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CHALLENGES FOR NAFTA: RENEGOTIATION OR DISINTEGRATION

Slavica STAMENIĆ¹
Mitko ARNAUTOV²

Abstract: Economic cooperation and integration on regional level represent a very attractive phenomenon in the period after World War II. The first examples of such integration we can notice on the European continent between states of the western European hemisphere. If we analyze from the economic point of view, we can draw a conclusion that cooperation between states which are geographically closer is always productive and fulfilled with positive effects for all parties. The North American Free Trade Agreement also represents an example whose main objective was deepening and widening the economic cooperation between the USA, Canada and Mexico. This article represents discussion on the topic of justification of the U.S. President Donald Trump decision to renegotiate NAFTA. It stresses the problem with the equality in free market trade. Although the idea of eliminating trade barriers between aforementioned neighbouring countries should have only positive results, this example of trade liberalization also showed negative impacts. It is primarily because it was not equally accepted and implemented by all partners, during 23 years, but also because of differences in the level of economic development and wage divergence between countries signatories. The authors concluded that there is no doubt that NAFTA should be renegotiated, but it should be transparent and in accordance with a common interest for all three member states.

Key words: North American Free Trade Agreement, NAFTA, international trade, renegotiation

¹ Slavica Stamenić, PhD candidate University of Belgrade, Faculty of political sciences, stamenic.slavica@gmail.com

² Mitko Arnaudov, PhD candidate University of Belgrade, Faculty of political sciences, mitko_arnaudov@yahoo.com

INTRODUCTION

NAFTA represents an acronym for the North American Free Trade Agreement, i.e. a treaty between the United States, Canada and Mexico, whose implementation started in 1994 and which is still the world's largest free trade agreement. Although it had been promised that NAFTA would enhance social and economic development and reduction in international migration in all three North American partners, especially in less developed Mexico, that commitment has not been fulfilled. Even though the major econometric forecasts on NAFTA effects estimated that the benefits of the agreement would be bigger for Mexico in comparison to the other two countries (Escobar Latapi and Janseen, 2006), each country has coped with some significant disadvantages of NAFTA.

Recently, political leaders of the United States - the world's only superpower and the second largest economy, announced the start of renegotiation of this 23-year-old agreement with the aim to assure the U.S. national interests. The Trump's administration has already taken the measures not only to stop negotiations about the Transatlantic Trade and Investment Partnership (TTIP), but also to withdraw the United States from the Trans-Pacific Partnership (TPP), which still has not been ratified but ought to become the world's new largest FTA. President Donald Trump, who obviously prefers bilateral trade agreements, at the beginning of his mandate, pledged that his administration will renegotiate or even abolish NAFTA in accordance with the Article 2205 of the NAFTA agreement, justifying that initiative with an intention to protect the rights of American workers.

If the withdrawal scenario happens, it could provoke reducing the income of the largest U.S. companies in many industries where companies tend to rely on imported raw materials from Canada or Mexico, such as automotive, agricultural, and textile. Changes could potentially trigger a return to the World Trade Organization most-favored-nation tariffs which certainly would have implications on the profitability of companies primarily from the U.S. (Terino, 2017). Considering that the U.S. President, Donald Trump, promised in his presidential campaign that protectionist measures and change in the trade policy will be implemented, reforming the NAFTA agreement became one of the most controversial topics in different academic and public debates.

NAFTA THROUGH HISTORY

When the idea about NAFTA saw the light of day, it was 1980 and there were presidential elections in the United States. The then-presidential candidate, Ronald Reagan, came out with an idea of unifying North America in the terms of trade. Supporters of that idea defended it as an opportunity for fighting against the main trade competitors, such as the EU or China, and improving conditions for the

market appearance of North American countries in the global marketplace. (Amadeo, 2017) Later, President Reagan explained the idea of the creation of NAFTA trade area with the aim of making better economic perspectives for all those three countries: the United States, Canada and Mexico and soon after the negotiations started. First, the United States and Canada started bilateral negotiations about free trade and it resulted in the agreement between these two countries that was signed in 1989. Later, in 1991, the U.S. started negotiations with Mexico, and Canada later joined, so three years later, after the ratification by all three parties NAFTA entered into force.

