

# TEXAS

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### Three's Company

#### U.S. Borders After September 11

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The terrorist attacks on the World Trade Center and the Pentagon on September 11, 2001, brought the issue of U.S. border security to the forefront. In the weeks following the attacks, heightened U.S. security measures caused serious delays on the northern and, especially, the southern borders. Increased security will in turn increase the cost of business in the North American Free Trade Agreement (NAFTA) countries. Resources must be deployed in a way that minimizes the economic costs of doing business across the borders of an increasingly integrated North American economy. At the same time, this must be accomplished without compromising U.S. security needs. Therein lies the dilemma.

#### Border Talks before September 11

While in Washington in early September 2001, Mexican President Vicente Fox raised the issue of legalizing the status of illegal migrants in the United States through some form of guest worker permits. On October 5, during his first U.S. visit after the September 11 attacks, President Fox reiterated his vision of a trilateral cooperation: "We have to share information about intelligence, share control of migratory movements, customs issues, information about airports and aircraft in our territories."

Such cooperation has long been a given in the U.S.-Canada relationship. Prior to the attacks, the notion of a common security perimeter was widely discussed in Washington and Ottawa. Amid security concerns and growing cross-border traffic, U.S. Ambassador to Canada Paul Cellucci suggested that Canada, the United States, and Mexico jointly manage external border entry points while dismantling internal borders. The Canada-United States Partnership (CUSP), an advisory group created by Prime Minister Jean Chrétien and President Bill Clinton in 1999, recommends policy harmonization on visa requirements, immigration, and security operations between Canada and the United States, and many Canadians support the idea as a means to reduce border frictions and the potential for gridlock. Indeed, a recent survey found that 85 percent of Canadians generally favor making the changes necessary to create a North American security perimeter. Although some Canadian officials object to the notion of policy coordination, voicing concerns over the independence of Canadian policy and the implications for Canadian sovereignty, the Canadian government has already begun the process of harmonizing some of its laws with the United States, introducing draft legislation on terrorism, border operations, and immigration procedures.

The number of people deported by the U.S. Immigration authorities fell by 40 percent during the first month after the attack. Moreover, efforts by the United States to legalize this flow of Mexican migrants will likely be delayed by the heightened concerns over border security.

Essentially, a common perimeter between Canada and the United States would mean that people or goods entering either country from other countries would gain entry to both simultaneously. But what about the third NAFTA partner? Where does Mexico fit in this equation?

### **Border Realities after September 11**

Unlike U.S.-Canada interactions, the U.S.-Mexico relationship is more fraught with mistrust, and nowhere is this more in evidence than along the border between the two countries. Security at the U.S.-Mexico border contrasts sharply with that at the U.S.-Canada border. At the time of the terrorist attacks, the United States employed 334 border patrol agents and 498 inspectors on the Canadian border and 8,893 agents and inspectors on the Mexican border, with more than 1,400 in Arizona alone. The northern border ratio is one border guard for every 4,000 legal crossings; on the southern side, one border guard for every 1,100 legal crossings. Clearly, most of the guards on the U.S.-Mexico border are deployed to catch illegal crossings.

September 11 only exacerbated these differences. Following the terrorist attacks, the U.S. customs service stationed one hundred extra officers on the Canadian border in order to staff all crossing points 24 hours a day. Initially, wait times to enter the United States increased dramatically—as much as twelve hours in some instances. Those times were reduced to near normal within one week (in part due to a sharp drop in freight volumes). The story was very different, however, on the southern boundary of the United States, the busiest border in the world. Trucks formed long lines on the Mexican side, and, in some cases, they were delayed by days, upsetting production schedules of U.S. manufacturing companies that depended on intermediate goods for just-in-time production processes.

Obviously, Mexico is one of the countries most adversely affected by the terrorist attacks on the United States. Extra security on the border has slowed the passage of goods and people. The economic impact on the United States echoes across the border in Mexico. Almost 90 percent of Mexican exports are destined for the United States and roughly one-third of the Mexican economy depends on trade. Manufacturing in Mexico grew at the rate of 10 percent annually between 1996 and 2000. Much of this growth resulted from the export of durable goods. In September 2001, U.S. consumption of durable goods decreased by 8 percent, *the single biggest monthly drop ever recorded*.

Movement, both legal and illegal, across the border has also been severely affected. In the first month after the attacks, big tourist resorts in Cancun and Acapulco reported a 50 percent decrease in tourism. Likewise, the hundreds of thousands of poor Mexicans who cross the border illegally each year now find their passage north even more difficult, as indicated by indirect evidence: the number of people deported by the U.S. Immigration authorities fell by 40 percent during the first month after the attack. Moreover, efforts by the United States to legalize this flow of Mexican migrants will likely be delayed by the heightened concerns over border security.

