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The Second Decade of the Twenty-first Century: Factors of Uncertainty and Economic Crisis in North America

Introduction

A series of factors can be identified beginning in 2020 that, together, have led to uncertainty both on a global and regional level; they have not been transitory, as originally thought, and neither do they seem to offer conclusive responses.

In the North American region, economic uncertainty regarding productive, trade, and financial growth is not isolated from crucial issues of health, geostrategy, or climate, and some of its manifestations and the responses and policies to deal with it particularly affect the countries linked up by trade agreements for almost thirty years.

Outstanding among the factors determining this uncertainty is the Covid-19 pandemic, because of its devastating repercussions in health, death rates, and people's day-to-day socioeconomic activity. In the three USMCA countries, the health emergency caused the reduction or temporary close-down of economic activity, and this is reflected in the degrowth of production, the disappearance of thousands of jobs, and high inflation.

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The second fundamental aspect, not only in the United States, but also regionally and internationally, came in November 2020 when Joe Biden won the presidency and, on January 20, 2021, took office amidst an unprecedented crisis of electoral and democratic legitimacy. In addition, under his leadership, the United States is facing a domestic economic crisis and, undoubtedly, the policies undertaken and their results will directly impact North America because of its central role in the region.

The third crucial aspect in these countries is trade, with the implementation of the U.S.-Mexico-Canada Agreement (USMCA) on July 1, 2020. This made for important changes in the rules of origin for the auto industry and new stipulations in other areas, such as labor rights, intellectual property, and digital trade. The treaty has also taken on more importance for President Biden due to the cooperation that can exist for strengthening regional value chains, while also allowing for a process of re-localization of companies, nearshoring, in North America, especially in Mexico. At the end of the day, nearshoring will contribute to replacing Asian imports because that production would be carried out in this region.

The Pandemic

In March 2020, the World Health Organization declared Covid-19 a pandemic, taking into consideration its contagion rate and its seriousness since it has caused millions of deaths worldwide. It was not until late 2020 that the first vaccinations were given, which has slowly contained the disease.

Both vaccination and support programs made it possible to reestablish educational, productive, and social activities. However, statistics from 2020 show that the degrowth of production was severe and unemployment and inflation levels, very significant.

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In that year, the region's three countries suffered a declining gross domestic product, but the sharpest declines, of two digits, came in the second quarter. Nevertheless, in the three following quarters, with better handling of the pandemic, vaccinations, and government support, the drop was considerably less. By 2021 and 2022, the situation had already been reversed, and the three countries maintained their productive recovery and showed positive annual Global Domestic Product (GDP) rates.

On the other hand, as mentioned above, the pandemic affected employment drastically; paralyzed production resulted in high unemployment for the three economies in 2020. The monthly evolution of this indicator shows similar performance as that of GDP, since the greatest job losses also came in the second quarter; in the U.S. they reached two digits, which had not happened since the 2008-2009 economic crisis. However, just as what happened with GDP, unemployment rates dropped consistently later, returning to pre-pandemic levels.

The War

Although the economic situation improved, other events added to economic uncertainty and insecurity. In the first place, after the large scale Russian invasion of Ukraine in February 2022, both the United States and Europe imposed sanctions on the Russian energy sector, including banning investment in it and restrictions on its exports. This caused a rise in international oil prices, and therefore also gas prices. Just to give an example, around June 2022, in California the price of a gallon of gas rose to over US$6, when in December 2021, the average price had been US$3.33. With a few differences, the hike impacted the entire North American region and influenced each of the three countries to raise the cost of a wide variety of goods and services, prompting high inflation.

The war caused interruptions in the supply of fertilizers for agricultural production, affecting different crops. This was added to extreme weather events like flooding and droughts, which generated scarcity and very high food prices.

Clearly, many factors have fostered the insecurity we are experiencing, and in most cases, there are no immediate solutions; therefore, they will continue to exist in the short run. However, regarding controlling inflation, the central banks of North America and other regions have applied the traditional measures, fundamentally based on increasing interest rates.

Little by little, high inflation has been easing, but at the cost of growth and investment, leading to predictions of a recession in the United States in mid-2023. In that case, both Canada and Mexico will be directly affected negatively because of their close productive and trade relationship with that country.

Trade Policy under the Biden Administration

Since the beginning of his administration, Joe Biden has clearly stated his position about the need to transform foreign policy, and trade policy in particular. In fact, even as a candidate, he had made different criticisms of Donald Trump's foreign policy.

