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Introduction

Prior work for the US-Mexico Foundation detailed the tremendous mutual benefits to the US and our allies, including Mexico, of "ally-shoring" critical supply chains, and co-producing a variety of products and services, particularly in high-value emerging sectors. Now, current economic disruptors suggest further mutual benefits from meeting critical US workforce and skill needs through ally-shoring of labor.

For a combination of reasons, US employers are facing post-pandemic workforce shortages in key occupations that are likely to persist over time. Conversely, Mexico and other US trading allies have complementary latent skill and workforce capacities. The tight integration of the North American co-production system (given USMCA content requirements, proximity, and other factors) suggests mutual economic, employment, and even political and security benefits can be achieved through ally-shoring labor supply, along with other critical supply and production enablers. Outstanding benefits include reduced US inflation rates propelled by supply chain disruptions and critical worker shortages, increased regional competitiveness, higher supply chain resilience, and the potential to reduce the carbon footprint by supporting industries closer to home. An ally-shoring framework offers the opportunity to think strategically about current and future workforce requirements- and their link to economic security with our key allies in North America, and Mexico in particular, as a highly interconnected co-production partner.
Prior to the global pandemic, the US, relative to allies like Mexico, already faced an aging workforce with lower numbers of new entrants. The US workforce in several critical industrial sectors has been growing older over the past decade, with retirements outstripping new entrants. For example, nearly one-quarter of the US manufacturing workforce is over 55 years of age. The average age of a long-haul truck driver is 55. The average age of millwrights who install and set up machinery and other heavy equipment in manufacturing is 51. Additionally, other occupations also faced looming labor shortages and fewer young entrants, including auto assembly worker (average age 45), aerospace technician (45), and electrician (41).

Today, demand for workers is outstripping supply in the US, a dynamic which is likely to persist for some time. Early this year, the US Chamber of Commerce estimated there were 4.6 million more open jobs in the US than job seekers. The Economist reports the US is down 3 million workers from before the pandemic, marking a 2% contraction in the labor force. The ratio of job vacancies to unemployed is near a record high. The US labor force participation rate – those between the ages of 15 and 64 looking for work, has dropped over a full percentage point during the pandemic years of 2020 to April 2022.

This accelerated shrinking of the US working-age labor supply cohort reduces productivity and directly undercuts long-term prospects for economic growth, new jobs, and businesses across the whole economy.

The current mismatch between labor demand and supply derives from a number of causes, chief among them, the pandemic, which has radically restructured and reallocated the labor supply in the US. Many US workers, cushioned by an expansion of unemployment benefits and the Paycheck Protection Program, which allowed employers to retain workers, were able to stay home, contributing to greater stress and departures of colleagues who did work. As of March 2022, according to the Centers for Disease Control and Prevention, more than 100 million working-age Americans – people between the ages of 18 and 65, contracted the virus, many missing work and further stressing
employers and other employees. Higher COVID-19 infection rates also meant more workers were absent from their jobs than in other countries. For example, per capita case rates in the US are more than double Canada’s, which has a similar unemployment insurance scheme. Over 230,000 Americans of this working-age cohort died from the virus, a not insignificant contribution to the shrinking working-age workforce.

During the pandemic, many workers aged 65 and older exited the workforce for good. And while prime-age workers 25-64 are coming back to work on pace to reach pre-pandemic levels, the US has lost, likely permanently, 2 million workers aged 55 and over. According to economist Brad Hershbein of the W. E. Upjohn Institute of Employment Research, “We’re still a few million people short of where we should be because of lingering health issues (long COVID-19), childcare issues (some schools closed, others quarantined kids), and burnout issues (rude customers/clients and unsupportive bosses).”

Workers’ priorities and needs have also changed. Now, many US workers are leaving their jobs and looking for higher paying jobs, access to at least a partial remote-working environment, and in less dangerous occupations than front-line service or assembly line-production jobs. As employers have been forced to change the tasks demanded of workers (e.g., curbside pickup vs in-store/restaurant service), workers have proven reluctant to adjust to significantly changing demands and responsibilities.

These forces and factors, in combination, mean that the US has faced record-breaking job quits (3% of the whole labor force in November 2021 alone—the highest rate on record). This phenomenon is in dramatic contrast to the involuntary quits that characterized prior recessions. Also, since workers are better able to come back from voluntary vs involuntary quits, the US is seeing a significant amount of job switching, leading to “relocation shocks” in the employment market. This is especially true in sectors like manufacturing which has seen the biggest surge in worker quits, a nearly 60% jump compared to pre-pandemic levels. Additionally, worker reallocations leave understaffed facilities and higher training burdens — accelerating worker quits as workers remaining on the job are being asked to work more, for longer hours, and are experiencing significant stress.

