening the interpretation of 'in a manner affecting trade or investment' and reversing the burden of proof on this issue from the complaining to the responding government (cf. Section 7.3). Mexican negotiators from the

Peña Nieto administration argued that some of the amendments to USMCA agreed by the López Obrador administration, including the last footnote, expose Mexico to protectionist US policies. According to Mexican chief negotiator Kenneth Smith Ramos:

> The new Mexican government accepted a set of provisions that I think go beyond what was necessary, simply because they lend themselves to abuse from the part of anybody who wants to manipulate the mechanism. Throughout, from the beginning of NAFTA, and in many other trade agreements that we've dealt with, you have to find a balance between helping to defend labour rights and not opening the door for labour provisions to be used as protection tools, basically to block out the access for key industries. And that was our concern (interview, 16 October 2020).

The Rapid Response Labour Mechanism (RRM) is the amendment accepted by the López Obrador administration which is most decried by negotiators in the Peña Nieto administration as having the potential to be used by the US for protectionist purposes given its asymmetry (Annex 31-A). The RRM was proposed by Democratic Senators Ron Wyden and Sherrod Brown and elaborated in tandem with USTR officials (interviews with USTR and Democrat officials, 26 February 2021, 10 March 2021). Although the RRM applies in theory to both Mexico and the United States, a footnote to Article 31-A.2 specifies that claims against the US can only be brought against 'a covered facility under an enforced order of the National Labour Relations Board' (NLRB). An enforced order of the NLRB can take years of appeals, however, and the NLRB only produces approximately 50 enforced orders per year, of which many do not concern trade, which greatly restricts the choice of cases for Mexico (Compa 2022). The choice of cases is further restricted by the fact that the RRM does not cover agriculture, which is the sector where violations of Mexican migrant workers' rights in the US are most rife (Nolan García 2022). A similar footnote is present in the Canada-Mexico RRM restricting cases that can be brought against Canada (Article 31-B.2). The asymmetry in the working of the RRM facilitates its use for protectionist purposes. It also reveals the US government's hypocrisy given

that it refused to be subject to the same mechanism, despite the prevalence of worker rights violations in the US (Costa, Martin, and Rutledge 2020).

7.3.2. Locking-in the Mexican Labour Reform

Although the Trump administration and US Democrats demanded stronger labour provisions in USMCA for protectionist reasons, they were aware that those could also help the incoming Mexican government lock in its ambitious labour reform. López Obrador (2018-2024) was the first left-wing Mexican President since Lázaro Cárdenas (1934-1940) and had campaigned against Mexico's century-old labour relations system. This system consisted of 'protection unions' controlled by businesses and the PRI party, which had governed Mexico during most of the twentieth century. Although former PRI President Peña Nieto (2012-2018) pushed for labour law reform from the start of his presidency, he faced opposition from his political party, which had close links with protection unions (Israel 2012). Changing Mexico's labour system was difficult given that it required a constitutional reform: the tripartite boards controlled by protection unions were established by the 1917 Constitution (Article 123-XX). A constitutional reform required a two-thirds majority in both Mexican Houses of Congress and the support of a majority of Mexican states.

From 2012 to 2015, Mexico faced US pressure to reform its constitution as it joined negotiations over the Trans-Pacific Partnership (TPP). The US requested a side agreement to the TPP on Mexico's labour reforms (just as it was negotiating one with Malaysia, Vietnam, and Brunei), but this was rejected by Peña Nieto's government because it infringed national sovereignty (Bensusán and Middlebrook 2020: 1008). Although the Obama administration renounced its demand for a side agreement, it continued during the negotiations to press the Mexican government for constitutional labour reform.

Under Peña Nieto's presidency, the Mexican Congress reformed the country's constitution to better protect workers' rights to freedom of association and collective bargaining. The 2017 reform, approved overwhelmingly by both Houses of Congress, terminated 'Conciliation and Arbitration Boards', the tripartite organisations representing the government, labour, and employers, often used by the latter to influence the selection of labour unions and their activities (Bensusán and Middlebrook 2020: 1017). Arbitration was to be conducted instead by federal and local labour courts, which necessitated reforming the Mexican justice system, while conciliation would be implemented by 'specialised and impartial' federal and local conciliation centres (Clewer et al. 2017: 6-7).

Peña Nieto's constitutional reform required a bill in the Mexican Congress to be implemented. The Peña Nieto government faced opposition from the business sector and its political party (the PRI), however, which undermined its willingness and ability to enforce the 2017 constitutional reform. Senators González Cuevas and Medina Ramírez from the PRI proposed a reform bill in 2017 which created new institutions to maintain the status quo. Instead of tripartite boards, a new 'technical council' in charge of registering unions would be composed of unions, employers, and government: tripartism all over again (Bensusán and Middlebrook 2020: 1018-9). This change was denounced by opposition parties in Mexico, as well as in the United States by both Democrats and USTR Robert Lighthizer (Ibid.: 1023-4).

It is unclear the extent to which the Peña-Nieto government was committed to enforcing the labour reforms. Although it expressed support for Mexico's commitments in Annex 23-A (Compa and Brooks 2019: 245), it did not present adequate legislation to implement the changes to the Mexican constitution. Accepting Annex 23-A was also a policy change compared to the TPP, where the government had refused any side agreement conditioning the trade agreement on labour reforms. US chief negotiator John Melle recalled that although Peña Nieto negotiators 'had accepted NAFTA (labour) provisions and were willing to strengthen the dispute

settlement, there's not much they did like about anything that we proposed in the USMCA' (interview, 16 December 2020).

By contrast, there is considerable evidence that USMCA was used by the López-Obrador government to lock in its labour reforms, just as NAFTA was used 25 years earlier to lock in economic liberalisation. The incoming López Obrador administration was much more open to new labour provisions and willing to enforce the 2017 constitutional reform. Two other factors affected its negotiating position. First, it faced higher pressure to make concessions on labour as Democrats conditioned passage of USCMA through Congress on new labour provisions. Second, a change in negotiating capacity between the Peña Nieto and López Obrador administrations contributed to the asymmetric labour provisions discussed above. While the Peña Nieto administration had a well-staffed negotiating team, López Obrador appointed one person, Jesús Seade, to be in charge of the negotiations. Mexican government officials, business representatives, and labour law experts interviewed argued that this factor influenced the negotiation dynamics. Similarly, US chief negotiator John Melle recalled that:

> One of the impacts of the NAFTA was that Mexico had a core of negotiators trained in the NAFTA that also went out and negotiated a lot of other free trade agreements for Mexico. So they had a core technical team that was very good, very experienced. AMLO did not have a team, he had Jesús Seade. […] I think the outcome reflects that (interview, 16 December 2020).

Beyond those two factors, the pro-labour position of the Andrés Manuel López Obrador (AMLO) administration made it more receptive to stronger labour standards in USMCA. López Obrador had campaigned on an anti-neoliberal platform, arguing that the Mexican people's rejection of neoliberal policies contributed to his victory in the 2018 elections:

> Another element that explains the defeat of the neoliberal camp in 2018 is the proposal, contained in embryonic form in the 2018-2024 National Project, to build a new social pact capable of containing and overcoming the mess to which the country has been led (Gobierno de Mexico 2019b, translated from Spanish).

