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The Triangular Balance: Mexico, the United States, and China

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Contents

Introduction

The outbreak of the trade war between China and the United States launched a debate on issues ranging from how to reshape North American integration—which led to the replacement of the North American Free Trade Agreement (NAFTA) with the United States—Mexico—Canada Agreement (USMCA)—to whether decoupling from China was possible and advisable[1]. A topic that is implicitly incorporated in those debates is Mexico's position *vis-à-vis* China.

Mexico and China established diplomatic relations in 1972, and since then, the bilateral engagements have been increasing, although the pace of such exchanges accelerated in the early 2000's. It is fair to say that Chinese presence and influence in Mexico does not follow the pattern witnessed in the rest of the Latin American countries, where Chinese products, investment, and technology are more evident[2].

This has been in part because the manufacturing industries of China and Mexico largely compete for the same export markets, fueling the distrust and resentment of business communities in both countries. Moreover, despite the improvements in the relationship, there have been few events in the recent past that created a difficult environment—Mexico's reluctance to grant its approval for China's accession to the World Trade Organization (WTO), the cancellation of a highspeed train that had been awarded to a Chinese company, and the cancelation of a shopping mall called Dragon Mart in Cancun.

However, none of these circumstances stopped China from becoming the US' largest supplier, and Mexico's second source of imports. This trade flows reflect a little acknowledged fact: in a way, China became the adhesive that held North America together because of its contribution of affordable inputs and raw materials, which in turn were incorporated into Mexican exported goods. At the same time, consumer in both Mexico and the United States benefitted from cheap Chinese goods and low inflation rates[3].

It must be highlighted that this trade configuration happened by design; that is, the existence of a free trade agreement between Mexico and the United States, coupled with low tariffs for Chinese goods, were bound to create the conditions described. As this paper will discuss, it is important to consider the changing political context in Washington towards China, and how Mexico could respond to it.

This will be even more important in the context of the 2026 USMCA review. It has been touted already that China will be an important driver of such discussions[4], although the topics to be addressed at the review have yet to be decided.

It is expected that Washington's animosity towards Beijing will not change in the near future, regardless of who wins the upcoming US elections in November. What is less clear is how Mexico will handle its relationship with China, especially after the governing party (Morena) won the June general elections with an overwhelming majority. On the campaign trail, Morena's candidate, Claudia Sheinbaum, stated that Mexico's relationship with the United States was vital for the country, but after she received a congratulatory letter from President Xi Jinping, she underlined that relations between Mexico and China will continue to strengthen[5]. It remains to be seen how such contrasting views are integrated into her government plan.

Ideally, Mexico and the United States should have an understanding—if not outright cooperation—on how Beijing should be approached, and ideally, a joint position should spring naturally from the two neighbors. Yet, the reality is much more complex, especially since Chinese companies have started to invest in Mexico, and although the amount is still a slight fraction of the foreign direct investment (FDI) inflows that Mexico receives every year, the expectation is that such investments will increase in number and in quality, which has caused concern (and some incendiary remarks) from the United States.

The issue is further complicated because, should the United States attempt to coerce Mexico into adopting a specific position towards China, the result could be the exact opposite of what Washington wishes to accomplish. Indeed, it is wrong to assume that Washington can fully shape Mexico's policy towards China. Mexico is deeply protective of its own foreign policy[6], and there are legitimate reasons that Mexico could argue for defending its relationship with Beijing, independently from Washington.