Workers believe that with high demand for labor, they can pursue other opportunities. But those seeking different jobs often don’t have the right skills for available jobs. Therefore, labor exchange is currently very inefficient in marrying
appropriately skilled workers with available jobs.

The business sectors most affected by this mismatch of labor supply and demand, according to the US Chamber of Commerce and the Upjohn Institute, include: accommodation and food service; durable and non-durable goods manufacturing; wholesale and retail trade; professional, business, and information services; and education, health, and other social services. These sectors have job opening rates above the nationwide average of 6.8%, with many more unfilled job openings than unemployed workers with the required experience or skills. For example, even if every unemployed person with experience in the durable goods manufacturing industry were employed, the industry would only fill 65% of the vacant jobs. Sectors such as transportation and warehousing and non-durable goods manufacturing are also experiencing vacancies of over 8% among the highest business sectors.

Furthermore, as detailed in a recent Washington Post editorial by economics reporter Heather Long, the mismatch between supply and demand is exacerbated by the fact that sectors like manufacturing aren’t necessarily the best-paying jobs around anymore. In past decades, manufacturing pay for non-supervisory workers was traditionally higher than in other industries. Now, manufacturing pay is below average. Pay raises have been less robust in “nondurable” manufacturing, such as food-preparation facilities and meatpacking. The pay is low, conditions are harsh, and severe COVID-19 outbreaks which sapped employee morale. As employers in other sectors like logistics, retail, and hospitality agree to worker pay increases, nondurable manufacturing jobs look less attractive. The average pay for rank-and-file warehouse and transportation workers is now over $25 an hour vs $22.62 for nondurable manufacturing workers.

In addition, as many industries who relied on international supply chains (manufacturing, construction, retail, and wholesale trade) seek to diversify supply chains to avoid future disruption, there are obstacles to the reallocation of labor to meet these needs. These are sometimes in the form of regulations and contracting constraints (e.g., licensing and training of workers in different states and countries).

Finally, former President Trump’s policies and pandemic-induced restrictions on the movement of people served to shut the door to new immigrants to the US—potentially the fastest means to meet employer labor skill demands. However, the Biden Administration has been slow to roll back these changes. In the US,
it is estimated that the US has **about 2 million fewer working-age immigrants** than we would have seen if pre-COVID-19 rates had continued.

Rising **labor costs, worker shortages in key occupations, supply and component bottlenecks, increasing transportation costs, and the labor supply mismatch** are helping to fuel inflation in both the US and Mexico — and domestic inflation remains the most pressing economic issue facing the Biden Administration.

**Mexico: Uneven Recovery with Looming Demographic Challenges**

The dramatic labor market reallocation experienced in the US has no equivalent in Mexico. The recovery of the Mexican labor market since the COVID-19-induced recession of 2020 has been mixed and, when compared to the US, reflects a different set of labor and recovery dynamics. With fewer social and economic public transfers to support affected Mexican workers, sitting out the pandemic was not an option for most. Mexico’s overall labor participation rates have rebounded since the onset of the pandemic; however, the recovery has been uneven across sectors, workers, genders, age groups, and geographies.¹

Workers in export-driven markets, such as automotive, transportation, and communications, and manufacturing-intensive northern states, have seen stronger recovery with post-pandemic reemployment consistent with pre-pandemic levels.² Meanwhile, in hard-hit industries such as travel and tourism, agriculture, construction, and services, employment levels are still below pre-pandemic levels.³ About 1 million jobs were lost in the formal labor market during the pandemic, and about half of those losses were from the professional and personal services sector.

Generally, Mexicans are going back to work if they can, but some are working less or fewer hours.⁴ Insufficiency of work in some industries has driven more workers to join the informal labor market to make up for wage shortfalls. **Other workers have simply dropped out, especially women.**

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1. Interview with Ana Gutierrez, Coordinadora de Mercado Laboral y Comercio Exterior, IMCO, conducted by Elaine Dezenski on March 22, 2022, see also: https://www.worldbank.org/en/events/2021/11/19/uneven-recovery-taking-the-pulse-latin-america-caribbean-following-pandemic
3. ENOE 4Q2021
4. Gutierrez Interview
Official data states that nearly 30% of workers are in the informal sector, with limited, if any, access to labor protections and social safety nets. However, the real rate of informality is even higher (56%), with the inclusion of workers that, despite being employed in the formal sector, are treated as informal—irregularly hired, not formally registered with social security organizations, and without access to their full labor rights.

