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Harley Shaiken

The New Global Economy: Trade and Production under NAFTA

1. Introduction

What has happened to US-Mexico trade since the implementation of the North American Free Trade Agreement (NAFTA) on January 1, 1994? Proponents of NAFTA point with pride to a tripling of cross-border trade to over $235 billion in 2000, propelling Mexico past Japan into the second largest trading partner of the U.S. U.S. trade representative Robert B. Zoellick opined in the Los Angeles Times that the U.S. exports "more to Mexico than to the combination of the four European members of the G-7: Britain, France, Germany and Italy" (Zoellick 2001). Since exports create jobs in the U.S., proponents argue, this expansion of trade has beneficial consequences. Franklin J. Vargo, a vice president of the National Association of Manufacturers, told the U.S. Congress in May 2001 that "last year Mexico accounted for close to one-third of all U.S. export growth worldwide" (2001: 2). Vargo then added that the proposed Free Trade Agreement of the Americas (FTAA) "will have the same effect on our exports to Central and South America as NAFTA did on our exports to Mexico" (2001: 2). Critics, however, focus on the burgeoning trade deficit the US runs with Mexico which reached a record $34 billion in 2000 compared to a $1.6 billion trade surplus in 1993.1 As Robert E. Scott points out in an Economic Policy Institute (EPI) report "the U.S. has experienced steadily growing global trade deficits for nearly three decades, and these deficits have accelerated rapidly since NAFTA took effect on January 1, 1994" (Scott 2001: 3). Scott points out elsewhere that "EPI's analysis of the impact of trade reflects a simple, uncontested accounting rule: exports create demand for domestically produced goods, and imports reduce demand for domestically produced goods" (Scott 2001a: 2).

While both expanded trade flows and growing deficits define important dimensions of the US-Mexico trading relationship, this data alone leaves a critical question unanswered: what is the character of US-Mexico trade under NAFTA? Examining only the aggregate trade numbers conjures up images of Mexican consumers clamoring for U.S. goods while U.S. consumers are purchasing even more products from Mexican firms. The reality is far different. An increasing percentage of US manufacturing shipments to Mexico are "revolving door" exports-parts and components shipped to Mexico for assembly and further processing and ultimately sold to consumers in the US market. These "revolving door" exports comprised more than 60 percent of US manufacturing shipments to Mexico in 1999 compared to just over 40 percent in 1993.2 Put differently, the
vast majority of U.S. exports to Mexico stay in that country only long enough to be assembled into products that are ultimately sold in Wal Marts in Toledo, Ohio or automobile dealerships in Stockton, California. The result is a distorted trading relationship fueling Mexico's growth as an "export platform" rather than encouraging a more vibrant consumer market.

What are the forces that have caused this surge in intra-industry trade? Underlying these vastly expanded trade flows, a new international division of labor has emerged in which the Mexican export sector combines world-class manufacturing with low wages (Shaiken 1987, 1990, 1994). Export plants have demonstrated a capability to produce increasingly sophisticated products from automobile engines to projection televisions at high levels of quality and productivity. These plants often employ state-of-the-art manufacturing techniques and new forms of work organization (Carrillo 1998). While manufacturing sophistication has soared, wages have declined or remained stagnant over much of the last two decades, depressed by government policies to attract investment and a lack of labor rights, among other factors. This disconnect between growing manufacturing productivity and low wages flies in the face of much economic theory. Burtless et al. write that "... wages in poor countries are low because worker productivity in these countries is low" ignoring the complex institutional factors that shape wage levels (1998: 66). Burtless et al. then observe "this low productivity is not surprising since workers in poor countries are not as educated as U.S. workers, do not have the advantages of working with sophisticated factory equipment or in an economy with a modern infrastructure..." (1998: 68). While this observation may accurately describe a dimension of some developing economies, the evidence strongly suggests this analysis ignores the reality of the export sector in Mexico. In addition, low real wages in the most dynamic sector of the Mexican economy depress purchasing power and contribute to Mexico's serious income polarization (Dussel Peters 2000).