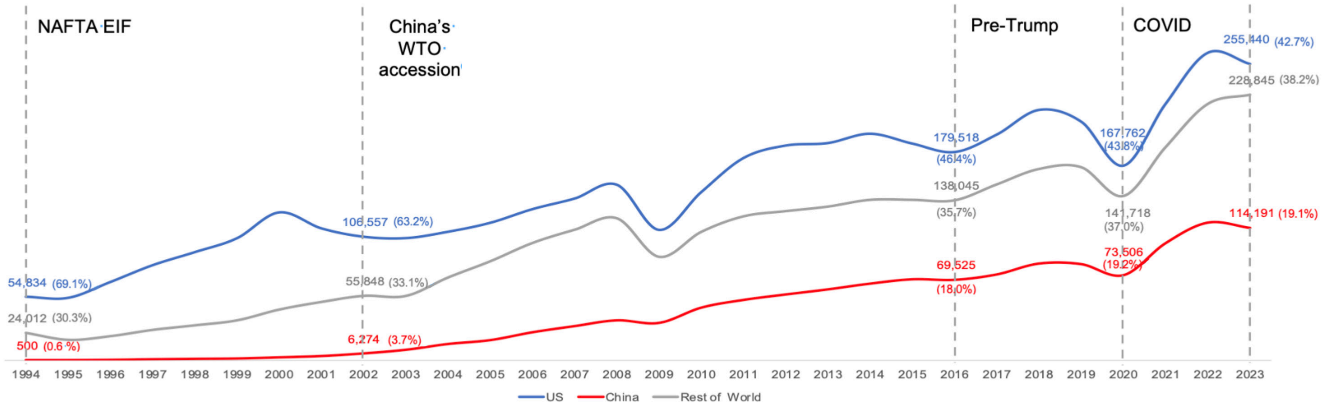
A North American discussion must include Canada, especially ahead of the USMCA review, in which Canada will be an active participant. It could be argued that given Canada's political climate, it is less likely to diverge significantly from Washington's policy towards China. In fact, there have already been public differences between Ottawa and Beijing[7]. Such analysis, as important as it may be, is beyond the scope of this paper but must certainly be developed because the decisions taken towards China will be crucial for the future of North American regional integration.

Thus, this document will begin by discussing the actual size of Chinese trade and investment in Mexico and the United States, and how the US and Mexico have responded to this dynamic. This paper will then explore the implications of China ahead of the 2026 USMCA review, concluding with some reflections on the importance of striking a trilateral balance between Mexico, the United States, and China.

Contemporary Mexico and China trade relationship

Since NAFTA's implementation in 1994, Mexico's imports from China have consistently risen, going from $6.2 billion in 2002- the year China joined the World Trade Organization (WTO)- to $114.1 billion in 2023. Consequently, China has swiftly gained a significant share of the Mexican market, reaching over 19% in 2023. This growth corresponds with a decline of over 20 percentage points in the US share of the Mexican market during the same period—it is worth noting that China became the US' main supplier in this same period.

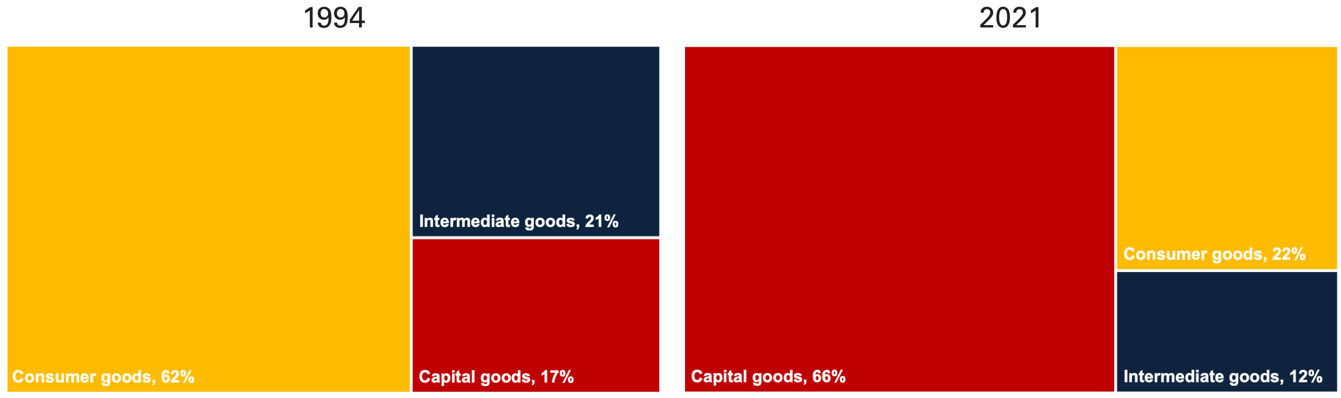
Figure 1: Imports into Mexico and market share growth



Market share is indicated in parentheses. Source: Banxico, 2024.

More importantly, Mexico began importing intermediate and capital goods from China, instead of just importing massive amounts of goods for consumption. This is relevant because it indicates that China started to export products with more value added, inserting itself in the Mexican manufacturing production, and by extension, into the United States market.