The interesting fact about NAFTA is that it is a bipartisan agreement because it was negotiated under President George H.W. Bush and Republican Party, but signed and implemented by Democratic President Bill Clinton. The first stage of NAFTA implementation comprised eliminating of trade tariffs by the U.S. and Canada on many Mexican agricultural and automotive products and dropping the trade barriers on American and Canadian autos from 20 to 10% by Mexico. The second stage was four years after the implementation and it included eliminating tariffs on cotton and wheat produced in Mexico by the U.S., but also nullifying of export taxes on many U.S. fruits. In this stage, the U.S. and Canada mutually eliminated many remaining agricultural tariffs. The next stage was in the 2007-2008 when Canada cancelled taxes on Mexican sugar, meat and flour and Mexico nullified the remaining tariffs on cars and auto parts from Canada and the U.S. During this period, the U.S. and Mexico mutually eliminated tariffs on dairy, rice and some vegetables. Until 2008, most of the remaining trade barriers were eliminated and North American economic relations were fundamentally reshaped.

During the 2008 presidential campaign in the United States, NAFTA was blamed by President Barack Obama for growing unemployment rate in the U.S. and he had promised to renegotiate NAFTA if he became U.S. President, but he did not keep the promise during his presidential mandate. However, it is not first, but also not the last time, NAFTA was attacked during presidential campaigns. Earlier, in 1992, before the agreement was ratified, a presidential candidate Ross Perot pointed out some disadvantages of NAFTA and predicted that workers in the U.S. would be displaced by lower cost workers from Mexico. On the other side, supporters of this FTA claimed that it would create conditions for opening hundreds of thousands of new jobs, and Mexican President Salinas saw NAFTA as an opportunity to develop and modernize the economy of Mexico. The agreement represented a watershed in global trade policy, not just because of the size of the free trade area it created, but also with regard to the comprehensiveness of the agreement, which covered not just merchandise trade but also issues related to investment, labor markets, and environmental policies.

OVERVIEW OF NAFTA

As the aforementioned, the main objectives of creating NAFTA agreement were making political, legal and business conditions for trade exchange and attracting foreign direct investments in the region of North America. Article 102 of the agreement specifies seven goals that NAFTA fulfilled and justified its purpose of existence. One of the advantages of NAFTA agreement is that it grants an equal treatment to all its signatories. It is especially important for foreign direct investments because countries signatories neither can offer better conditions to domestic investors than foreign ones, nor they can give better treatment to investors from countries that are not NAFTA signatories. This agreement provides eliminating trade barriers between three countries and facilitates movement of goods and services among their borders.

Many experts estimate that NAFTA provides many benefits to the North American region. Besides positive impacts on the regional trade that increased from \$290 billion in 1993 to more than \$1.1 trillion in 2016 (Villarreal and Fergusson, 2017), NAFTA influenced cross-border investments. For instance, the U.S. foreign direct investments in Mexico increased in that period from \$15 billion to more than \$100 billion (Villarreal and Fergusson, 2017). However, some economists draw attention on other factors that also influenced this macroeconomic indicator in the same period of time such as trade expansion with China and other emerging economies and rapid technological change and internal developments of these countries (Autor, Dorn and Hanson, 2016).

Most of the NAFTA estimations agree that it had a positive impact on GDP of the U.S. but the effect was modest, i.e. less than 0.5 %, or a total addition of up to \$80 billion dollars upon full implementation. The developed economy of Canada had many benefits in the NAFTA era. The U.S. and Mexican FDI in Canada increased by three times. For example, the U.S. is the largest investor in Canada and its investments increased from \$70 billion in 1993 to over \$368 billion in 2013. Canadian exports to the U.S. increased from \$110 billion to \$346 billion, while imports from the U.S. grew reciprocally. Since Canada is the leading importer of agricultural products from the United States, their agricultural trade has tripled after 1994.