The underpinnings of this new pattern of trade predate NAFTA. Beginning in the early 1980's transnational firms in industries such as automobiles and electronics began siting sophisticated manufacturing and assembly facilities in Mexico that have become increasingly linked into global production networks. In some cases, these operations initially responded to Mexican domestic content rules and were intended to produce for the Mexican market. The collapse of the Mexican market after 1982 and the increased competitive pressure faced by U.S. manufacturers, especially from Japan, led to a rethinking of Mexican plants as part of integrated production networks aimed at the U.S. market.

This far-reaching manufacturing integration would likely have continued and even expanded without the trade agreement. NAFTA, however, has provided two important additional incentives. First, it secures a stable business climate by providing strong investment protection in Mexico and political assurances that the U.S. market will remain open. Second, the weak provisions in the NAFTA labor side agreement leave intact a labor relations environment that has contributed to holding wages down. During the final negotiations of the trade agree-

2. The character of U.S. Mexico trade under NAFTA

U.S.-Mexico merchandise trade has tripled since NAFTA went into effect from $79 billion in 1993 to $235 billion in 2000. In the midst of this exceptional growth, the U.S. went from small trade surpluses to large trade deficits. The U.S. trade surplus with Mexico peaked at $5.7 billion in 1992. NAFTA proponents widely cited this trade surplus during the debate over ratification in the U.S. Congress in 1993 and projected significant growth in U.S. surpluses with Mexico through
the 1990s and beyond (Hufbauer 1993). Instead the U.S. trade surplus slumped to $8.5 billion in 1994 on the eve of Mexico’s peso devaluation and then went over a cliff to a record $16.8 billion trade deficit as the Mexican economy imploded in 1995. In the midst of Mexico’s economic calamities, U.S. exports slid by almost $4 billion in 1995 while U.S. imports continued to rise as Mexican plants shifted their production from the evaporating domestic market to the growing U.S. market. As Mexico’s economy recovered after 1995, US exports rose once again but imports from Mexico rose even faster, resulting in large U.S. trade deficits for the rest of the decade, culminating in the record $34.3 billion deficit in 2000.

As trade between the two countries grew, intra-industry trade grew even faster. The result is that over 60 percent of US exports to Mexico feed production facilities that will export the final product to the US market, a sharp increase from the 41 percent of “revolving door” exports recorded in 1993. This phenomenon explains the seeming anomaly of the large volume of US exports to Mexico, given the size and, at times, weakness of the Mexican economy. In effect, most U.S. exports to Mexico are part of a highly integrated North American production base and independent of Mexico’s domestic economy.

Complex manufactured products account for an important share of Mexican exports to the U.S. The two largest categories—electrical machinery and equipment (Harmonized Tariff Schedule 85) and vehicles (HTS 87)—accounted for $62 billion of Mexico’s $135 billion of exports to the U.S. in 2000, almost half the total. Illustrating the country’s new industrial prowess, Mexico has become the world’s largest exporter of television receivers, exporting $5 billion worth in 1998, more than double the value of number two exporter Japan. Motor vehicles play a particularly critical role. The automobile industry alone represented almost one fifth of U.S.-Mexico merchandise trade in 2000. The U.S. imported $28 billion in finished vehicles, parts, and engines and exported $12 billion in these categories for a trade deficit of about $16 billion, almost half of the total trade deficit with Mexico. The largest category is trade in light vehicles—passenger cars, SUVs, and pickup trucks—which accounted for over $23 billion of the $40 billion in automobile trade. Mexico produced 1.9 million cars and trucks in 2000 of which 1.2 million were exported to the United States. In contrast, Mexico imported only 280,000 vehicles from the U.S. Mexico’s vehicle exports to the United States equaled two thirds of Japan’s shipments and exceeded the combined exports of Germany and Korea. Given the importance of motor vehicles to Mexican trade with the United States, this industry offers an unusually good case study of “revolving door” trade.