Figure 2: Mexican imports coming from China by type of good



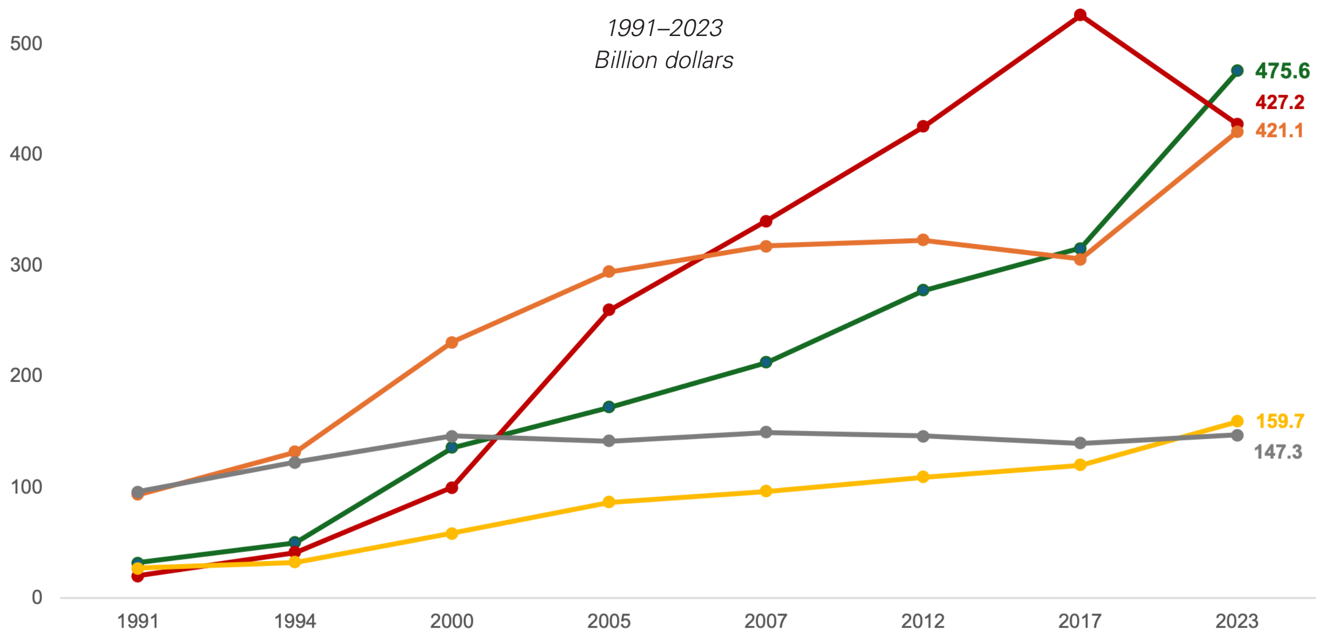
Source: World Bank, 2024.

China's role in the North American integration project

China's presence in North America grew rapidly and was by no means an accident, nor did it happen unnoticed. Rather, its presence grew, particularly regarding imports, as the trade policies in both the US and Mexico favored the articulation of North American supply chains with Chinese inputs, establishing relatively low tariffs and benefiting from China's accession to the WTO.

The origins of this trend go back to when Mexico, who was a relatively minor trading partner for the United States, negotiated NAFTA in 1994. Due to the removal of tariffs that this agreement provided, Mexico became one of the top three largest suppliers of the United States, displacing countries such as Japan and Germany, only behind Canada, as shown in Figure 3.

Figure 3: Top five US Suppliers



Source: Statista & World Integrated Trade Solutions, 2024

The objective of NAFTA was to create regional supply chains that galvanized the region's competitive advantages and promoted investments in North America[8]. For Mexico, it also meant the possibility to deepen its economic dependency with the United States, breaking the volatility that the country experienced during the 1980s.

However, China quickly surpassed Mexico and Canada in the United States import market, despite not having any free trade agreement and the logistical and geographical costs associated. This scenario caused strong reactions and, at least for the past ten years, it became a focal point in the development of US trade policy.

What are Mexico and the US doing with China?

Arguably, the defining issue of the first half of the 21st century centered on how China and the United States would conduct their relationship, which has swung from friendliness to open hostility in the past three decades. The United States efforts to contain China's rise started with the George W. Bush administration, which criticized the attempt of President Clinton to seek a partnership with China, instead of openly competing against it[9].