López Obrador pledged to progressively double the minimum wage during his campaign, which he surpassed. Between 2018 and 1 January 2024, the daily minimum wage nearly tripled from 88 pesos to 248 pesos (Associated Press 2023). At the northern border, the minimum wage increased to 375 pesos per day in 2024, which is the equivalent of 21.50 dollars per day (still far from the 16 dollars per hour average wage rule of origin in the auto sector) (Ibid.). During his time as president-elect, López Obrador also confirmed to the US administration that he planned to implement reforms breaking with the century-old Mexican labour justice system undermining workers' rights to freedom of association and collective bargaining. The first paragraph of Annex 23-A states:

> Mexico shall adopt and maintain the measures set out in paragraph 2, which are necessary for the effective recognition of the right to collective bargaining, given that the Mexican government incoming in December 2018 has confirmed that each of these provisions is within the scope of the mandate provided to the government by the people of Mexico in the elections.

Strong and easily enforceable labour standards in USMCA provided an opportunity for López Obrador to incentivise recalcitrant businesses and state governments to implement his labour reforms. His chief negotiator, Jesús Seade, recalled:

> The strong (labour) obligations created by USMCA were something that the President told me directly and very clearly: that is fine. It will only help us come forward, roll out the labour reform. So that is not a problem. If there are cases, let them come, and if there is merit, we will address it because it is part of the labour reform. That was something that was very much part of his agenda politically for 20 years or so. He was unhappy with the very archaic labour regime we had for decades and decades in Mexico (interview, 27 March 2023).

Speaking of the RRM, a Canadian negotiator concurred with this interpretation:

> The Mexican government, while it was maybe offensive, in some ways, they also probably liked the fact that it was an extra tool that can be used to get businesses or maybe state governments to play ball on something that is difficult in Mexico (interview, 5 March 2021).

Indeed, López Obrador's pro-labour agenda also faced opposition from Mexican states and the business sector, who wanted a weaker labour reform bill. According to an official in the Peña-Nieto government:

> I think everybody understood that Mexico had an arcane, old and unacceptable legal framework that needed to be changed. But then what happened is that the new Mexican administration, the AMLO government, was even more enthusiastic about these changes. And they (labour standards) were part of his program. What the election did was to reinforce the momentum towards these changes. And the private sector was still trying to prevent some of the changes, at least at the margin. [...] Clearly AMLO and his team gave a lot of momentum to what the Trump administration wanted. And the AMLO government and the AMLO team and Bob Lighthizer's office were completely aligned in making these changes happen (interview, 7 April 2021).

By committing Mexico to a radical reform of its labour justice system in USMCA Annex 23-A, López Obrador facilitated the politics surrounding the passage and implementation of his bill. He used the US government's pressure to rally support, stating in a public conference that 'a labour reform must be passed in line with the agreements that were established in the treaty; we do not want to give (the US) any reason to reopen the negotiations' (Díaz 2019, translated from Spanish). Nancy Pelosi, Speaker of the US House of Representatives, had clearly stated that USMCA would not be adopted until Mexico passed a labour bill consistent with Annex 23-A. The Mexican labour reform bill was passed in May 2019 with overwhelming support in the Mexican Chamber of Deputies and unanimously in the Mexican Senate (Camara de Diputados 2019; Campbell 2019).

The role of USMCA Annex 23-A in locking in the Mexican labour reform is also evident from their common language (Gobierno de Mexico 2019). For instance, Annex 23-A states that workers must express their choice through a 'personal, free, and secret vote', and requires employers to provide their employees with a copy of their collective bargaining agreement. The Mexican labour law specifies that voting must be conducted in a 'personal, free, direct and

secrete vote' (Article 371), and requires employers to 'deliver to their workers, free of charge, a printed copy of the initial collective bargaining agreement, or its revision within fifteen days after such agreement is deposited with the Federal Centre for Labour Conciliation and Registration' (Gobierno de Mexico 2019: Article 132 XXX, translated from Spanish).

Some provisions in the Mexican labour law reform reproduce nearly word for word the requirements in USMCA Annex 23-A. For instance, clause (f) in Annex 23-A requires that:

> All existing collective bargaining agreements shall be revised at least once during the four years after the legislation goes into effect.

The reform of the Mexican Labour Law, approved on 1 May 2019, states that:

> Existing collective bargaining agreements shall be revised at least once during the four years after the entry into force of this Decree (Gobierno de Mexico 2019: Transitional Article 11, translated from Spanish).

By locking in his labour reform agenda in USMCA, the López Obrador administration sought to ensure rapid change and lower resistance from Mexican states and the business sector. Requiring new trade union elections across Mexico within four years of the reform bill created pressure to rapidly alter the previous arrangement of 'protection unions', by contrast to the mostly symbolic measures of the previous administration.

Similarly, the López Obrador administration favoured an operational dispute settlement mechanism to enforce the USMCA labour chapter given that it would incentivise Mexico's business sector and political elites to comply with the labour reforms. López Obrador's chief negotiator, Jesús Seade, had to resist 'huge pressure' from the US to accept US labour inspectors operating in Mexico, and pushed instead for the creation of a dispute settlement system which would cover labour:

> You (the US) want enforcement of labour issues. Good for you. We also want enforcement of labour issues. But if you want to have an instrument to force us, we aren't going to give inspectors. What we can give you, what we want to give you, is a proper dispute settlement system (interview, 15 October 2020).

Mexico sided with US Democrats and Canada against the Trump administration on the creation of a state-to-state DSM, which was included in the amended USMCA. For both Mexican governments involved in the negotiations, an operational state-to-state DSM was essential to ensure disputes with the US could be settled in court, by contrast to the US blocking the DSM under NAFTA. Both Mexican administrations also agreed that the DSM should cover the labour chapter. The López Obrador administration went further, however, by accepting the creation of the Rapid Response Labour Mechanism. While labour disputes adjudicated through the state-to-state DSM can take years, the RRM targets specific factories and provides a resolution within a few months.

7.4. Developmental Effects?

The first three years of USMCA provide an opportunity to assess the developmental effects of its labour provisions, measured in terms of impact on labour conditions (freedom of association, collective bargaining, wages) and Mexico's access to the US market. In addition to the ex-ante effect of facilitating the passage of the Mexican labour reform, USMCA labour provisions had ex-post effects on labour conditions due to US support for the implementation of Mexico's labour reform and use of the Rapid Response Mechanism. As to Mexico's access to the US market, it remained stable during the first three years in large part due to the López Obrador administration's commitment to address cases raised by the US. The auto industry also played an important role during the negotiations to ensure the Labour Value Content (LVC) auto rule of origin would not undermine investments in Mexico (cf. section 5.4.3.).

USMCA helped the López Obrador administration lock in its labour reform, yet implementation still proved difficult as it required overhauling a hundred years of labour relations. At the start of the reform, the Mexican Labour Ministry estimated that 80 to 85 per cent of unions were 'protection unions' (Associated Press 2020). The reform attributed incumbent unions the authority to schedule the new vote, generating an obvious conflict of interest. Many abuses were documented, including incumbent unions threatening to withhold benefits should they be ousted or bribing workers to send them a picture of their vote (IMLEB 2023). By the end of the four-year implementation period, approximately ten per cent of contracts had been legitimated, which represented around half of all Mexican union members (Ibid.). Only two per cent of all the legitimisation votes resulted in the rejection of the collective bargaining agreement (Maquila Solidarity Network 2023). Despite the Mexican administration's efforts, 'protection unions' often continued to violate worker rights to freedom of association and collective bargaining, while many workers remained unaware of their rights (Bensusán, Valdenebro, and Nicolas 2022).