Mexican government saw both, liberalizing trade and NAFTA, as a chance to accelerate reforms to the Mexican economy. They achieved change in the country's economic model, stabilized inflation, reducing the public debt and the country's foreign reserves at a satisfying level. (García Zamora, 2014)

Thus, when it was hit by the global economic crisis in 2008 it recovered relatively quickly. Mexican farm exports to the U.S. tripled after the NAFTA implementation, hundreds of thousands of manufacturing jobs have been created and the NAFTA agreement also had a positive effect on the productivity of Mexican workers and consumer prices. (Villarreal and Fergusson, 2017)

It is not difficult to conclude that the absence of import tariffs caused decreasing prices. Considering that oil is one of the most significant factors for production and the economy, NAFTA helped the U.S. to reduce its reliance on oil imports from Venezuela and OPEC countries with a cheaper import of oil from Mexico and Canada. It resulted in reducing costs of production, so it lowered overall prices. It is important to highlight that NAFTA enhances protection of intellectual property rights and promotes conditions of fair competition. This trade agreement also establishes procedures for the resolution of trade disputes in order to protect businesses from unfair situations and facilitate to all parties the interpretation of complex rules and procedures of the NAFTA agreement. Also, NAFTA creates a framework for further regional and multilateral cooperation which expand the trade agreement benefits.

However, obviously the most noticeable thing about NAFTA is that two developed economies, such as the United States and Canada, signed a free trade agreement with Mexico which stands for a developing country. Some opponents of NAFTA agreement asserted there is a huge discrepancy between these countries, especially in terms of wage amounts, because at the moment of negotiation about NAFTA, Mexico's GDP *per capita* was about 30% of the United States. (Blecker, 2014)

Although NAFTA obviously created the largest free trade area in the world, increased trade exchange more than four times between the NAFTA members and consequently it has had a positive impact on their economic growth, GDP and foreign direct investments, NAFTA has many significant shortcomings. First of all, it provoked losing many jobs in the United States, mostly in the manufacturing industry in the states like New York, California, Texas and Michigan. Some economists assess that this caused the loss of 600,000 U.S. jobs during two decades of the NAFTA agreement. Companies had to move their factors of production, especially in the sectors such as textile, automotive, computer and electrical appliance, to cheaper destinations to lower costs and enhance competitiveness. Mexico, as a developing country with a lower living standard and a cheaper labor force, was recognized by many manufacturing companies from the U.S. and Canada as an excellent opportunity for reducing expenses and increasing competitive advantage. With offshoring not only parts of the production but also jobs in Mexico, many companies cut their costs and Mexico decreased its unemployment rate. However, it also had an impact on losing jobs or lowering wages of blue-collar workers in the U.S. and increasing the U.S. trade deficit with Mexico. Experts who support NAFTA estimated that plenty of jobs, about fourteen million, in the U.S. mostly relied on the trade relations with Mexico and Canada and that benefit from created jobs was larger than the damage from the jobs that were lost. (Hills, 2014) However, some researchers assumed that China's joining the WTO in 2001 had a bigger negative impact on jobs in the United States (Autor, Dorn and Hanson, 2016) They agree that the decline in manufacturing jobs is primarily attributable to

underlying technological changes and trade with China. (Autor, Dorn and Hanson, 2016). The aforementioned authors added that NAFTA helped the U.S. automotive sector to compete with China, because NAFTA improved competitiveness of the workforce in the U.S., increased productivity and lowered costs.

Secondly, the NAFTA agreement has had bad implication on the Mexican workforce too. They suffered exploitation in the maquiladora program which comprised that companies from the United States employ workers from Mexico near the border to transport goods that is made in Mexico to consumers in different parts of the United States. Today this program includes about one-third of the Mexican labor force and these workers had “no labor rights or health protections, they work in sub-standard conditions”. (Hufbauer and Goodrich, 2001.) When negotiations for NAFTA began it has been promised that NAFTA would help the integration of Mexico with the high-wage economies, and in accordance with it was expected to achieve the “wage convergence” between Mexican and U.S. wages and to increase the living standards in Mexico. On the contrary, poverty in Mexico remains at the same level as before NAFTA and NAFTA indirectly influenced the massive illegal migration of working-age Mexicans. Migration to the United States started to be considered an attractive life choice because real average wages of workers in Mexico have fallen below levels they were before implementing the NAFTA agreement.

Third, but not the last, the disadvantage of the NAFTA agreement is reflected in the fact that NAFTA allowed the U.S. government to subsidize farm products that it has been exporting to Mexico so it obviously resulted in putting out of business numerous Mexican farmers. This measure had a consequence of losing jobs for almost two million small rural Mexican farmers, especially those who were corn producers and were not highly subsidized such as American farmers and could not offer competitive prices for some agricultural products. (Economist, 2008.)