Similarly, President Barack Obama repeatedly stated that the Transpacific Partnership (TPP) negotiations were Washington's strategy for guaranteeing that the trade rulebook would be written by the United States and its partners, and not by China[10]. In this sense, President Donald Trump, largely considered responsible for instigating a trade war with China, was merely articulating positions that his predecessor had already announced.

Arguably, Mexico perceives China as a less threatening power than Washington does. A recent analysis compared how citizens view China and the United States in 24 countries, and it found that Mexico holds favorable views of both the US (63%) and China (57%)[11]. Despite the deep economic ties and bilateral trade of the US-Mexico relationship, when asked which country they considered the world's leading economic power, 40% of Mexicans answered the United States, while 33% said China. Interestingly, Mexico perceives that Chinese technology is superior to US technology - 53% of Mexicans consider that US technology is above average, but 68% consider Chinese technology to be more advanced.

The data seems to back these claims: the Mexican and Chinese governments have enjoyed an increase flow of trade without investing any political or diplomatic capital. The structure of the economic and trade relationship between China and Mexico has by and large been articulated by the business community and not necessarily by the governments. The business community took advantage of a political environment that allowed for those exchanges to occur uninterrupted, ensuring that China could maintain its position as Mexico's second largest source of imports since 2002[12].

However, the increases in trade flows were not accompanied with an increase of Chinese FDI in Mexico. According to the Ministry of the Economy, Chinese FDI in Mexico represented less than 0.5% of the total amount of foreign direct investment received by the country between 1994—2023. As the United States changed its views towards China, from embracement to open rivalry, the policy measures that Washington took to "contain" China became more aggressive, substantially increasing tariffs, imposing restrictions on Chinese companies' access to US technology, screening Chinese FDI, ultimately culminating in the renegotiation of NAFTA.

As discussed above, a permanent point of discussion during the USMCA discussions was how to "close" the indirect access that China had to the North American market, through low Most Favored Nation (MFN) tariffs applied by both the US and Mexico, if not by outright illegal practices[13]. Thus, the USMCA's objectives were twofold: promote a higher degree of regional content in industries such as the automotive sector and incorporate stricter rules and disciplines in areas such as labor, environment and SOEs, to better control companies operating in North America and simultaneously combat Chinese companies' misconduct[14].

Moreover, the United States and Mexico increased tariffs on Chinese goods, although Washington used domestic legislation (Section 301[15]) to specifically target Beijing, while Mexico increased its Most Favored Nation (MFN) tariffs twice[16], covering Chinese goods, but also affecting goods from third countries such as Brazil, South Korea or Turkey. Mexico, the United States, and Canada have pledged to consider more policy options to address concerns about China. Although it does not reference China directly, trade authorities at the Fourth USMCA Free Trade Commission Meeting,

> "… *agreed to jointly expand their collaboration on issues related to non-market policies and practices of other countries, which undermine the Agreement and harm US, Canadian, and Mexican workers, including in the automotive and other sectors."*[17].

It remains to be seen what such collaboration may entail, and how far the USMCA countries are willing to coordinate its policies towards China, but the fact that their commitment is reflected in an official trilateral document is undoubtedly relevant. The 2026 review can provide a window of opportunity for any decisions or actions that countries wish to implement in this regard.

On FDI screening, the US has more tools available than Mexico. Mexico's Ministry of the Economy is tasked by the Foreign Investment Law to keep a registry of foreign companies starting operations in the country, but it does not have any mandate to assess national security risks or similar concerns, as does the Committee on Foreign Investment in the United States (CFIUS). Yet, in December 2023, US Treasury Secretary Janet Yellen visited Mexico to meet with Mexico's Secretary of Public Finance (SHCP), Rogelio Ramirez de la O, and both *"signed a Memorandum of Intent (MOI) to affirm the importance of foreign investment screening in protecting national security and express their desire to establish a bilateral working group for regular exchanges of information about how investment screening can best protect national security".* Bilateral efforts to construct more robust cooperation on investment screening is key, though it will need to be deepened in the near future, even if these efforts are carried out by only a handful of specialized agencies.