3. High quality, high productivity exports

Since the early 1980s the Mexican auto industry has traveled a path from import substitution industrialization to a strong export orientation. On the shop floor this has meant a move from being a low-volume producer using antiquated machinery for the domestic market to becoming a high volume exporter using state-of-the-art equipment and methods. When asked to name the great manufacturing centers in North America, Troy Clarke, the president of General Motors de Mexico, responded “you’ve got Ontario and Michigan. You’ve got Kansas and
Ohio and Indiana. Now you add Mexico to the list" (Lippert 2001). The emergence of Mexico as a major auto exporter is underscored by the technological sophistication and economic importance of the finished vehicles it is producing. "Mexico has transformed itself from a second-tier carmaker to a hotbed of unique, popular vehicles made anywhere else in the world," a Reuters article stated (Klayman 2000). The Daimler-Chrysler Toluca plant is the sole source in North America for the company's hot selling, retro-design PT Cruiser; the Volkswagen complex in Puebla is the only manufacturing site world-wide for the new Beetle, and General Motor's truck plant in Silao is the primary production location for the full-sized, highly-profitable Chevrolet Suburban SUV. In addition, the automakers are moving upscale in what they plan to produce in Mexico. General Motors intends to build a Saab version of a car-SUV hybrid in its northern Ramos Arizpe plant in 2002 and Ford plans to produce Volvos in its Hermosillo plant in 2004 (Klayman 2000). Auto companies invested $30 billion in Mexico from 1994–1999 and projections indicate an additional $13 billion between 1999 and 2002 (McNay and Polly 2000: 26). The consulting firm of Price Waterhouse Coopers predicts vehicle production in Mexico will hit 2.5 million units by 2005–6 (Corbett et al 2000: 50).

The output of these factories is clearly world-class. "Mexico's auto assembly plants now are equal to those in the rest of North America in quality and labor productivity and sometimes better," Corbett et al commented, reflecting a sentiment increasingly found in the trade press (2000: 50). George Owens, the manager of product research at J. D. Power and Associates, the leading research firm concerning auto industry quality, concurred that Mexican plants have steadily improved and are now in the "same league" as their North American counterparts. J. D. Power ranked the Daimler Chrysler Toluca plant as their fourth highest quality facility in North America in 2000. "Knowledgeable sources say most of GM's Ford's and Daimler-Chrysler's Mexican plants rank at or near the top in their internal rankings of plant quality," Corbett et al maintained. Comparing the Ford Hermosillo plant with the Daimler Chrysler Satillo facility and the GM Silao complex, Automotive News concluded that "Hermosillo, like the other operations, is one of the most competitive plants in North America and eclipses the performance of other Ford plants in most areas" (Automotive News 2000). And, while auto is clearly among the most advanced exporters in Mexico, the ability to achieve these results in manufacturing of this complexity indicates the possibilities for other industrial sectors as well.

In a highly-competitive consumer industry such as automobiles, achieving high quality is pivotal. In fact, poor quality levels undermine even large manufacturing cost advantages. In earlier research, I found that automakers were capable of achieving high quality in state-of-the-art engine manufacturing and assembly plants (Shaiken 1987, 1990). New data from the initial quality survey done by J. D. Power and Associates for the 1998 and 1999 model years allows a broader comparative look at light vehicle assembly quality in Mexico and the U.S. This data measures the number of defects per hundred vehicles after three months of service which is a closely watched indicator of assembly plant performance. For the 1999 model year, sufficient data was available to compare 10 models produced in both countries. The quality recorded in Mexican plants was better than their U.S. counterparts for 6 models. Data was available for 13 models for the 1998 model year. Mexican plants scored better than U.S. plants for 4 models and equal to the industry average in two others. Overall, quality in both countries was comparable for both years.
Productivity is more difficult to compare even among plants producing identical models because it is dependent on factors such as capacity utilization; the number of operations done in the assembly plant versus those that are done at suppliers; and levels of automation. A plant employing more robots, for example, would score higher productivity than one with less automation, all other things being equal. As a result of far lower labor costs, Mexican plants tend to have fewer robots and therefore would record lower productivity. Less automation, however, tends to make these plants more flexible for rapid model changes.

