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U.S.-Mexico Trade Relations

Overview

The U.S.-Mexico economic and trade relationship is of interest to U.S. policymakers, including Members of Congress, because of Mexico’s proximity to the United States, the extensive bilateral trade and investment relationship under the North American Free Trade Agreement (NAFTA) and its replacement, the U.S.-Mexico-Canada Agreement (USMCA), and the strong cultural and economic ties that connect the two countries.

Mexico’s Economy

Mexico is the second-largest economy in Latin America. It has a population of 129 million people, making it the most populous Spanish-speaking country in the world and the third-most populous country in the Western Hemisphere. Mexico’s gross domestic product (GDP) was an estimated \$1.1 trillion in 2020, equal to an estimated 5% of U.S. GDP of \$21.1 trillion. In terms of purchasing power parity (PPP), Mexican GDP was higher, \$2.4 trillion, or about 11% of U.S. GDP. Mexico’s per capita GDP is relatively high by global standards, and falls within the World Bank’s upper-middle income category. Trends in Mexico’s GDP growth generally follow U.S. economic trends, but with higher fluctuations.

U.S.-Mexico Trade

In 2020, Mexico was the United States’ second largest merchandise trade partner, after China. In U.S. merchandise exports, Mexico ranks second among U.S. markets after Canada. It also ranks second, after China, among suppliers of U.S. imports. The United States is by far Mexico’s most important export market for goods, with 80% of Mexican exports destined for the United States. Merchandise trade between the two countries increased exponentially since NAFTA entered into force. In 2020, the economic slowdown due to the Coronavirus disease 2019 (COVID-19) pandemic resulted in a 12% decrease in total bilateral merchandise trade from \$614.5 billion to \$538.1 billion. The merchandise trade balance went from a surplus of \$1.7 billion in 1993 (the year before NAFTA entered into force) to a widening deficit that reached \$112.7 billion in 2020.

U.S. Merchandise Exports

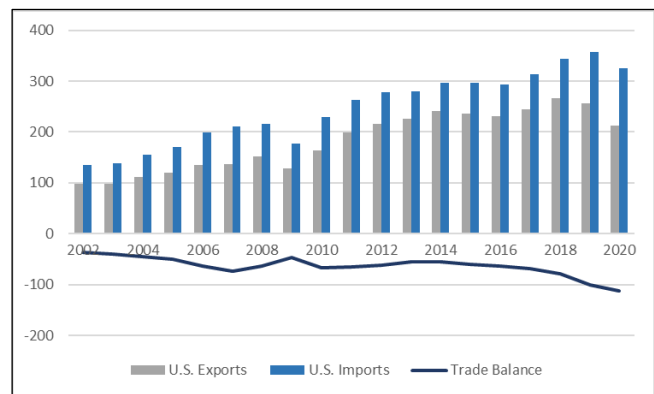
U.S. merchandise exports to Mexico increased from \$41.6 billion in 1993 to a peak of \$265.9 billion in 2018, and then decreased to \$212.7 billion in 2020. Leading U.S. exports to Mexico in 2020 consisted of petroleum and coal products (\$18.2), motor vehicle parts (\$15.8 billion), semiconductors & other electronic components (\$15.3 billion), computer equipment (\$11.5 billion), and basic chemicals (\$8.9 billion).

U.S. Merchandise Imports

U.S. merchandise imports from Mexico increased from \$39.9 billion in 1993 to \$358.0 billion in 2019, and then

decreased to \$325.4 billion in 2020. Leading U.S. merchandise imports from Mexico in 2020 included motor vehicles (\$56.4 billion), motor vehicle parts (\$43.7 billion), computer equipment (\$27.0 billion), audio and video equipment (\$12.7 billion), and electrical equipment (\$11.8 billion).

Figure 1. U.S.-Mexico Merchandise Trade 2002-2020
Current U.S. \$ in billions



Source: U.S. International Trade Commission’s DataWeb.

Services Trade

In services trade, the United States had a surplus with Mexico of \$3.1 billion in 2019, down from \$5.1 billion in 2018. U.S. services exports to Mexico totaled \$32.9 billion in 2019, up from \$14.2 billion in 1999, while imports increased from \$9.7 billion in 1999 to \$29.8 billion in 2019. U.S. services trade with Mexico largely consisted of travel, transportation, business, and financial services.

Bilateral Foreign Direct Investment

Foreign direct investment (FDI) is an integral part of the economic relationship between the United States and Mexico since NAFTA implementation. The liberalization of Mexico’s restrictions on foreign investment in the late 1980s and early 1990s, combined with NAFTA investment provisions, played an important role in attracting foreign investment to Mexico. The United States is, by far, the largest source of FDI in Mexico. According to the U.S. Bureau of Economic Analysis, the stock of U.S. FDI increased from \$37.2 billion in 1999 to a high of \$100.9 billion in 2019. While the stock Mexican FDI in the United States is much lower, it has increased significantly over the past 20 years, from \$3.0 billion in 1999 to \$42.9 billion in 2019 (by ultimate beneficial owner).