In the US, Congress has created specific committees to monitor the country's policies towards China, and they have designed complementary measures. The Select Committee on the Strategic Competition between the United States and the Chinese Communist Party (CCP) of the US Congress is bipartisan body aimed at developing a plan of action to address potential CCP threats to the US. It issued a comprehensive report in December 2023[18] suggesting a strategy for economic and technological competition with China, which consists of several policy recommendations.

Some of the outstanding findings and recommendations include (i) China's economic system is incompatible with WTO rules and the United States should remove the Permanent Normal Trade Relations (PNTR) status granted to it; (ii) the US should renew the former China-specific Safeguard Mechanism; (iii) promote research and development in emerging technologies in sectors such as commercial space ventures, autonomous vehicles, and hydrogen technologies, among others.

Mexico, on the other hand, has not established similar committees on these issues. In both the Chamber of Deputies and in the Senate, there are commissions that study and assess general issues that could be important to Mexico's relationship with China, but there are no specific committees solely focused on evaluating policies *against*

China. Several members of Mexico's private sector are openly against any rapprochement towards Beijing[19], given that this has led to a lost opportunity to access China's domestic market[20].

This set of mixed messages sent by high-level Mexican officials makes it difficult to understand Mexico's position towards China. The Secretary of the Economy[21] and the Secretary of Hacienda[22] have taken policy decisions that suggest a disapproval of certain business practices by Chinese companies. However, these policies co-exist with open invitations to Chinese companies to invest in the country and with courtesy calls with Chinese officials. President Lopez Obrador met with Chinese officials[23] and president-elect Sheinbaum met with the Chinese ambassador to Mexico almost immediately after her electoral victory, who presented her with a letter from President Xi Jinping[24].

In conclusion, the United States has established a confrontational relationship with China—at times openly and sometimes with more nuances, but nonetheless confrontational. Washington's stance towards China has influenced the proceedings and activities of a myriad of stakeholders[25], and it is unlikely that such environment will see significant changes in years to come.

Mexico has not developed a clear position vis-à-vis Beijing, in either sense (friendly or confrontational), but has so far maintained the *status-quo* to protect its interests, and how shown little interest in modifying its bilateral relationship with China. A few Mexican policy decisions—increases in tariffs and restrictions on the exploitation of certain critical materials—are fully aligned with what Washington is already implementing, but a significant reframing of the relationship has yet to occur.

Rather, the debate in Mexico is focused on how to reap the benefits from maintaining a close relationship with China without antagonizing its top trading partner, the United States[26], a strategy that is reflected in the mixed signals previously mentioned. Nevertheless, the discussions in Mexico regarding China are consistently influenced by the political climate in the United States. It is undeniable that the US' perspectives on Mexico, China, and Mexico's stance (or lack thereof) towards China may intensify as the US election approaches.

The US electoral processes and its relevance the development of a China policy

The 2024 US presidential elections will serve as a referendum on America's role in the world, including its foreign policy towards Russia, Israel, Palestine, and China. In fact, America's policy towards China is poised to take center stage during the electoral cycle[27]. The complex relationship between the two world powers, characterized by economic interdependence and strategic competition, has become a focal point for debate among candidates and voters alike, with more US citizens considering China as the US' most important enemy[28].

The presidential candidates are under pressure to articulate clear and decisive policies towards Beijing. Both Joe Biden and Donald Trump seem to compete on who can propose the most radical policies towards China. While it is unlikely that the results of the November elections will significantly change Washington's position towards China, the winning candidate will set the tone for the future of the US-China bilateral relationship.

The question of how to address US competition with China has become deeply intertwined with domestic concerns such as job creation, national security, trade, and investment. Therefore, it is not unrealistic to imagine that US policies towards China will naturally affect Mexico, as it plays an important role in the region. Given Mexico's substantial economic dependence on the United States, particularly on exports, such a stance could emerge as a prominent feature of campaign rhetoric. Both US presidential candidates will promise to safeguard US economic interests and preserve US hegemony in the Western Hemisphere by constraining Mexico's ties with China, an issue that may resonate with certain voters.

There is ample evidence of how this rhetoric could present itself: from Trump stating that he would tax Chinese cars exported from Mexico[29] (although there are currently no Chinese automakers producing cars in Mexico) to USTR Ambassador Tai suggesting that China will be a fundamental issue in the 2026 USMCA review process[30].