This also provoked floods of illegal migrations to the United States after 1994, with the peak in 2008 because of the economic downturn. In addition, we could not neglect that U.S. companies influenced the degradation of the Mexican environment intentionally to keep costs low. On the other hand, NAFTA provides protections for multinational corporations giving them rights to exploit low-wage countries and their labor force and territory for the purpose of maximizing profit.

USA ECONOMY FACTS

Despite facing challenges at the domestic level along with a rapidly transforming global landscape, the U.S. economy is still the largest and most important in the world. The U.S. economy represents about 20% of total global output and is still larger than the Chinese. (Focus Economic, 2017.) According to the numerous

analyses, a generator of the American economy represents the sector of services. The most productive and efficient sectors are technology, financial services or banking, healthcare and retail. However, one of the most important parts of American economy represents the manufacturing sector, which comprises roughly 15 percent of American output. The U.S. is the second largest manufacturer in the world and a leader in higher-value industries such as automobiles, aerospace, machinery, telecommunications and chemicals. (Focus Economic, 2017.) The United States mainly exports high-value capital goods and manufactured products, including industrial machinery, airplanes, motor vehicles and chemicals. In 2015, the U.S. exported USD 1.510 trillion in goods. (Focus Economic, 2017.) The biggest percent, around 80% of total American import is goods. Roughly 15% of these imports are in the form crude oil, fuel oil and petroleum products. (Focus Economic, 2017.)

In the years since NAFTA, the U.S. trade with its North American neighbors has more than tripled, growing more rapidly than the U.S. trade with the rest of the world. (Council on foreign relations, 2017.) However, within the American society thoughts are still separated to the effects of NAFTA. During the huge economic crisis which started in 2008, American citizens have been demanding the USA government withdrawing from this agreement. Even during the presidential campaign of the last autumn, a Republican candidate Donald Trump said that if he won the elections, he would start renegotiating of the agreement. The U.S. President Donald Trump delivered a formal notice to the Congress on May 18 that the administration will renegotiate the agreement, following a 90-day consultation period. Trump repeatedly attacked it during his campaign, promising a renegotiation and warning that if the results “aren’t satisfactory, we’re going to tear it up.” (Investopedia, 2017.)

Most estimates conclude that the deal had a modest but positive impact on U.S. GDP of less than 0.5 percent, or a total addition of up to \$80 billion dollars to the U.S. economy upon full implementation, or several billion dollars of added growth per year. (Council on foreign relations, 2017.) A 2014 PIIE study of NAFTA’s effects found that about 15,000 jobs net are lost each year due to the pact—but that for each of those jobs lost, the economy gains roughly \$450,000 in the form of higher productivity and lower consumer prices. (Council on foreign relations, 2017.)

MEXICO ECONOMY FACTS

Analyzing the case of the Mexican economy, researchers find out that it is possible unilaterally to become a part of world economic flows. Its economic output, as measured by gross domestic product was \$2.2 trillion in 2015. This was much less than its primary trading partner, the United States (\$17.9 trillion) but

larger than its other NAFTA partner, Canada (\$1.6 trillion). (The balance, 2017.) It unilaterally liberalized foreign trade and investment policies in the 1980's and then enacted NAFTA in 1994, which further reduced trade barriers and helped lock in reform by enshrining it in a multilateral treaty. (Gordon H. Hanson, 2003.) At the beginning of the 21st century this state was deeply integrated within so-called North-American economic zone. For example, in 2000 Mexico sent 88,7% percent of its domestic production to the United States market and from the other side, 73,1% of Mexican imports were from the United States. Greater openness has helped increase the share of trade in Mexico's GDP from 11.2% in 1980 to 32.2% in 2000. (Gordon H. Hanson, 2003.) Trade with the United States and Canada has tripled since the implementation of the North American Free Trade Agreement in 1994. More than 90 percent of Mexico's trade is under 12 free trade agreements with over 40 countries. (The balance, 2017.)