Given the limited enforcement capacity of the Mexican government, US support for the implementation of the labour reform facilitated improvements in labour conditions. By contrast to labour standards in previous US PTAs, which suffered from limited resources devoted to support and enforcement, the USMCA implementation bill included 180 million dollars in technical assistance over four years to implement Mexico's labour reform, the creation of an 'Independent Mexico Labour Expert Board', funding for five US labour attachés in Mexico, and the creation of a 'hotline' to collect anonymous testimonies of Mexican workers victim of denial of rights (US Department of Labour 2022). The bill established the Interagency Labour Committee for Monitoring and Enforcement, regrouping staff from USTR and the US Department of Labour's Bureau of International Labour Affairs. Giving monitoring authority to the Department of Labour broke with past US practices of giving this authority to the

Department of Commerce, which was typically more concerned with addressing the demands of businesses rather than unions. Table 9 summarises the ex-post effects of USMCA relative to the RRM during the first three years.

TABLE 9. US-RAISED RAPID RESPONSE LABOR MECHANISM CASES (JULY 2020-JUNE 2023)

Date of initiation	Facility	Industry	Results (non-exhaustive)
May 2021	General Motors, Silao, GTO	Auto	August 2022: workers at the facility vote to reject their collective bargaining agreement. February 2022, workers elect an independent union. May 2022/May 2023: 8.5/10 per cent wage increase.
June 2021	Tridonex, Matamoros, TLP	Auto	August 2021: the US reaches a side agreement with Tridonex, including more than $600,000 of severance pay and commitments to ensure freedom of association. February 2022: workers elect an independent union.
May 2022	Panasonic Automotive Systems, Reynosa, TLP	Auto	July 2022: workers elect an independent union. The facility offers back pay and reinstatement to workers fired for unionising, reimburses workers for wages unpaid, and increases wages by 9.5%. February 2023: wage increase of 11.9%.
June 2022	Teksid Hierro, Frontera, CHL	Auto	July 2022: Teksid pays union dues to the union, and reinstates fired workers with back pay. September 2022: workers elect an independent union. February 2023: wage increase of 9%.
July 2022	Manufacturas VU, Piedras Negras, CHL	Auto	August 2022: the Mexican government commits to ensure a free election in the facility. September 2022: workers elect an independent union.
Jan 2023	Manufacturas VU, Piedras Negras, CHL	Auto	March 2023: the Mexican government commits to initiate sanctions proceedings; and the company to take action against staff that violated worker rights. October 2023: VU announces plant closure.
March 2023	Unique Fabricating, QRO	Auto	April 2023: The company signed an agreement with a new union and provided it with dues from its affiliates.
May 2023	Goodyear, SLP, SLP	Auto	May 2023: workers vote out existing union.
June 2023	Draxton, GTO	Auto	July 2023: the Mexican government commits to a plan of remediation.
June 2023	Industrias del Interior, AGS	Textile	July 2023: the Mexican government commits to a plan of remediation.
June 2023	Grupo Mexico San Martin, ZTC	Mining	To be determined. (US requested a panel in August 2023)

Source: Author's own.

During the first three years of USMCA (July 2020-June 2023), the US government requested eleven reviews of labour rights violations in Mexico concerning collective bargaining and freedom of association (three alone in the last month), and the Canadian government one. By the end of 2023, another eight cases had been raised by the US, raising the total to nineteen. Those reviews led to swift action by the Mexican government to address concerns raised, and in one case (Tridonex) a side agreement between the US and the exporting firm (IMLEB 2023; USTR 2023a). In another case (VU Manufacturing), the company chose to close the plant rather than comply with the remediation plan, which points to the unintended consequences that USMCA labour provisions can have on Mexican workers (Bown and Claussen 2023).

The second case illustrates power asymmetries and differences in interests between the US and Mexico. Following the US government's request, the Mexican government conducted a review of labour rights violations in Tridonex but concluded that 'since the events in question occurred before the entry into force of the Treaty, there was no denial of rights for the plant workers as provided for in the USMCA' (Gobierno de Mexico 2021, translated from Spanish). The general interpretation of international treaties is that they are not retroactive: although the plant had laid off workers for unionising, this did not constitute a denial of rights given that the events occurred before USMCA entered into force (Matos and Kryvoi 2021). By contrast, the Biden administration argued that the RRM could be applied retroactively:

> We have a different interpretation. Our interpretation is the agreement says "denial of rights". So if some particular event occurred at some period of time in the past, whenever it may have been, and there still is a present denial of those rights, it doesn't matter when the triggering action occurred, it matters whether there's a denial of rights. That's what the agreement says. So, if it hasn't been remedied, that still exists and it's fair game (Biden administration official, interview, 23 September 2021).

Although the López-Obrador administration used USMCA labour standards to force the implementation of its labour reform, it also sought to prevent the US from infringing on

Mexico's national sovereignty. This did not deter the US government, however, which persisted in its retroactive interpretation by negotiating directly with the parent company of Tridonex:

> The conversation with the company just seemed the most fruitful route to get meaningful results. And there's 600,000 dollars for workers during a pandemic, who are out of work, who needed the money. We just thought that was the best way to get meaningful results. The time periods involved in this went back pretty far in terms of statutes of limitations, and this is a state that hasn't gone through Mexico's labour reform yet. So it was still in the old labour justice system that is being overhauled for a reason, because it's broken. And so rather than just tie our fate to that system and have it drag on for months or years, this just seemed like the result that was gonna be the most positive and the most meaningful for workers. So that's the route we took (interview, 23 September 2021).

This disagreement resurfaced in the Grupo Mexico San Martin case. The Mexican government refused to conduct a review, arguing that the alleged denial of rights at the plant could not be investigated by the RRM given that they occurred before USMCA entered into force (Secretaría de Economía de México 2023). The US government rejected this interpretation and in August 2023 requested the first RRM panel.

Even if a panel finds a denial of rights, the RRM is unlikely to lead to a significant loss of market access given that it targets specific firms. By the same logic, it is also unlikely to lead to improvements in labour standards across the Mexican economy. Well-known brands are most likely to comply with labour laws to avoid the negative publicity of an RRM case. As to the use of the RRM by the US to create market access uncertainty, it is mitigated by USMCA Article 31-A.11 which authorises a country to request a state-to-state DSM panel. If the panel finds that the responding government has not used the RRM 'in good faith', the complaining government can choose to prevent the responding country from using the RRM for two years. A ruling by the state-to-state DSM over labour rights violations could be more effective in reducing market access, yet the US government has so far privileged the RRM, which provides quick and visible results and enables sanctions to be targeted at the firm violating labour rights.

7.5. Conclusion

Whereas the Trump administration demanded the inclusion of unprecedented labour provisions in USMCA for protectionist purposes, President López Obrador used them to lock in his ambitious labour reforms, just as NAFTA was used in the 1990s by President Salinas de Gortari to lock in trade liberalisation (Cameron and Tomlin 2000). Despite protectionist US efforts leading to the threat of loss of market access, USMCA labour provisions did not reduce Mexico's access to the US market during the agreement's first three years while generating limited improvements in labour conditions. This is due to a combination of US political will to enforce USMCA labour provisions, Mexican political will to address issues raised by the US, and the successful efforts of the auto industry to ensure the LVC would not undermine investments in Mexico.