The intricate web of trade relationships between Mexico and the United States makes the issue more complex. Aside from Mexico being the largest US trading partner, Washington could consider other measures to compel Mexico to get tougher on China by pressuring its southern neighbor on areas like migration, cross-border management, and security.

Any disruption to Mexico's economic stability could influence Mexico's geopolitical positioning, but this strategy could easily backfire because if the US decides to exploit Mexico's vulnerability to compel the country to modify its relationship with China, it might trigger nationalistic responses from Mexico, especially with a newly-elected government, whose ideological leaning and political discourse emphasizes a closer relation with non-traditional geopolitical partners[31].

The alternative for the US would be to engage in a more cooperative and constructive manner, considering that China is trying to actively upgrade its relationship with Mexico, and it has insisted on the tangible benefits that it could offer Mexico, with its Belt and Road Initiative (BRI) and other economic strategies[32]. Washington cannot realistically expect Mexico to simply reject these potential benefits and reject any engagement with China. Instead, the US should aim to provide competitive alternatives and engage in collaborative projects that highlight the advantages of partnering with American businesses and technologies under the USMCA framework.

The US should consider incorporating Mexico as a key partner in future industrial policies developed by the new US administration. By integrating Mexico into its broader economic and industrial strategies, the US can create a more robust and resilient North American economy. This integration can include joint ventures in high-tech industries, green energy initiatives, and advanced manufacturing.

By aligning industrial policies, the US and Mexico can enhance their economic interdependence and competitiveness on a global scale. Additionally, Washington should actively seek Mexico's participation in the Indo-Pacific Economic Framework (IPEF) and urge it to take a leadership role in the Americas Partnership for Economic Prosperity (APEP) to further integrate Mexico into Washington's key economic and trade priorities. The 2026 USMCA review could serve as an ideal launching platform to achieve these objectives.

The 2026 USMCA review and other potential unilateral measures

The USMCA features a unique clause that initiates a review process every six years following its implementation. However, the USMCA does not provide specifics on how this review should be conducted. Article 34.7, Paragraph 2 of the USMCA specifies that on the sixth anniversary of the Agreement's entry into force, the Commission will undertake a "joint review," considering any "recommendations for action" submitted by any Party. These recommendations need to be presented to the Commission at least one month before the review.

There are no guidelines outlining the steps involved in the review process, or how the three countries should agree on the review rules, or who the participants should be. Similarly, there is no direction for the Commission on which recommendations to accept and which to reject, other than the lines included in the 2024 Fourth Meeting of the Free Trade Commission.

As the first USMCA review approaches, it is expected that the China question will become more pressing, and as certain actors have already shown, the United States will surely use the USMCA review as an opportunity to include some elements to tighten North American policies toward China.

Based on the above, it is worth discussing what other potential policies Washington could incorporate into the USMCA review to bind its USMCA partners to Washington's views on China. First, it is important to remember that the USMCA already includes provisions geared to counter Chinese presence in North America, although the agreement never mentions the country by name. Rather, article 32.10 refers to what USMCA countries could do if they attempt to establish free trade negotiations with a "non-market country", a phrase clearly aimed at China.

> *"[…]*
>
> *2. At least 3 months prior to commencing negotiations, a Party shall inform the other Parties of its intention to commence free trade agreement negotiations with a non-market country.*
>
> *3. Upon request of another Party, a Party intending to commence free trade negotiations with a non-market country shall provide as much information as possible regarding the objectives for those negotiations.*
>
> *4. As early as possible, and no later than 30 days before the date of signature, a Party intending to sign a free trade agreement with a non-market country shall provide the other Parties with an opportunity to review the full text of the agreement, including any annexes and side instruments, in order for the Parties to be able to review the agreement and assess its potential impact on this Agreement. If the Party involved requests that the text be treated as confidential, the other Parties shall maintain the confidentiality of the text.*
>
> *5. Entry by a Party into a free trade agreement with a non-market country will allow the other Parties to terminate this Agreement on six months' notice and replace this Agreement with an agreement as between them (bilateral agreement).*
>
> *[…][33]"*

This language has never been tested, given that no USMCA country has launched negotiations with a non-market country, but it is worth remembering that China applied for membership in the Comprehensive and Progressive Transpacific Partnership (CPTPP), the agreement enforced by the TPP after the United States withdrew in 2017, and to which Mexico and Canada are signatories.