"The ultimate flexible plant is a manual plant," commented Ron Harbour, the president of Harbour and Associates, a manufacturing consulting firm. "The Big 3 plants I’ve seen in the last couple years [in Mexico] are their leanest plants in North America. They’ve put many of the U.S. plants to shame" (Klayman 2000). *The Harbour Report: North America 2001*, a widely cited annual report on auto industry productivity, elaborated on these observations.

After visiting Mexican plants for several years, the report concludes “in almost every case, plants in Mexico have proven to be some of the best in North America, with high levels of quality, strong emphasis on safety, solid systems and processes, an emphasis on lean manufacturing and, maybe most important of all, an outstanding workforce committed to improvement” (Harbour 2001: 163). In commenting on an extensively reworked production line in an existing GM plant in Mexico, the report stated “reports say the company would have spent about four times the amount to create a similar plant in the United States” (Harbour 2001: 180). Of the 10 most improved assembly plants in terms of hours per vehicle (HPV) in 2000, the leading criteria Harbour uses to rank plants, 3 were located in Mexico (2001: 27). In a comparison of three newer Mexican assembly plants with US plants producing the same product, the Mexican plants showed impressive results. One Mexican plant required fewer hours, and although two Mexican plants required somewhat more hours, the numbers were relatively close and reflected lower levels of automation. (These plants produced over 500,000 vehicles in 2000, over one third of Mexico’s export production.) Given the high productivity and quality of Mexican plants, large wage differentials matter. The hourly compensation costs in U.S. dollars for manufacturing production workers in Mexico was only 11 percent of their U.S. counterparts in 1999 – $2.12 in Mexico versus $19.20 in the U.S. (BLS 2000: 14). In unionized U.S. automotive assembly plants, hourly rates approach $25 an hour compared to about $2.50 an hour in Mexican plants and total compensation can double these rates. The average vehicle took 26.4 hours to assemble in North America in 2000 (Harbour 2001: 59). At $50 an hour total compensation in the U.S. this would result in a labor cost of $1,320 per vehicle versus $132 in Mexico (at a total compensation of $5 an hour) or a difference of close to $1,200 per vehicle. If the Mexican plant required double the assembly hours of the U.S. plant, the difference would still be over $1,000 per vehicle. And these labor-cost savings are replicated throughout the supply chain, adding to a potentially significant cost advantage for a Mexican location and a strong incentive to shift production. As a point of reference, the most profitable U.S. automaker in 2000 was Ford which recorded about $1,500 per vehicle pre-tax profit in North America while Daimler-Chrysler achieved less than $200 per vehicle pre-tax earnings.

![Figure 6: U.S. – Mexico Auto Plant Productivity (Hours per Vehicle)](image1)

*Source: Harbour and Associates Report*

### 4. The productivity-wage relationship

Over the last several decades Mexico has recorded strong productivity growth in manufacturing while real wages have either declined or behaved sluggishly. From 1980 to 1993, for example, manufacturing productivity rose by 53 percent while real wages in pesos declined by 30 percent. Since 1993, manufacturing productivity has risen by 45 percent while real hourly wages in pesos remain 8 percent below their already depressed 1993 levels (INEGI 2001). Viewing a somewhat longer period, Rogelio Ramirez de la O concludes that “over the long run the decline in manufacturing employment and wages in Mexico is one of the most dramatic in any country in the world and at first sight in contradiction with a spectacular increase in exports and productivity, even after NAFTA has been in effect for six years” (2000: 119). Analyzing the period from 1970 to 1999 he points to a rise in manufacturing output of 219 percent and a decline of real wages of 22 percent (2000: 119). He then observes that “the benefits of structural change and export growth have not reached average wages…” (2000: 129).