NAFTA gave Mexico a considerable preferential tariff advantage. There was a substantial increase in the volume of Mexican exports entering into the U.S. market duty free as the share of imports from Mexico entering duty free increased from approximately 50 percent in 1993 to more than 85 percent in 2001. (M. Ayhan Kose, Guy M. Meredith, and Christopher M. Towe, 2004.) For numerous researchers of the Mexican economy and its trends, NAFTA represents a continuation of Mexico's comprehensive market liberalization. Also, this country has continued with the internal economic reform strategies. "Mexico's trade with the NAFTA partners has increased significantly since the inception of NAFTA. For example, Mexico's exports to the United States and Canada more than doubled in dollar terms between 1993 and 2002. Mexico's trade (the sum of exports and imports) with the NAFTA partners rose from 25 percent of its GDP in 1993 to 51 percent in 2000. Mexico's trade (the sum of exports and imports) with the NAFTA partners rose from 25 percent of its GDP in 1993 to 51 percent in 2000. (M. Ayhan Kose, Guy M. Meredith, and Christopher M. Towe, 2004.) While the growth of trade has slowed down since 2000, Mexico's trade with the NAFTA partners still accounted for more than 38 percent of its GDP in 2002. Approximately 90 percent of total exports of Mexico went to the partner countries in 2002, while imports from the partner countries constituted more than 65 percent of total imports." (M. Ayhan Kose, Guy M. Meredith, and Christopher M. Towe, 2004.)

CANADA ECONOMY FACTS

Canada's economic output, as measured by gross domestic product, was \$1.67 trillion in 2016. This was just one-tenth of its primary trading partner, the United States (\$18.5 trillion) and slightly less than its other NAFTA partner, Mexico (\$2.3 trillion). (The balance, 2017.) Actual data said that the Canadian economy is moving forward and that it will provide impressive results during 2017. Because

Canadian northern half is so cold for so much of the year only 4,3 percent of its land is suitable for farming, compared to 16.9 percent of land in the United States of America, and 12.9 percent in Mexico. Canada is the 12th largest exporter in the world. It exports amounted \$402 billion in 2016. Three-fourths of this goes to the United States. Trade with the United States and Mexico has tripled since 1994, thanks to NAFTA. Canada is America's largest supplier of energy. That includes oil, gas, uranium and electric power. (The balance, 2017.)

Interesting fact about the Canadian economy represents the discovery of oil sands in Alberta. That gave it the third largest oil reserves in the world or concretely 173.1 billion barrels, which means that Canadian oil reserves fit this state behind Saudi Arabia and Venezuela. On the other hand, Canada's reliance on oil exports may throw it into a recession. That is because oil prices fell from \$100 to \$25 a barrel in 2014. (The balance, 2017.) The new Canadian Prime Minister Justin Trudeau has started his governing with liberal measures. He is planning further to stimulate the Canadian economy through 60 billion dollars in new infrastructure. This plan will increase the budget deficit, but that might be paid for taxes on marijuana which Trudeau plans to legalize. (The balance, 2017.)

Canada did enjoy a 243% real increase in FDI from the U.S. between 1993 and 2013, and real GDP per head grew faster – just barely – than its neighbors from 1993 to 2015, though it remains about 3.2% lower. (Investopedia, 2017.) Overall, NAFTA was neither devastating nor transformational for Canada's economy. Opponents of the 1988 free trade agreement had warned that Canada would become a glorified 51st state. While that did not happen, Canada did not close the productivity gap with the U.S. either: Canada's productivity per hours was 74% of the U.S.'s in 2012, according to the OECD. (David Floyd, 2017.)

CONCLUSION

From the beginning of existence of NAFTA, there were different opinions about its effects. Numerous American researchers and economists have thought that this agreement cannot bring positive implications on the American economy. They were convinced that this agreement will have a positive influence on the Canadian economy and a huge economic profit for the Mexican economy. From the beginning, critics of NAFTA were concerned the Agreement would result in U.S. jobs moving to Mexico. (Investopedia, 2017.) Between 1994 and 2010, the U.S. trade deficits with Mexico totaled \$97.2 billion. During the same period, 682,900 U.S. jobs went to Mexico. However, 116,400 of those jobs were displaced after 2007. The 2008 financial crisis could have caused them instead of NAFTA. (Kimberly Amadeo, 2017) That suppressed the wage growth. Between 1993 and 1995, 50 percent of U.S. manufacturing companies in industries that were moving to Mexico used the threat of closing the factory. By 1999, that rate grew to 65

percent. (Kate Bronfenbrenner, 2000.) Such trends, especially within economic relations between the United States of America and Mexico, lead American citizens to demonstrations and expressions of dissatisfaction. The American labor market has become determined by economic flows in Mexico. For each administration in Washington such trends were negative point during its governing.