Therefore, it is not difficult to imagine that the United States would propose to expand the spirit of Article 32.10 to other latitudes. For example, it could be suggested that in order to enter the US market duty-free, in addition to meeting the applicable rules of origin and fulfil all other related requirements, it would be necessary to demonstrate that the company that manufactured such goods does not originate from a "non-market country".

It may not be necessary for the United States to craft entirely new dispositions for the USMCA—it may suffice with insisting on incorporating a separate track to enforce current obligations, with stricter standards to non-market countries' companies operating in North America. For example, the United States could demand that, for those dispositions applicable to labor, the environment, and state-owned enterprises, the enforcement and consequences will be steeper if the company that allegedly breached the obligations is Chinese.

It is less clear if Mexico and Canada will align with these demands. Canadian and Mexican business communities are asking their governments to adopt measures similar to those adopted by Washington in recent years, but the realities and political contexts of Ottawa and Mexico City are vastly different[34]. Should Mexico and Canada show reluctance in bandwagoning entirely with Washington's crusade against China, the United States could try to implement unilateral actions, derived either from Congress or from the White House to force its hand.

Conclusions: the need to strike a balance

There is no doubt that North America fully recognizes the challenge that a rising China represents, both in military terms but also on economic prowess, investment capabilities, and its ability to rapidly make technological advances. However, such challenge is perceived differently in Washington than in Mexico City. For the United States, China represents the only credible alternative to the US-led international order, threatening its hegemonic position in the world. For Mexico, however, China is an important partner that cannot be ignored.

The US' concerns on China are not new, but the escalation of the rhetoric coincides with the 2016 electoral campaign of Donald Trump, as the criticisms against the open-trade policy that the US pursued towards China accumulated. The Biden administration did not roll back the trade and investment measures implemented by former president Trump—in fact, some were strengthened and deepened. The shared bipartisan consensus that *something* must be done against China indicates that there is no possibility of a more amenable attitude towards Beijing.

Even if the next US administration wishes to radically change US policy towards China, it would need to convince key stakeholders—especially Congress—of the rationale behind such a move. Business organizations may be more open to the idea of a managed relationship with China, even if it implies restrictions and burdensome requirements (permanently filing exemptions under section 301, for example). However, even if the United States does find a way to balance the several angles of the China equation, it forcefully requires Mexico's support in complementing or even mirroring these actions.

Most countries in Latin America have developed and implemented a "China policy", with concrete objectives depending on their specific needs (investment, market access, soft loans, etc.), resulting in a stronger Chinese presence in these countries[35]. Mexico, on the other hand, has adopted a more pragmatic approach to China, benefiting from the incorporation of Chinese inputs and raw materials to its exports, thus enhancing the competitiveness of Mexican exports, and more recently, from the expectation of significant Chinese investments.

In that sense, China's influence in the Mexico—United States trade relationship should not come as a surprise. Between 2007 and 2022, China was the largest supplier of the United States, and it has been Mexico's second source of imports since 2002. It could be argued that Chinese insertion into North American supply chains happened by design, and it started to be questioned when the political views towards Beijing changed.

Even though Mexico's incoming government has yet to structure its policy on China, the United States, Canada, and others, it cannot be expected that the Sheinbaum administration will adhere entirely to Washington's views on this issue. Mexico's first female president, who will take office on October 1 of this year, will protect Mexico's interests and establish its own policy towards China.

Although Mexico, the United States, and Canada are trade partners, the political climate in each country may push each government to protect its own interests while simultaneously abiding by the USMCA regulatory and legal framework. If the next president of the United States tries to force its wishes on Mexico, under the premises that the country is too dependent on the US market, they risk a nationalistic response from Mexico, endangering the economic integration and perhaps jeopardizing collaboration in other vital areas for Washington, such as migration.

The most advisable approach would be for Mexico and the United States (and Canada, from a trilateral perspective) would be to establish clear limits to their respective Chinese policies. Mexico must recognize and implicitly incorporate its views, while understanding that the United States is its largest trading partner and prime source of foreign direct investment, and thus, coordination is paramount. For its part, the United States cannot expect Mexico to turn down potential benefits if it does not offer a similar package of incentives. The 2026 USMCA review could serve as a unique opportunity and platform to discuss and develop mutually beneficial policies.

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