While USMCA labour standards already had some developmental effects in the Mexican export sector, the informal sector may be negatively affected if higher wages reduce demand for maquila workers (Levy and Fentanes 2022: 71-72). Workers not employed in the export sector are likely to have informal jobs, yet USMCA labour provisions do not address the regulatory framework in Mexico incentivising informal activity. In 2018, nearly 60 per cent of Mexican workers were in the informal sector (Ibid.: 70). Furthermore, labour standards alone are unlikely to raise productivity growth in Mexico, which has been anaemic during NAFTA outside of the export sector (Blecker 2019). This preliminary assessment of the developmental effects of USMCA labour provisions in their first three years, based on interviews with stakeholders and government reports, needs to be complemented in due time with a quantitative analysis focusing on both intended and unintended effects (Alfaro-Urena et al. 2022; Bown and Claussen 2023).

As to the risk that USMCA labour standards will be used by the US to reduce Mexico's access to the US market, it is mitigated by the fact that the US has far more effective protectionist tools

at its disposal. Chapter Four demonstrated that the US can reduce Mexico's market access or undermine market access certainty through a variety of non-conventional threats and trade laws, such as national security tariffs, trade remedies and emergency acts. Furthermore, USMCA labour standards can reduce protectionist sentiments in the US by reducing workers' perception that the trade agreement promotes 'unfair' trade practices. This is attested by differences in levels of support between NAFTA, the first USMCA (signed in 2018) and the final USMCA with the labour enforcement amendments (signed in 2019). While NAFTA and the first USMCA faced a divided Congress and no support from US labour unions, the final USMCA text received widespread bipartisan support and was endorsed by many labour unions. The concluding chapter includes reflections on the policies which, combined with USMCA labour standards, could promote wage convergence in North America.

Chapter 8. Conclusion

> *Many companies in the United States approach us (the Mexican government) as they see us as a reliable partner, a partner that thanks to the USMCA has greater certainty compared to other countries in the world, especially in the context of the Trump administration. They see Mexico as a partner that has already, in some way, passed the test in the United States because we already have a modernized agreement, a new agreement.*
>
> Mexican official, López Obrador administration, interview, 2 December 2020

> *I don't see any reshoring within the USMCA region. Reshoring is from outside of that region into the region, not necessarily between the three countries. […] Both the rules around USMCA and the geopolitical environment are going to force companies to rethink how they supply certain markets. You will see more localised parts sourcing within the USMCA region for both of those reasons.*
>
> Auto industry representative, interview, 16 November 2020

This final chapter first provides a summary of the argument and details the three main research contributions of this thesis. It then outlines the future research agenda: developing the theoretical model to cover other cases of 'hostile' trade renegotiations, and analysing the evolution of US trade policy, especially during the USMCA's first review period in 2026. It concludes by providing policy reflections based on the findings, focusing on the possible development strategies of the global South in light of the consolidation of regional economic blocs.

8.1. Summary of the Argument

The forced renegotiation of the North American Free Trade Agreement (NAFTA) between 2017 and 2019 unravelled norms of market access stability provided by previous US preferential trade agreements. The Trump administration imposed national security tariffs on Mexico and Canada, threatened to unilaterally withdraw from NAFTA, and proposed protectionist negotiating objectives such as a five-year sunset clause, a requirement that 50 per cent of the value of autos be manufactured in the US to be exempt from tariffs, and the elimination of all dispute settlement mechanisms. Although the Trump administration failed to impose its initial negotiating objectives, the new US-Mexico-Canada Agreement (USMCA) sets precedents, such as a six-year review period and sixteen-year sunset clause, a labour rights enforcement mechanism in practice only enforceable in Mexico, and a 16 dollars per hour average wage rule of origin for parts of the auto sector.

This first case of a preferential trade agreement renegotiation raised important questions. First, the preferences of actors changed compared to those during the signing of NAFTA in the 1990s. US Congressional Democrats and labour unions, once vocal opponents of NAFTA, lobbied the Trump administration to reform rather than withdraw from the agreement. In Mexico, President López Obrador, who historically opposed NAFTA, also supported the agreement. In Canada, labour unions and the Liberal party sought to preserve NAFTA, whereas they had led opposition to trade liberalisation in the 1980s and 1990s, influenced by the nationalist economic policies of Justin Trudeau's father, Pierre. Second, the renegotiation was marked by a power paradox: despite the large US power asymmetry with Mexico and Canada, the Trump administration was not able to impose any of its initial negotiating objectives.

Theoretically, the thesis engaged with two disciplines, international relations and international development, to understand how NAFTA shaped actors' preferences and power to renegotiate

the agreement. It integrated historical institutionalism into the two-level game framework, identifying two path dependence mechanisms which conditioned negotiators' interactions with their counterparts (Level I) and domestic actors (Level II). First, increasing economic returns reinforced the power of exporters and changed the preferences of NAFTA opponents. By closely integrating industries such as autos, NAFTA rendered the jobs of many US workers dependent on the effective functioning of North American supply chains. Second, Congressional veto power over the decision to withdraw from or enter a new trade agreement undermined Trump's capacity to alter NAFTA. Institutional stability was reinforced by firms and citizens voicing their preferences by lobbying and voting, respectively. Combined, increasing returns and veto power ensured that Mexico and Canada's efforts to preserve the trade agreement superseded the Trump administration's disruptive negotiating strategy and protectionist objectives. Faced with the costs of withdrawing from NAFTA, Trump chose to pursue more modest changes to the agreement.

The international development literature helps understand the Trump administration's protectionist turn and evaluate the developmental effects of NAFTA and USMCA. Two chapters outlined the causes of the renegotiation. Chapter Two contrasted the predictions of US-Mexico wage convergence provided by NAFTA advocates with the warnings from structuralist economists. Absent an industrial policy to insert domestic firms in global supply chains, structuralist economists feared growth in Mexico would remain elusive. Twenty-five years later, Mexico's average wages in the production sector were lower than before NAFTA, the informal sector reached 60 per cent of the workforce, and economic growth remained anaemic (Blecker 2019). US blue-collar workers blamed NAFTA for incentivising multinationals to produce in Mexico and voted for a change. Drawing on structuralist economic theory, the third chapter developed a typology of US trade policies based on trading partners' space for industrial policies and access to the US market.

After WWII, US trade policy was ‘magnanimous’ (1945–70): the US provided open and stable market access while tolerating and even sometimes encouraging trading partners’ industrial policies to catch up technologically. Beginning in 1971, US trade policy became ‘competitive’ as the US sought to protect its workers from import competition while unsuccessfully attempting to restrain trading partners’ industrial policies. By 1991, the US began a ‘restraining’ policy by providing stable access to its market in exchange for restrictions on trading partners’ industrial policies. In 2017, US trade policy globally shifted towards ‘power-based’ as Trump created market access uncertainty while preserving restrictions on trading partners’ industrial policies (a policy maintained by Biden with more diplomacy). Chapter Four demonstrated that Mexico and Canada were largely exempted from this policy approach by signing the USMCA, which preserved the ‘restraining’ trade policy. Although benefiting from US industrial policies (such as subsidies of the Inflation Reduction Act), Mexico and Canada face higher market access uncertainty than before 2017 as the USMCA review periods and sunset clause create opportunities for the US to demand new concessions and threaten the removal of preferential market access.

