The north american free trade agreement

Terminal Objective #8 The North American Free Trade Agreement, which was ratified on January 1994, aims to remove the trade and investment barriers among the United States, Canada and Mexico. The impact of NAFTA to US in particular is remarkable specifically in the agricultural sector as the agreement intends to eliminate all agricultural tariffs and quotas by 2008 (Foreign Agricultural Service, 2005). This paper focuses on the benefits derived from and downside of the NAFTA for economic participants in the US.

The positive effect of NAFTA can be illustrated citing the bilateral agricultural trade between the US and Mexico for select products. For instance, the US is able to substitute the production of corn and nut at the exchange ratio of . This means that at optimal labor utilization it can either produce, say 600 pounds of corn or 300 pounds of nuts. Meanwhile, Mexico is able to substitute the production of same products at the exchange ratio of . As such, it may choose to produce either 200 pounds of corn or 150 pounds of nuts. (Samuelson & Nordhaus, 2000)

Upon opening up or liberalizing trade between the two nations, their initial production possibility curves, represented by the solid line, pivot. In case of the US, it could still produce 600 pounds of corn. However, with trading with Mexico, it may now end up with relatively more nuts using Mexico's price ratio. Similarly, Mexico ends up with the same quantity of nuts but this time it may end up with more corn as it traded with Mexico at the latter's price ratio. The above example exhibits the benefits derived by countries, particularly exporters and consumers, when countries open up to trade or undergo trade liberalization. According to the Foreign Agricultural Service

(2005), sales of corn to Mexico and Canada increased by 175% with exponential increase in export value between 1993 and 2004. In this case, farmers are able to find overseas markets for their harvest, thus, enhancing their earnings potential. Similarly, consumers also gain as more producers, both foreign and local, enter the domestic market. This is because increased competition especially for agricultural products bids down prices. They also get to enjoy higher quality products as businesses are driven to compete through quality aside from pricing in order to profit.

However, this may not bode well with local producers as their profits are squeezed with the presence of foreign competition in the domestic industry. As such, local producers, particularly those with limited capitalization and exclusively cater to local consumers, may opt to shut down business with unprofitable operations given shrinking market share. With this, losers may also include those people who lose their jobs when these businesses seized to operate. (Mankiw, 1999)

Works Cited

Foreign Agricultural Service, 2005. " Benefits of NAFTA." Available from: www. fas. usda. gove/itp/policy/nafta/nafta_backgrounder. htm [23 April 2007].

Mankiw, G., 1999. Macroeconomics. W. H. Freeman & Company

Samuelson, P. and W. Nordhaus, 2000. Economics. McGraw-Hill.

.