

# Intelligence MEMOS



*As NAFTA renegotiations proceed through the summer and fall C.D. Howe Institute Intelligence Memos will be looking at what to expect and provide analysis on the latest developments at the table. This post is part of that series.*

From: Jon Johnson  
To: The US Automotive Industry  
Date: September 29, 2017  
Re: **ACCESS TO MEXICO AUTO MARKET – NAFTA BEST TRADE DEAL EVER**

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The Trump Administration needs reminding of the major victory that the US negotiators achieved in the original NAFTA negotiations in the complete dismantling of the highly restrictive pre-NAFTA auto regime that existed in Mexico.

Before NAFTA, the production in Mexico of all light duty vehicles was governed by the Mexican Automotive Decree. Assemblers in Mexico (at that time restricted to the Big Three, Nissan and Volkswagen) were limited to producing motor vehicles and engines in Mexico and no other automotive products. Motor vehicles produced in Mexico by these assemblers were subject to domestic value added requirements that meant that most parts could only be sourced from Mexican suppliers. Mexican auto parts industry suppliers had to be majority Mexican-owned. The assemblers were subject to trade balancing requirements that severely limited their ability to import vehicles into Mexico. There was a parallel parts industry operated through in-bond manufacturing plants known as maquiladoras that imported inputs without paying duty and re-exported the finished parts. However, parts produced by maquiladoras had to be exported and could not be used by vehicle assemblers in Mexico.

The US NAFTA negotiators succeeded in negotiating the dismantlement of this highly restrictive managed trade regime. The Automotive Decree was phased out and completely eliminated by 2004. Ownership restrictions of Mexican auto parts industry suppliers were eliminated. Subject only to complying with NAFTA rules of origin for vehicles exported to the US and Canada, vehicle assemblers in Mexico can source parts from wherever they choose.

Free trade in motor vehicles and parts has worked very well for Mexico and if the US chooses to withdraw from NAFTA, Mexico will not return to the highly restrictive regime that NAFTA eliminated. However, the US automotive industry will be disadvantaged if the US withdraws from NAFTA because of significantly diminished access to the Mexican automotive market. While US tariffs on light duty vehicles of 2.5 percent will not provide much of a deterrent to imports of vehicles from Mexico into the US, Mexican tariffs of 30 percent on light duty vehicles will significantly curtail the export of light duty vehicles from the US to Mexico. While Mexican tariffs on most parts are low, assemblers in Mexico will no longer have the incentive to use parts imported from the US now provided by the need to comply with NAFTA rules of origin for NAFTA duty free access. Mexican assemblers will import parts from sources that are most economical or from Mexican free trade partners such as the European Union or Japan.

NAFTA has been the best trade deal ever from the standpoint of your industry's access to the Mexican automotive market. The US cannot withdraw from NAFTA unless Congress agrees. Your industry should exercise all the influence that it can to ensure that Congress asserts its constitutional authority to prevent the US from withdrawing from NAFTA.

*Jon Johnson is a former advisor to the Canadian Government during NAFTA negotiations and is a Senior Fellow at the C.D. Howe Institute.*

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