From the other side, the Mexican economy has also had huge challenges. Thanks to NAFTA, Mexico lost 1.3 million farm jobs. The 2002 Farm Bill subsidized U.S. agribusiness by as much as 40 percent of net farm income. When NAFTA removed trade tariffs, companies exported corn and other grains to Mexico below cost. Rural Mexican farmers could not compete. (The balance, 2017.) However, considering the fact that more than a third of U.S. exports flow to Canada and Mexico, business and labor groups were watching closely to see what Trump's team would prioritize in the negotiations. Companies that export products to Canada and Mexico are wary of anything that could limit their future access to those markets. Firms that have struggled against foreign competition, as well as labor groups that have seen their members' wages undercut by foreign workers, were hoping for measures that would give them a leg up. (Ana Swanson, 2017.)

The new NAFTA objectives and a requirement to begin talks on updating the agreement contain the first specifics for the Trump's administration that has made bold promises on trade. Trump has pledged to recover factory jobs and boost wages by crafting new trade deals. Supporters note that NAFTA enabled companies to charge cheaper prices for products that range from cars to vacuum cleaners, helping many U.S. consumers. (Josh Boak, 2017.) After few months of Trump's presidential mandate seems that it is not so dangerous for sustainability of the open market.

The Trump's administration is pushing up the plan for the renegotiation of NAFTA, but in correlation with American Congress, they become aware that it is not just one step decision. Advancement and strengthening the economic ties between those three partners within NAFTA do not mean unilateral decisions and alternatives, but common, comprehensive and cohesive decisions which will allow a better economic basis for all interested sides. During the process of renegotiation, American officials should consider national interests of other two member-states in this contract, Mexico and Canada. If the U.S. officials enter into the process of renegotiation led exclusively by their own egoistic and mercantilist interests, they could face with the dissatisfaction of the other two countries and the impossibility of achieving consensus. It could consequently provoke disintegration of the NAFTA agreement which would contribute to negative economic and commercial implications to all three partners.

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Slavica STAMENIĆ
Mitko ARNAUTOV

IZAZOVI PRED NAFTA SPORAZUMOM: PONOVNO PREGOVARANJE ILI RASKID SPORAZUMA

Apstrakt: Ekonomska saradnja i integracija na regionalnom nivou predstavlja veoma atraktivan fenomen u periodu nakon Drugog svetskog rata. Prve primere takve integracije možemo da uočimo na evropskom kontinentu između država koje se nalaze u zapadnoj evropskoj hemisferi. Ako analiziramo sa ekonomske tačke gledišta, možemo zaključiti da je saradnja između država koje su geografski bliske uvek produktivna i ispunjena pozitivnim efektima za sve strane. Severno-Američki sporazum o slobodnoj trgovini (NAFTA) predstavlja još jedan primer čiji je glavni cilj produbljavanje i širenje ekonomske saradnje između Sjedinjenih Američkih Država, Kanade i Meksika. Ovaj članak predstavlja svojevrsnu diskusiju na temu opravdanosti odluke novog američkog predsednika Donalda Trampa o ponovnom pregovaranju Sporazuma NAFTA. On je naglasio problem jednakosti pristupa odnosno trgovine na otvorenom tržištu. Iako je ideja o otklanjanju trgovinskih granica i barijera između gorepomenutih susednih država trebalo bi da implicira samo pozitivne rezultate, ovaj primer trgovinske liberalizacije je takođe pokazao svoje manjkavosti i negativne posledice. Takve posledice su uočene prvenstveno zbog toga što ovaj Sporazum nije bio jednako prihvaćen i implementiran od svih strana potpisnica u poslednje 23 godine, ali takođe zbog velikih razlika u nivou ekonomske razvijenosti i platne nejednakosti između država potpisnica. Autori su zaključili da ne postoje sumnje da NAFTA sporazum treba da bude ponovni predmet pregovaranja između država članica, ali ovi pregovori bi trebalo da budu transparentni i u skladu sa zajedničkim interesom za sve zainteresovane strane.

Ključne reči: Severno-Američki sporazum o slobodnoj trgovini, NAFTA, unutrašnje tržište, ponovno pregovaranje.

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