The historical institutionalist framework is also relevant to the analysis of eras of US trade policy outlined above. At every critical juncture, US presidents were constrained by the policies of their predecessors and the evolution of the global economy. In the 1970s, despite similar economic conditions to the 1930s, US policymakers did not revert to high tariffs given the costs of dismantling post-WWII economic liberalisation. Instead, the US found new strategies such as creating market access uncertainty through trade remedies and non-tariff measures. In the 1990s, constrained by the need to offshore to remain globally competitive, the US secured its firms’ investments abroad by restricting trading partners’ policy space at the WTO and PTAs in exchange for stable access to its market. Between 2017 and 2023, the US remained a member

of the WTO and PTAs while developing novel protectionist policies such as industrial subsidies and national security measures.

Despite NAFTA epitomising the restraining trade policy rejected by Trump, USMCA largely preserved NAFTA provisions and even strengthened North American economic integration. Chapter Five provided an overview of Trump's radical negotiating agenda, focusing on ten negotiating objectives considered unacceptable by Mexican or Canadian negotiators and the negotiation process leading to their abandonment or weakening. It also examined Trump's threat to withdraw the US from NAFTA, arguing that, during the first four months of his presidency, the civil disobedience of White House officials undermined the President's will to execute his threat. In the long run, however, the veto power of Congress and the preferences of voters and businesses reduced his determination to withdraw the US from NAFTA and capacity to achieve his negotiating objectives, as detailed in Chapter Six.

Chapter Seven presented the unprecedented labour provisions in USMCA and argued that they were supported by the US and Mexican governments for different reasons. Whereas the Trump administration and Democrats in Congress had protectionist motives, the incoming López Obrador government accepted the unprecedented USMCA labour provisions as a means to lock in its ambitious labour reform, just as NAFTA had been used by President Salinas de Gortari in the 1990s to lock in trade liberalisation. In their first three years, USMCA labour provisions have contributed to limited improvements in labour conditions in Mexico's export sector without reducing access to the US market. This result is due to a combination of US political will to use the Rapid Response Mechanism (RRM), Mexican political will to address RRM cases raised by the US, and the auto industry's successful lobbying efforts to ensure the Labour Value Content rule of origin would not undermine investments in Mexico.

8.2. Research Contributions

As highlighted in the introduction, the first research contribution of this thesis is empirical: it is so far the only overarching account of the NAFTA renegotiation process drawing on interviews with its actors and stakeholders. Interviews began in September 2020, just three months after the end of negotiations over the rules of implementation of USMCA. The 80 participants of the first round of interviews (September 2020 – December 2021) had a fresh memory of the negotiation process, untainted by the fast pace of politics. Participants in the second round of interviews (March 2023 – June 2023) also provided reflections on the implementation of USMCA in its first three years. This account based on primary sources provides a reference point on the intentions of actors during the NAFTA renegotiation.

The second research contribution is to identify changes in the market access – policy space trade-off characteristic of North-South trade agreements. Since NAFTA, countries in the global South which entered PTAs with the global North obtained *stable* preferential market access at the cost of relinquishing policy space to conduct activist trade and industrial policies (Shadlen 2005). The Trump presidency demonstrated that access to the US market became less stable than before for PTA partners. While USMCA restored market access certainty for Mexico and Canada, the sunset clause laid the foundations for future US attempts to create market access uncertainty. The Peña Nieto government sought to further reduce Mexico's policy space to promote investment certainty, while President López Obrador was unable to regain policy space due to the Mexican government's previous commitments, including policy space restrictions in CPTPP.

This leads to the main theoretical research contribution: by combining the excessively static two-level game framework with the historical institutionalist literature, this thesis analysed how a preferential trade agreement (NAFTA) shaped actors' preferences and power to renegotiate

it. In the two-level game framework, negotiators' win-sets are determined by both negotiating strategies at the international level (Level I) and *preferences* and *institutions* at the domestic level (Level II). In the case of a PTA renegotiation, preferences and institutions are shaped by path dependence mechanisms: increasing returns to economic integration augment the costs of withdrawing from or significantly undermining the PTA, while veto power provides an opportunity for domestic actors to block changes to the PTA. Just as President López Obrador was constrained in his ability to regain policy space, President Trump had to abandon his initial negotiating objectives to consider the preferences of domestic actors and obtain support for USMCA from Congress.

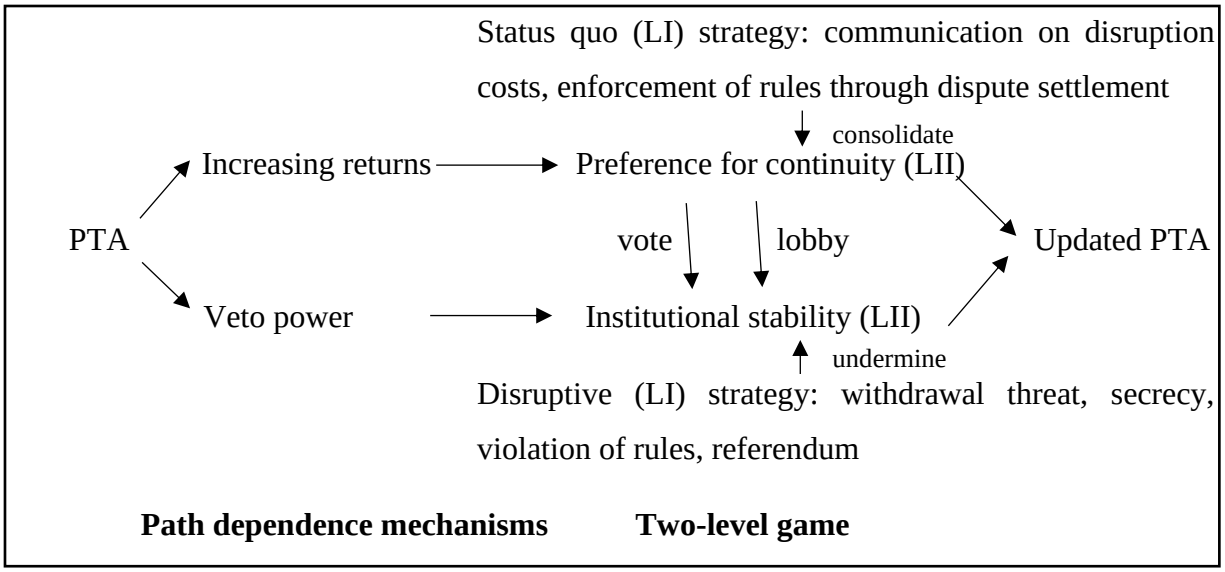
This analysis of a trade renegotiation contributes to the two-level game and historical institutionalist literature. For instance, the traditional two-level game framework predicts that 'when the executive is the most hawkish, domestic politics has *no effect* on the international negotiations […] (and) the legislature cannot exercise any constraint on the executive' (Milner 1997: 79). In a trade renegotiation, however, a hawkish executive will be constrained by domestic politics due to the legislative's veto power: whereas the executive can refuse to sign a PTA approved by the legislative, it requires legislative support to replace that PTA with another and faces constraints on its capacity to withdraw unilaterally from the PTA. As to the historical institutionalist framework, it predicts that power asymmetries beget power asymmetries, creating path dependence (Fioretos 2011: 377; Pierson 2015). In a trade renegotiation, however, path dependence can undermine power asymmetries by constraining the executive's win-set. The Trump administration could not impose its radical negotiating objectives on the Mexican and Canadian governments due to domestic politics. The extent to which this theoretical model can be applied to other trade agreement renegotiations forms part of the future research agenda.