This economic damage, coupled with the criticism leveled at Mexico for its lukewarm response to U.S. calls for international anti-terrorism efforts (initial polls showed 62 percent of Mexicans favoring neutrality), have provoked some soul searching among Mexicans that may ultimately do much to improve the relationship between these neighbors. Mexican authorities cooperated fully with their American counterparts to monitor the flow of people from the United States to Mexico in the days following the attacks. The Mexican airlines worked with the Federal Aviation Administra-

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tion to meet U.S. security standards. In fact, the two largest Mexican carriers, Mexicana and AeroMexico, already have code-sharing agreements with United Airlines and Delta Airlines. Regardless of past difficulties, it is even more imperative now that Mexico and the United States work more closely on security issues. And paramount among these issues is the cross-border movement of people.

### Moving People: Trilateral Cooperation?

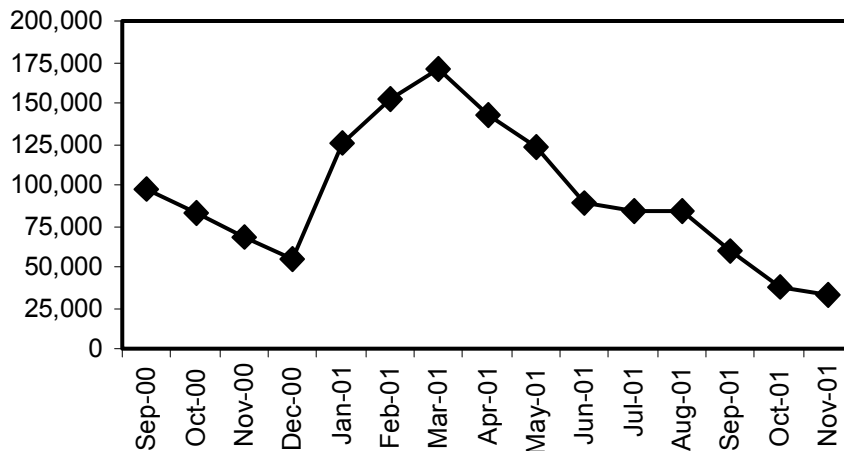
The exact implications of September 11 for the movement of people across borders remain unclear. Roughly 5 million Canadians and 6 million Americans cross the northern border each month. An estimated 25 million people cross the southern border each month. Although Mexicans may prove more resistant than Canadians to the notion of giving up some national sovereignty to ensure the security of the region, the Fox administration has improved cooperation on many fronts, including a degree of harmonization of immigration policies in order to reduce the attractiveness of Mexico as a gateway for

people smugglers whose destination is the United States. Nevertheless, many U.S. lawmakers continue to resist the Mexican government's push for some form of legalization for the estimated 3 million undocumented Mexicans working in the United States.

Illegal immigration from Mexico represents both a blessing and a curse for the United States. The U.S. economy benefits from a much-needed supply of labor. On the other hand, the illegal flow of people promotes more illegal activities, such as people smuggling and the abuse of undocumented workers' rights.

In the long run, demographic and economic trends could force a resolution to the problem. Projections for the next thirty years point to increasing shortages of labor in the United States and a rapidly aging population in Mexico that will reduce the number of young men making the journey north to the United States. Economic trends in Mexico will likely raise incomes sufficiently over the same period of time so that the same degree of openness the United States affords Canadians can also be achieved for Mexicans.

**Border Patrol Apprehensions of Illegal Migrants on the Southwest Border, September 2000-November 2001**



Source: U.S. Immigration and Naturalization Service, *Monthly Statistical Report*.

The tighter security on the Mexican border remains insufficient to stop the annual passage of 300,000 illegal migrants who remain in the United States, making it a less than optimal solution over the long term.

In the meantime, however, border issues related to the mobility of people will probably not be addressed on a trilateral basis among the members of NAFTA. Such issues have not been addressed trilaterally in the past, primarily due to the dramatic differences in standards of living. The United States requires visas for Mexicans but not for Canadians and imposes a limit of 5,500 NAFTA visas for Mexican white-collar workers but no limit for Canadians. U.S. customs officers are stationed at airports in Canada, but not at airports in Mexico because of Mexican constraints on U.S. law enforcement operations within that country. The United States continued to resist the entry of Mexican trucks long after they allowed Canadian trucks to operate in the country. Many border issues are handled on a bilateral basis, and that format may continue.

The impact of September 11 may be to perpetuate the existing asymmetries in the bilateral border relationships in North America with respect to the movement of people. National security takes precedence over trade under the trade agreements that apply and is perhaps the broadest exception contained in those agreements. Despite recent advances in the relationship between Mexico and the United States, the Canadian border remains more open to the movement of people and can be policed with fewer personnel. However, the tighter security on the Mexican border remains insufficient to stop the annual passage of 300,000 illegal migrants who remain in the United States, making it a less than optimal solution over the long term.

### **Movement of Capital: What Does NAFTA Say?**

On the surface, free capital movement is already a fact among NAFTA countries, although, for security purposes, each of the three governments may exercise a lot of discretionary power in the financial sector. More than 70

percent of banking capital in Mexico is under foreign control. In mid-2001, the largest bank in Mexico, Banamex, was taken over by Citigroup, which took the unprecedented step of listing itself on the Mexican Stock Exchange, the first foreign company ever to do so. More than half of the insurance industry in Mexico is under foreign control as well. Canada is the largest foreign real estate owner in the United States, which, in turn, is the largest source of foreign investment in Canada. A recent flurry of cross-border mergers and acquisitions in the financial sectors of the United States and Canada has further blurred financial borders.