Wage setting is a complex phenomenon that reflects government macro-economic policies, the average productivity in the economy, the real exchange rate, the number of people entering the labor force, employer strategies, and the strength of unions. A combination of Mexican government policy to attract investment and a lack of labor rights in the export sector have served to disconnect wages and productivity. As a *Human Rights Watch* report on NAF-
puts it in the context of the global economy "if we compete in the same product market as the Chinese, our workers have to be paid the same as the Chinese adjusted for productivity differences, if any" (Leamer 2000: 62). These global pressures are particularly apparent when unions seek to organize new workers in the U.S. Bronfenbrenner concludes that "capital mobility and the threat of capital mobility have had a profound impact on the ability of American workers to exercise their rights to freedom of association and collective bargaining" (2000: v). In a study of over 400 certification election campaigns, over half the employers made closing threats during the organizing drive, a figure that approached 70 percent in manufacturing. In the campaigns with threats, 18 percent of the employers threatened to move to another country, most usually Mexico (Bronfenbrenner 2000: vi). Bob King, the vice president of the United Automobile Workers (UAW) for organizing, places the threat much higher in terms of his own experience. "In manufacturing the threat of moving to Mexico is used in almost every campaign," he stated, adding "workers think it is a real threat." During an organizing campaign at an auto parts supplier in the late 1990s, supervisors made repeated verbal threats about plants closing and moving to Mexico throughout the campaign and then in the final days the employer distributed a leaflet that showed a padlocked plant bearing a sign that said "moved to Mexico." The UAW lost the election by 15 votes out of a 650 person bargaining unit. In another union organizing drive, the UAW received signed authorization cards from 80 percent of the eligible workers but after a fierce campaign in which the employer repeatedly threatened moving the plant to Mexico, the union lost the actual vote by a margin of 2 to 1. The ironically named Mexican industries, a now bankrupt Detroit-based auto supplier, was cited for fifteen violations of plant closing threats in an organizing campaign by the National Labor Relations Board (NLRB) (Bronfenbrenner 2000: 23). In one such case, the employer asked workers "if they planned to wear their T-shirts with the Charging Union's logo in Mexico," according to the NLRB. At Mexican Industries, a significant number of workers were undocumented which makes them extremely vulnerable in an organizing campaign and with far fewer options should the plant close and move. The UAW is currently in the midst of a highly visible organizing drive at Nissan in Smyrna, Tennessee which employs over 4,000 hourly workers. Nissan operates two major assembly plants in Mexico and supervisors have reportedly threatened the movement of new products and investment to Mexico should the union win the election. These threats are particularly unusual because they are happening early in the campaign. In many cases explicit threats do not have to be made because employees are well aware of the credible possibility of a plant moving, given the number of firms that have already taken that route.

In practice, while the threats are credible, they nonetheless often are not followed up by actual closures. Bronfenbrenner found that "after the election, employers followed through on the threat and shut down all or part of their facilities in fewer than 3 percent of the campaigns in our sample where threats were made," although she cautions that these results may have been too soon

TA's labor side agreement points out "Mexican law protects a broad array of labor rights. In practice, however, these are not enforced and are routinely flouted by employers in Mexico" (2001: 14). A key component of government economic strategy flowed through a series of economic pacts which began in December 1987. These pacts were ostensibly agreed to jointly by the government, the private sector, and the unions, although the government and private sector largely shaped the goals and a compliant, state-dominated labor federation was charged with implementing them.

The recent emergence of an independent labor federation in Mexico, the UNT, is an important development, but there are no independent unions in the maquiladoras (export-oriented assembly plants) and few in the export sector more generally. (A notable exception is at the massive Volkswagen manufacturing complex in Puebla.) The economic pacts not only depressed real wages in manufacturing but also dampened consumer demand and exacerbated Mexico's inequality. As Hernandez-Lazo concludes, "when union activity is absent, the benefits of productivity do not reach the workers" (2000: 241). In a study of unions and wages from the mid-1980s to the mid-1990s in Mexico, Fairris found that "roughly one-third of the increase in wage inequality over the period can be accounted for by the changing power of unions" (2001: 35).