8.3. Future Research Agenda

8.3.1. Towards a Theory of Trade Agreement Renegotiations

The research question of this thesis, centred on the NAFTA renegotiation, can be generalised: how do trade agreements affect actors' preferences and power to renegotiate them? Although NAFTA was the first PTA to be renegotiated, others have followed, such as the EU-Mexico and EU-Chile PTAs in 2020 and 2022, as well as the Brexit negotiations leading to the EU-UK PTA in 2020. However, whereas the NAFTA and Brexit renegotiations were characterised by one country seeking to reduce economic integration, the EU-Chile and EU-Mexico PTA renegotiations were characterised by both parties seeking to deepen economic integration. The model of the NAFTA renegotiation used in this thesis is most relevant to renegotiations where one country seeks to break path dependence, such as the UK seeking to exit from the European Union. Figure 11 generalises the model of the NAFTA renegotiation to other 'hostile' PTA renegotiations, defined as renegotiations where one country implements a disruptive strategy aimed at undermining the trade agreement.

FIGURE 11. MODEL OF A HOSTILE PTA RENEGOTIATION



Source: Author's own.

Although Brexit does not fit well this model given that the UK sought to renegotiate a political and economic union rather than a PTA, it is the only comparison available to date and provides valuable insights on the negotiation dynamics in 'hostile' PTA renegotiations. The UK's disruptive strategy began during the 2015 general elections as Prime Minister (PM) David Cameron pledged to renegotiate his country's relation to the European Union and submit the deal to a referendum. Once re-elected, he negotiated with the EU to reduce UK political and economic integration, seeking 'special treatment' regarding the EU goal of achieving an 'ever closer union', lower contributions to the EU budget, and constraints on freedom of movement, such as introducing the rule that 'if jobseekers have not found a job within six months, they will be required to leave' (BBC 2016). In addition to obtaining the support from Eurosceptics within his party, PM Cameron's pledge to call a referendum formed part of his disruptive negotiating strategy as, by locking his hands, he pressured the EU to make concessions to reduce the risk of a vote for Brexit. The EU largely defended the status quo, however, which led to limited concessions.

Faced with the referendum result, the path dependence mechanisms of increasing returns and Parliamentary veto power could not prevent Brexit but helped maintain free trade with the EU, as the UK Parliament blocked the 'hard Brexit' proposals of Eurosceptic Conservatives (Jones 2020). The UK Parliament passed a motion to reject a 'no deal' outcome, echoing threats from the US Congress to pass 'veto-proof' legislation should Trump attempt to unilaterally withdrawing the US from NAFTA (Ibid.: 55). Just as US business groups and labour unions lobbied Trump to 'do no harm', UK business groups and unions lobbied PM Theresa May to maintain free trade with the EU, warning her that the country was 'facing a national emergency' (Ibid.). The UK Parliament voted three times against proposed withdrawal agreements, leading to the resignation of PM Theresa May. As the UK Parliament refused to vote on a renegotiated withdrawal agreement, PM Boris Johnson successfully won a general election on the platform

'get Brexit done'. The new UK parliament passed the EU Withdrawal Agreement Act on 23 January 2020. Although the UK left the EU on 31 January 2020, it had negotiated a deal and transition period to negotiate a free trade agreement with the EU by 1 January 2021. The EU-UK Trade and Cooperation Agreement was signed on 31 December 2020, replacing UK participation in the EU single market with a free trade agreement. The new agreement largely preserved free trade with the EU, although services were not fully liberalised due to the EU's refusal (Institute for Government 2020).

Brexit demonstrates that the generalisability of the model in Figure 11 depends on the strength of the path dependence mechanisms identified, as well as the weight of non-economic factors during a renegotiation, such as identity, sovereignty, and national security (which are much more prevalent in a political and economic union renegotiation than a PTA renegotiation). Whereas six per cent of Americans believed the US should withdraw from NAFTA (IUST 2017n), the British voted to leave the EU by 52 per cent and gave PM Boris Johnson a mandate to 'get Brexit done'. Testing and developing the model in Figure 11 to provide a framework for hostile PTA renegotiations constitutes the main research agenda. The analysis below provides three hypotheses which can be tested in future research to develop the theory.

First, countries are less likely to withdraw from a regional PTA than non-regional PTAs. Drawing on the first path dependence mechanism, increasing returns, members of regional PTAs face much higher levels of economic integration than members of non-regional PTAs, leading to greater opposition to eliminating the regional PTA. Despite the UK government's promises of signing PTAs with the rest of the world to compensate for the loss of trade with the EU, no deal was strongly opposed by businesses, which stressed that 49 per cent of the country's trade was with the EU in 2017 (BBC 2018). Similarly, while the US has a PTA with both Mexico and Chile, it is much more economically integrated with Mexico. A US President would face less domestic opposition to undermining a PTA with Chile. Levels of economic integration

tend to be greatest in regional blocs, such as in Europe, East Asia, and North America. In addition to USMCA, the most prominent examples of regional trade agreements are the European Union and the PTA between the Association of South East Asian Nations (ASEAN) and Japan. The low salience of PTAs with less economically integrated countries, however, can reduce the incentive to undermine them.

Second, democracies are less likely to withdraw from a PTA than authoritarian regimes, just as they have been found to be more likely to enter into PTAs (Mansfield and Milner 2012). Regarding the second path dependence mechanism, domestic veto power, its strength is stronger in democracies than in authoritarian regimes as the legislative and judiciary are independent from the executive. The US Congress and UK Parliament both used their veto power to force the executive to preserve a trade agreement. In the US, an attempt by the President to withdraw the US from NAFTA by presidential decree would have been challenged in court. In the UK, the Supreme Court ruled illegal PM Boris Johnson's decision to suspend the Parliament in order to undermine opposition to the Withdrawal Agreement he was negotiating (Jones 2020: 38, 65). In addition to separation of powers, other characteristics of a democracy, such as electoral competition and lobbying, also reinforce institutional path dependence. Businesses in the US and UK strongly lobbied against no deal, while trade retaliation contributed to the US Democratic Party regaining control of the House in the 2018 mid-term elections. A democratic referendum, however, created new institutional pressures for change in the case of Brexit. Both increasing returns and veto power were necessary during the NAFTA renegotiation to prevent a US withdrawal from NAFTA, and are likely to be necessary in USMCA review periods.

Third, path dependence is sufficient to preserve a PTA but insufficient to sustain deeper economic and political integration. The key difference between NAFTA and the EU is that the first is a PTA whereas the second is an economic and political union. Even though the UK

retained its currency when in the EU, it had accepted to harmonise tariffs (customs union), allow free movement of labour (single market), elements of an economic union (e.g. adhere to EU sanitary and phytosanitary standards) and of a political union (e.g. adhere to rulings of the European Court of Justice). This deeper economic and political integration was precisely what the Leave Campaign criticised, demanding to 'Take Back Control' over immigration, tariff rates, standards regulation, and the justice system. According to a survey, the first and second most important reasons for voting Leave were the impact of EU membership on immigration and British sovereignty (Owen and Walter 2017: 183). Had the US entered into a common market with Mexico, let alone an economic or political union, it is not difficult to imagine that opposition against Mexican immigration and the loss in US sovereignty would have resulted in support for withdrawing from the common market.