NAFTA has done much to break down barriers to cross-border capital flows. The agreement applies to “persons” of a NAFTA country, that is, citizens or permanent residents of a NAFTA member or a business organized under the law of a NAFTA member. Thus, as long as a company from outside the region meets the requirements for incorporation (or other forms of business organization) and complies with foreign investment laws, it may become a NAFTA company. However, companies that are controlled by investors from outside the region with no substantial business activities in the territory of the country under whose laws it is constituted may be denied NAFTA benefits. Benefits may also be denied if a NAFTA country does not maintain diplomatic relations with the investor’s home country or prohibits business transactions with enterprises from that country.

NAFTA provides standards for the treatment of foreign investors. Standards of nondiscrimination require that equal treatment be accorded foreign and domestic investors and that all foreign investors be treated equally. In addition, foreign investors are entitled to a minimum standard of treatment: each country must treat investors in accordance with customary international law, including fair and equitable treatment and full protection and security.

The agreement also prohibits restrictions on transfers of profits, proceeds, or payments, unless the restrictions are due to the application of laws relating to bankruptcy, securities, criminal offenses, currency transfer reporting, or enforcement of judgments. Governments therefore remain free to restrict transfers under laws such as those relating to money laundering and those that permit the freezing of assets in litigation and bankruptcy proceedings. Following September 11, the NAFTA governments used money laundering laws to deal with terrorist funds.

NAFTA also contains a more general national security exception that applies to all of its provisions, including the treatment of foreign investors. Because it is so broad and discretionary, this exception could be used to restrict capital movements whenever one of the governments considers such restrictions necessary for the protection of its essential security interests in a time of war or other emergency in international relations. While there have been no cases interpreting this provision under NAFTA or the equivalent provision under the General Agreement on Tariffs and Trade (GATT), capital restrictions placed on terrorist funds in the context of the September 11 attacks would very likely qualify under this exception. Support for this view may be found in the preparatory work relating to the equivalent GATT security exception. One of the drafters of the original charter stated: "We cannot make it [the security exception] too tight, because we cannot prohibit measures which are needed purely for security reasons. On the other hand, we cannot make it so broad that, under the guise of security, countries will put on measures which really have a commercial purpose." In the case of restrictions on terrorist funds, the purpose of the measures would clearly be related to their security interests, not a commercial purpose.

## Movement of Goods

Heightened security efforts will increase the cost of moving goods across the border. This will impose a higher cost of producing goods with production systems spread across the borders. This might slow the process of integration across the three countries. With technology and the large-scale movement of goods, NAFTA countries should be able to exploit economies of scale. Thus, the additional long-run marginal cost may be negligible. An instructive example can be drawn from the seizure of illegal drugs, a barometer of the drug trade (between Mexico and the United States). For the first two weeks after September 11, the drug seizures across the border were down by half. By early October, the drug seizures were back to pre-attack level, indicating that traffickers quickly found alternative ways of keeping up their supply. The same could apply for the movement of legal goods within a few months.

## The Importance of Including Mexico

The movement of illegal goods and illegal migrants also points to the importance of Mexico. Ignoring Mexico leaves a large hole in the U.S. security perimeter. If it is so easy for goods and people to move across the border, how does the United States plan to improve security without Mexican cooperation? As long as the United States cannot set up an impenetrable fence across its southern border, it needs Mexico to be a part of the security strategy. The uneasy history between the two neighbors, however, complicates the task confronting policymakers on both sides of the border as they consider new security realities after September 11. ♦

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### Value of U.S. Merchandise Trade with Canada and Mexico Compared with U.S. Trade with All Other Countries, 1996-2000

Year	Total U.S. trade (current \$ millions)	U.S. trade with NAFTA partners (current \$ millions)	U.S. trade with all other countries (current \$ millions)	Ratio: U.S.-NAFTA to all U.S. trade (percentage)
1996	1,420,364	421,192	999,172	29.7
1997	1,557,472	475,382	1,082,090	30.5
1998	1,594,000	502,715	1,091,285	31.5
1999	1,717,587	558,987	1,158,600	32.5
2000	1,997,306	653,270	1,344,036	32.7

**Sources:** U.S. Department of Transportation, Bureau of Transportation Statistics, special tabulation, April 2001; based on total trade, air and water--U.S. Department of Commerce, U.S. Census Bureau, Foreign Trade Division; all land modes--U.S. Department of Transportation, Bureau of Transportation Statistics.

## Announcement

### Women's Business Leadership Conference *Charting New Landscapes*

The Bureau of Business Research and The McCombs School will host this one-day event for matriculated and prospective MBA students on Friday, February 15, 2002. The conference will feature Bernee Strom, CEO of The Strom Group, as keynote speaker and will include panels of business leaders, entrepreneurs, and managers discussing topics such as managing in the corporate environment, balancing work and home life, and working in a small high-tech firm. Registration is free but space is limited. Visit the conference website (<http://texasmba.bus.utexas.edu/MBAWomen/conference/>) or call (512) 475-7813 for information. ♦