The NAFTA labor side accord has been of little value in addressing labor violations in Mexico. Riddled with structural defects to start with, the pact has not even lived up to its limited potential. "... the NAFTA countries have ensured the accord's ineffectiveness in protecting workers' rights (2001: 1)," Human Rights Watch concluded.

Capital mobility in general and the expansion of the Mexican industrial base in particular has had a significant impact on U.S. industrial relations. As Leamer

Figure 7: Productivity and Real Wages in Mexico's Manufacturing Sector, 1993–2000
Source: INEGI: Banco de Informacion Economica
after the elections to estimate the total number of plants that eventually will move or shutter their operations (2000: vii). Bob King emphasizes that “if you run a good enough organizing campaign you can overcome [threats].” At the two campaigns mentioned above which the UAW initially lost, they were able to return in subsequent drives and win. Nonetheless, “if workers believe the threat to close the plant and move work, they will not vote for the UAW,” according to King, who also points out that “if the cost advantage is effective enough, [the employer] will move with or without a union.”

At Mexican Industries, UAW Local 600 is playing an unusual role that could shape future organizing campaigns. When the company declared bankruptcy and began shuttering its facilities, many workers who were migrants from Mexico blamed the union, associating it with government-dominated unions in Mexico. Initially surprised at the hostility and perceptions of many workers, the local union was able to show how hard it had fought to keep their jobs and engaged its resources to try to place people in new jobs at Ford and other suppliers it had organized. The local itself became an important community center for many of the displaced workers, offering English classes, food certificates, and advice. The result was a significant shift in perception and new commitment to the union among an important and fast-growing immigrant community.

5. Conclusion

While Mexico-U.S. trade has soared under NAFTA, Mexico has grown faster as an export platform rather than a consumer market. Contributing to this phenomenon is a paradox associated with a new international division of labor: world-class productivity and quality are driven by first world markets while wages are set based on third world institutions. On a micro-level, this paradox is underscored in the automobile industry in Mexico. This industry has effectively been integrated into the North American auto manufacturing complex with impressive outcomes at the same time that wages hover at a fraction of U.S. levels. These results have created incentives to invest in Mexico based on low wages and guaranteed by the general imprimatur of NAFTA and the specific investment guarantees it offers. Although many argue that labor standards have little place in trade agreements, the NAFTA experience indicates that a lack of strong labor standards may contribute to distorting a trading relationship. Ironically, the result dampens consumer markets in Mexico, thereby limiting trade, at the same time that U.S. workers are exposed to new downward pressures.

Abstracts


While Mexico-U.S. trade has soared under NAFTA, Mexico has grown faster as an export platform rather than a consumer market. Contributing to this phenomenon is a paradox associated with a new international division of labor: world-class manufacturing combined with low wages. This paper examines three dimensions of Mexico-U.S. trade: first, the overall nature of the trading relationship, focusing on "revolving door" exports; second, the emergence of Mexico as a high quality, high productivity exporter, a transformation illustrated through the experience of the automobile industry; and third, the institutional factors shaping the disconnect between Mexico’s increasing productivity and low real wages.

Notes
1 All trade data are from the United States International Trade Commission, Dataweb (http://dataweb.usitc.gov) unless otherwise noted.
3 SUV refers to Sport Utility Vehicles which include auto models such as the Ford Explorer and the Jeep Grand Cherokee. Autos, SUVs, and pickups together comprise the category "light vehicles."
4 Comparing the same model assembled in both the U.S. and Mexico minimizes variables that could influence the outcome such as the complexity of the design.

References
Kristina Pirker
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1. Einleitung