8.3.2. US Role in the Global Trade Regime

Another future research agenda, stemming from the typology of US trade policies developed in Chapter Three, is to understand the impact of the decline in US economic hegemony over the rules of the global trade regime. The first three periods of US trade policy, from WWII to 2016, all conditioned the global trade regime, from trade liberalisation (WWII to 1970) to 'new protectionism' (1971-1990) to the creation of a rules-based regime (1991-2016). The new era in US trade policy (2017-) has so far also shaped the global trade regime, with a tripling of global non-tariff barriers imposed annually between 2019 and 2022 (IMF 2023). US trading partners' protectionist response has also been caused by supply chain disruptions resulting from the COVID-19 pandemic, Russia's invasion of Ukraine, bottlenecks in key maritime routes, and climate change. By contrast to previous eras, US trading partners seek to maintain the trade regime without the US. For instance, they created an alternative to the Appellate Body at the

WTO and pursued trade liberalisation when the US exited TPP, leading to the signing of CPTPP (WTO 2023a). This era of US trade policy could be the last to shape the global trade regime.

The next years will determine whether US trade policy becomes even more 'power-based'. Trump is campaigning for the 2024 presidential election on a platform to impose a ten per cent tariff on all trading partners, with possible exceptions. This policy is supported by USTR Lighthizer (2023: 318) who argues that the most practical solution to reduce the US trade deficit is to 'put tariffs on all imports at a progressively higher rate year after year until we achieve balance'. As the share of US GDP in world GDP declined since WWII, the 'exorbitant privilege' of having the reserve currency also became an exorbitant burden as high demand for dollars led to its overvaluation, which in turn contributed to the large US trade deficit (Eichengreen 2012; Ganziro and Vambery 2016). Between 2016 and 2022, the US trade deficit nearly doubled from 500 to 945 billion dollars (US Bureau of Economic Analysis 2023). As the US seeks to reduce imports from China, its deficit is growing with other trading partners, such as Vietnam and Mexico. The US trade deficit with Mexico nearly doubled from 71.1 billion dollars in 2017 to 131.1 billion in 2022 (Ibid.), which could cause renewed tensions during the USMCA review periods. Between 2016 and 2022, Chinese FDI into Mexico surged from 107 to 611 million US dollars, although it remains dwarfed by FDI from the US and Canada (20.4 and 3.2 billion dollars in 2022, respectively) (Gobierno de México 2024).

The USMCA review period in 2026 will provide an opportunity to analyse whether the US applies the same power-based trade policy towards Mexico and Canada as to the rest of the world. Although facing protectionist pressures, US trade policy towards its neighbours will be constrained by the two path dependence mechanisms detailed in this thesis: increasing returns and veto power. Although those mechanisms also exist in US trade relations with the rest of the world, they are reinforced with Canada and Mexico given the strength of regional economic integration and the signature of a PTA. North American economic integration enables the US

to remain globally competitive and as such is likely to be treated differently than economic ties with the rest of the world. The next section provides policy reflections on this issue and its impact on development strategies in the global South, starting with Mexico.

8.4. Policy Reflections

The continuity between NAFTA and USMCA despite Trump's radical agenda has important implications for North American politics and economic development. Just as President López Obrador could not regain policy space due to path dependence, President Trump was constrained to abandon his radical negotiating objectives. Even though the NAFTA renegotiation undermined Mexico and Canada's stable access to the US market, and the USMCA contains review periods and a sunset clause which institutionalise market access uncertainty, the signing of USMCA was sufficient to restore business confidence in North American economic integration. This indicates that PTAs do not need to completely lock in market access stability to be beneficial. Instead, it is sufficient that they provide more stability than in their absence, as the two path dependence mechanisms, increasing returns and veto power, make withdrawal less likely.

As Mexico and the US remain tied by regional economic integration, the US has an interest in helping Mexico catch up, which would alleviate domestic concerns over low-wage competition (as well as migration pressures). From a structuralist economic analysis, a catch-up policy compatible with Mexico's policy space restrictions would be a North American industrial policy providing financial support for economic upgrading in Mexico. The extension of the US Inflation Reduction Act subsidies to PTA partners is a first step in that direction. The European Union provides a good example of more ambitious actions, having succeeded in helping Eastern European countries catch up through its regional cohesion policies. For instance, the North

American Development Bank could be capitalised to provide similar assistance to the European Investment Bank. The Brexit vote is a reminder, however, that following the EU model of deeper economic and political integration can be counterproductive by generating new sources of tension, such as over sovereignty, identity, and migration. Some of the proposals to strengthen North American integration, such as free movement of labour and a customs union are ill-suited to the political climate (Pastor 2001, 2011).

As the US remains focused on domestic concerns, however, it is unlikely to provide such levels of financial assistance to Mexico. To catch up economically without incentivising US protectionist policies, the Mexican government could implement industrial policies compatible with policy space constraints in USMCA and other PTAs. These include educational and technological policies to help domestic firms integrate into global value chains and progressively upgrade their production. Some Mexican states implemented these policies with tangible results, such as Querétaro which attracted the multinational Bombardier and its suppliers thanks to the construction of a new airport, the creation of an institution to train aeronautic engineers, and financial incentives (Kahn 2019; Tijerina Sepulveda 2016). Efforts to integrate local firms in global supply chains had limited results, however, while competition between Mexican states to attract multinationals incentivises a race to the bottom in tax breaks. To finance industrial policies, Mexico would need a tax reform as it remains the OECD country with the lowest tax-to-GDP ratio: 16 per cent in 2019, less than half the OECD average (OECD 2023).

Beyond North America, the findings suggest that the long-term effects of regional trade agreements on domestic coalitions and institutions can insulate some countries from the risks of increased asymmetric interdependence. The European and East Asian regional production networks are good comparisons given the power asymmetries between industrialised (Germany, Japan) and industrialising (Eastern Europe, ASEAN) countries. In Europe, Germany