U.S.-Mexico Supply Chains

Many economists credit NAFTA with helping U.S. manufacturing industries, especially the U.S. auto industry, become more competitive through the development of

supply chains. A significant portion of merchandise trade between the United States and Mexico occurs in the context of production sharing as manufacturers in each country work together to create goods. The flow of intermediate inputs produced in the United States and exported to Mexico and the return flow of finished products greatly increased the importance of the U.S.-Mexico border region as a production site. U.S. manufacturing industries, including motor vehicles and electronics, all rely on the assistance of Mexican manufacturers. In the auto sector, for example, there are multilayered connections between U.S. and Mexican suppliers and assembly points. An automobile produced in the United States, for example, can have thousands of parts that come from different U.S. states and various Mexican locations. The place of final assembly may have little bearing on where its components are made. Most economists suggest that these linkages offer important trade and welfare gains from free trade agreements.

NAFTA and the USMCA

NAFTA, which entered into force on January 1, 1994, contained provisions on tariff and nontariff barrier elimination, customs procedures, energy, agriculture, technical barriers to trade, government procurement, foreign investments, services trade, temporary entry for business persons, intellectual property rights protection, and dispute resolution procedures. NAFTA was the first U.S. free trade agreement with labor and environmental provisions. See CRS Report R44981, *The United States-Mexico-Canada Agreement (USMCA)*, by M. Angeles Villarreal and Ian F. Ferguson.

On July 1, 2020, USMCA replaced NAFTA. It retains many of NAFTA's chapters, while making notable changes to others, including on those related to market access provisions for autos and agriculture products, rules on investment, government procurement, and intellectual property rights (IPR). It also contains stronger labor and environmental provisions and adds new chapters on digital trade, state-owned enterprises, and currency misalignment.

NAFTA's requirements of 62.5% North American content for motor vehicles and 60% for all other vehicles and automotive parts are tightened under USMCA. The new rules require that 75% of a motor vehicle and 70% of its steel and aluminum originate in North America and that 40%-45% of auto content be made by workers earning at least \$16 per hour. Side letters exempt up to 2.6 million vehicles from Canada and Mexico annually from potential Section 232 auto tariffs.

USMCA maintains the NAFTA state-to-state mechanism for the settlement of most disputes as well as the binational dispute settlement mechanism to review trade remedy disputes. However, it maintains investor-state dispute settlement (ISDS) only between the United States and Mexico, without Canada, regarding government contracts in oil, natural gas, power generation, infrastructure, and telecommunications sectors. It also maintains U.S.-Mexico ISDS in other sectors provided the claimant exhausts national remedies first, among other changes.

Issues for Congress

USMCA

U.S. policymakers may follow trade policy issues regarding USMCA. Some policymakers view the agreement as vital for U.S. firms, workers and farmers, and believe that the updated agreement will benefit U.S. economic interests. Others are concerned over Mexico's implementation of USMCA worker rights provisions and the ability of the Mexican government to implement required labor reforms. Other concerns include the scaling back of ISDS provisions and the effect on U.S. investors in Mexico, especially in the energy sector. The U.S. business community contends that USMCA will strengthen North American supply chains and help the region recover from the COVID-19 pandemic. Nevertheless, others are concerned about Mexico's recent steps to strengthen the state's role in the energy sector and argue that these actions violate USMCA and could adversely affect U.S. investment in Mexico's energy sector.

The full effects of the USMCA on the U.S.-Mexico trade relationship are not expected to be significant, because nearly all U.S. trade with Mexico that meets rules of origin requirements has been conducted duty and barrier free for many years under NAFTA. The USMCA maintains NAFTA's tariff and non-tariff barrier eliminations. Many economists believe that USMCA is not expected to have a measurable effect on U.S. trade and investment with Mexico, jobs, wages, or overall economic growth.

Bilateral Economic Cooperation

The United States shares strong economic ties with Mexico and any disruption to the economic relationship could have adverse effects on investment, employment, productivity, or North American competitiveness. The COVID-19 pandemic has raised new issues regarding the U.S.-Mexico supply chain and North American manufacturing. Policymakers may consider issues on how the United States can improve cooperation with Mexico in areas of mutual interest such as coordination on essential services. Some policy experts encourage increased bilateral cooperation in cross-border trade and investment. Mexican officials have pointed to a USMCA-established "Competitiveness Committee" as an important framework through which the two countries can advance shared interests. U.S. Trade Representative Katherine Tai met with her Canadian and Mexican counterparts in March 2021 and discussed USMCA implementation efforts, reportedly committing to holding a USMCA Free Trade Commission meeting soon.

For more information, see CRS Report R42917, *Mexico: Background and U.S. Relations*, by Clare Ribando Seelke and CRS Report RL32934, *U.S.-Mexico Economic Relations: Trends, Issues, and Implications*, by M. Angeles Villarreal.

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