In this sphere, Biden said that some of the trade conflicts Trump had sparked even with friendly countries had been counterproductive. He classified calling imports from friendly nations a threat to national security, which even led Trump to impose tariffs, a mistake.

One example of this was in March 2018, when Trump decided to levy tariffs on steel and aluminum from everywhere, including his North American Free Trade Agreement (NAFTA) partners. This led both Mexico and Canada to levy "mirror" tariffs on goods produced in the United States.

Biden has decided to put to one side Trump's unilateral practices and rhetoric, which created a climate of threats and reprisals; and it is clear how the terms of trade relations have changed in North America.

By contrast, these changes have not applied to China, and trade relations have tensed even more. Biden has promoted greater trade restrictions with China, increasing the tariffs between the two countries. This firm position is not surprising given that he has said that China represents a real economic threat and has openly accused it of stealing technology and intellectual property from U.S. companies.

The USMCA

Despite the new trade deal containing important changes vis-à-vis NAFTA, undeniably, the central discussion and the most important clauses in the new treaty are aimed at the auto industry, for which changes in the rules of origin were negotiated. The percentages of regional content required to receive preferential tariff treatment increased particularly for vehicles and auto-parts. These new stipulations in the USMCA aim fundamentally to prevent auto parts and components from third countries (Asia, Europe, or South America) from being incorporated into vehicles produced in North America, replacing parts made in the region.

Considering these objectives, the profound regional integration of this and other industries, as well as the vulnerability caused by disruptions in the supply chain, the presidents of North America have proposed deepening economic cooperation, promoting investment, and strengthening innovation and resiliency.

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This commitment agreed on in early 2023 among the USMCA partners stems from the need to reduce the risks of new breaks in the supply chains, above all in the case of semiconductors. We must remember that in 2020, during the pandemic, auto plants were closed for several weeks and therefore, their orders for semiconductors dwindled. Semiconductor manufacturers, therefore, changed their focus to making those needed for consumer electronics like computers and cell phones, which were under heavy demand due to the lockdown and millions working from home.

Therefore, when the economic recovery began, those manufacturers could no longer immediately supply the auto industry; in fact, scarcity led some plants in North America to stop production for weeks or even months.

It should be mentioned that today, both the United States and a large part of the world depend to a great extent on Asian companies, especially from Taiwan, South Korea, and China, for advanced semiconductors, since they concentrate almost 90 percent of the world's production.

The problem that had originated in the supply chains led Biden to commission a report in February 2021, which showed the supply risks involved in four classes of products, among them, the semiconductors and batteries used in electric vehicles. Undoubtedly, that document outlined the establishment of the commitment by the North American presidents to decrease their vulnerability and promote the strengthening of the supply chains.

Finally, this was also based on relocation of companies that want to be close to the enormous U.S. market. This process can be seen, especially in the case of Mexico, which would also contribute to the substitution of Asian imports, since production would be carried out in this region, taking advantage of the USMCA-established conditions. In fact, the companies most interested in relocating to Mexico are Asian.

Amidst the unfavorable context derived from the pandemic, the war between Russia and Ukraine, and the weather factors that, together, have caused inflation, the USMCA came into effect and continues being the axis for productive and trade integration in North America.

In early 2023, information about companies interested in relocating to our country —seemingly between seventy-five and one hundred— is barely being gathered. According to available information, northern Mexico would be the most sought-after destination. In the first place, relocation would seem very positive; however, challenges exist that must be taken into account, among them infrastructure. On the other hand, the preference for locating in northern border states would accentuate the tendencies toward regional inequality in the country, especially between Mexico's North and South.

Conclusions

When 2020 was just beginning, North America was going through very critical events that caused economic uncertainty and insecurity. Despite the global character of some of them, their manifestations and possible solutions acquired a national or regional character.

In the first place, the Covid-19 pandemic impacted heavily, not only in the sphere of health and the lives of the populace, but it also changed and to a great extent stopped economic and social life. However, the vaccination programs implemented in this region mitigated contagion and activities slowly recovered, although full control of the situation has not been regained.

The broad vaccination coverage in the three countries, added to diverse kinds of support and stimuli, managed to invigorate the economy and decrease unemployment, reversing the slumps in these spheres. In that period, Joe Biden took office, which made for a very positive change in his country's foreign and trade policies. The rhetoric has changed radically, and everything indicates the United States will return to multilateralism.

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Lastly, a collateral result of all these conditions is that in the coming years, it is predicted that companies will want to relocate in the North American region, especially in Mexico, in order to be close to the U.S. market. This would broaden out the opportunities for our country to insert itself into the regional value chains.