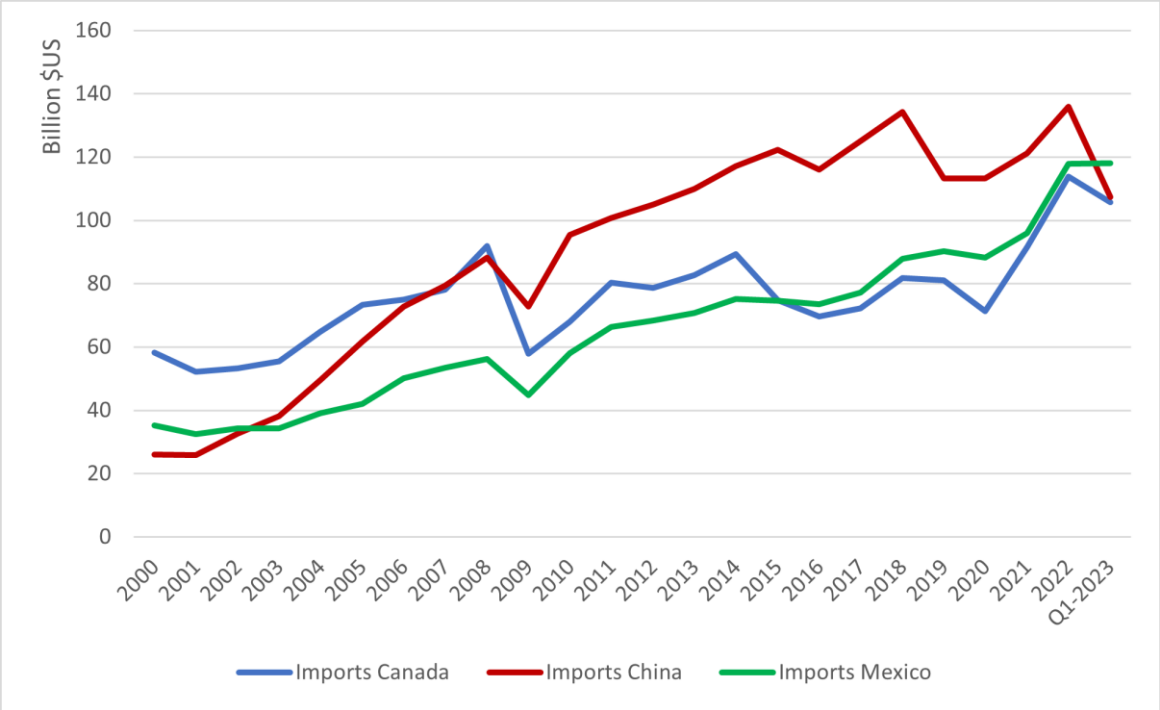
became increasingly reliant on integration with Poland and other Eastern European countries to remain competitive. In East Asia, South Korea and Japan each signed a PTA with the Association of South East Asian Nations (ASEAN) in 2006 and 2008, respectively, and closely integrated their production. Although PTAs in East Asia have been less ambitious than in Europe or North America, East Asian countries provide their neighbours with lower tariffs than their bound rates, resulting in a de facto preferential trade area (Hale 2011). Some of those preferential conditions are now formalised in the Regional Comprehensive Economic Partnership (RCEP), of which China is a member.

As the US implements protectionist policies to reduce domestic tensions and remain ahead of China, other industrial powerhouses are following suit with dire consequences for countries in the global South which are not part of regional PTAs. The European Union is implementing its industrial policy to achieve 'strategic autonomy', which includes subsidies to re-shore production (Damen 2022). China and Russia continue their strategy of achieving self-reliance by developing their own productive and technological capacities. India implements industrial policies to develop national champions, while Japan and South Korea seek to reduce their reliance on China by restructuring their supply chains towards ASEAN members (Maciejewska and Alifandi 2023). The result for countries in the global South not part of a regional industrial powerhouse, such as in Africa, Latin America, and parts of South Asia, is lower market access, while policy space remains restricted by WTO and PTA rules.

By contrast, Mexico displaced China in the first quarter of 2023 as the top exporter to the US, and Canada was close to becoming the second biggest exporter (Figure 12). While China accounted for 16 per cent of total US trade in 2017, before the US-China trade war, its share fell precipitously to 12 per cent by 2022, aside from a brief peak during the height of the COVID-19 pandemic (Torres 2023). Mexico and Canada's share of total US trade remained at

approximately 15 per cent each between 2017 and 2022, but recent data indicate a positive trend.

FIGURE 12. US IMPORTS FROM MEXICO, CANADA AND CHINA (2000-Q1 2023)



Source: Author's own based on data from Federal Reserve Bank of Dallas (2023).

Since the US-China trade war and the COVID-19 pandemic, Mexico has also benefited from foreign investment inflows due to nearshoring. FDI inflows in Mexico reached a record 33 billion US dollars in the first nine months of 2023, despite firms struggling with electricity and water shortages, safety concerns, and some of López Obrador's policies (FT Editorial Board 2023). As one Mexican negotiator aptly described, 'the US has a China problem and Mexico solution' (interview, 31 March 20221). Faced with the increased salience of regional economic blocs, Mexico's biggest return on investment from joining NAFTA is paradoxically occurring after NAFTA.

Annex

This annex presents data on interviews conducted (Table 10), provides the list of interview participants (Table 11), and identifies a selection of interviews in the media as well as events attended in Washington D.C. which enabled the author to engage in informal conversations with negotiators and stakeholders (Table 12).

Table 10 below presents data on interviews conducted (it does not include the many informal conversations at events and conferences). "Other" includes respondents working for academia, think tanks, international organisations, and NGOs.

TABLE 10. OVERVIEW OF INTERVIEWS CONDUCTED

	Government	Business	Labour	Other	Total
American	14	14	10	11	49
Mexican	16	6	8	3	33
Canadian	10	6	2	3	21
Other	0	1	0	4	5
Total	40	27	20	21	**108**

Interviews before 2023 were conducted online to eliminate health risks caused by the COVID-19 pandemic. Respondents were contacted by email and most interviews were conducted by video call. A few respondents were interviewed via phone calls, and several agreed to answer follow-up questions sent by email. Interviews typically lasted one hour and were conducted mostly in English, but also in Spanish and French. The online format facilitated the engagement of many respondents by reducing time and space constraints. Given that interview respondents were part of their country's political and economic elite, access to digital technologies was not a problem (Janghorban, Roudsari, and Taghipour 2014).

Table 11 provides the list of interviewees. To ensure the quotes cannot be attributed, the interview dates are not included. For further safety, the list will be removed from the thesis before it is submitted to the Bodleian library.

The research also benefited from media interviews given by negotiators and stakeholders, as well as informal conversations at conferences and roundtables hosted by think tanks, universities, and associations in Washington D.C. (Table 12).

TABLE 11. SELECTION OF MEDIA INTERVIEWS CONSULTED AND EVENTS ATTENDED

Interview or event name	Organisation	Date
Media interviews		
Gabriela Marquez Colin	Woodrow Wilson Centre (2018), Event	April 2018
Steve Verheul	Global Exchange, Podcast (Robertson and Verheul 2018, 2023)	April 2018; May 2023
Mexican negotiating team, Peña Nieto administration	Estrategia Aduanera (2019), Magazine	August 2019
Idelfonso Guajardo	Baker Institute (2021), Webinar	February 2021
Robert Lighthizer	Mexico Matters, Podcast (Campero and Lighthizer 2021)	October 2021
Negotiators and stakeholders	Washington International Trade Association, Events (WITA 2022)	2018-2022
Stakeholders and experts	Trade Talks, Podcast (Bown and Keynes 2022; Bown 2023)	2018-2023
Events in Washington D.C.		
Floating exchange rates at fifty	Peterson Institute for International Economics	March 2023
Global Trade Academy	Georgetown University	March 2023
Annual meeting	American Society of International Law	March-April 2023
Rethinking World Trade 2023	Center on Inclusive Trade and Development, Georgetown	April 2023
Katherine Tai, speech for 'Wenger Lecture'	American University Washington College of Law	April 2023
Revitalising American Commercial Diplomacy	Center for Strategic and International Studies	April 2023
Chrystia Freeland, speech for 'Macro week' event	Peterson Institute for International Economics	April 2023
Spring Meetings	IMF/World Bank	April 2023
Several events	Brookings	April-May 2023; Oct. 2023 (online)

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