Similar to the trends in the US, inflation is also affecting the Mexican labor market and its purchasing power. The annual inflation rate reached 7.45% in March 2022, up from 7.28% in February 2022—the highest figure since 2001. Approximately 60% of Mexican workers—34 million out of an economically active population of 57 million—individual workers are earning less than the equivalent of two minimum wages in Mexico, a salary not enough to buy the basic food basket.

In contrast to the US, where upward pressure on wages is occurring across the board, in Mexico, the excess supply of labor is pressuring wages downward. In response, the Mexican government announced in late 2021 a 22% increase in the daily minimum wage rate for 2022, on top of large increases in 2020 and 2021. However, some key labor market dynamics have hindered the impact of this policy, including the persistently high percentage of workers in the informal economy.

Finally, some demographic trends will also have a growing impact on labor market outcomes in Mexico over the next decade. Particularly, the Mexican economy faces a looming economic challenge as an estimated 2 million young workers per year are set to enter the workforce over the next five years. This may lead to growing rates of unemployment, underemployment, and continued downward pressure on Mexican wages. However, this emerging demographic cohort of workers presents an opportunity to develop a broader pipeline of skilled labor to serve both the US and Mexico.

5. Gutierrez Interview
6. Gutierrez Interview
The Case for Ally-Shoring

The Case for Ally-Shoring Workforce with Mexico

The key labor market trends and drivers identified across the US and Mexican labor markets suggest very different but complementary labor market dynamics between the two countries. On one hand, the US is experiencing a stubborn and constrained labor supply and strong labor demand. Structural shifts in the labor market and changes in worker occupational preferences, combined with supply chain bottlenecks are leading to rising pressure on wages and helping super-charge inflation. Mexico, on the other hand, faces growing downward pressure on wages and a looming youth demographic bulge entering a labor market already thin with work opportunities. In other words, the two countries face opposing labor dynamics that could be addressed by a single solution.

Ally-shoring is rooted in the idea of strengthening the critical manufacturing and services production base in both countries for greater economic security and supply chain resilience. So, could a workforce ally-shoring approach help to optimize, better harmonize, and create more resilient labor markets across borders?

Areas of Opportunity to Enable Workforce Ally-Shoring

Building a better-functioning, highly mobile “bi-lateral” workforce between the US and Mexico could enable greater supply chain resilience and efficiency by allowing a smoother, demand-driven flow of skilled and semi-skilled workers where they are needed most. As the US reconsiders supply chain resilience and economic security in the wake of pandemic shocks and emerging geopolitical realities, it is fundamental to not only consider pivoting manufacturing closer to home but also protect industries that are losing out on the US competition for labor. Mexico has strong technicians (particularly in Northern Mexico with its concentration of manufacturing), along with skilled agricultural and professional service workers. Nevertheless, there are key areas of opportunity that need to be addressed. This report will highlight five of the most pressing issues.
First, North America needs to increase co-production and sourcing in key sectors to grow a larger economic and employment base together. The last attempt to develop a US-Mexico labor mobility model in the early 2000s ended with the tragic events of 9/11. Since then, the paramount focus on security and border control has blunted any efforts to address the fundamental issue of labor movement across the US-Mexico border. However, the calculus may be changing. While the border must be secure from criminals, terrorists, illegal immigration, and other threats, global shocks such as the pandemic and geopolitical threats posed by China challenge how we define secure borders and North American economic security. North American solutions to securing supply chains are preferable to relying on far-flung production that may be at risk when faced with global shocks. North American workers are at the heart of ensuring North America’s supply chains remain secure. Immigration policy must be balanced against the need for resilient supply chains, especially in critical industries.

Under a framework of building critical supply chain resilience for the long-term, the US and Mexico could proactively co-identify one or two key critical industrial sectors— for example, food processing and agriculture; pharmaceuticals and PPE manufacturing; or advanced manufacturing to support electronics, semi-conductors, and transportation— where improving workforce availability and capacity on both sides of the border would benefit from targeted labor mobility. Step by step, an ally-shoring-driven approach to labor mobility would help shift the immigration discussion from reactive and fear-driven to one that recognizes that our shared borders offer unique opportunities for enhancing skills, greater job opportunities, and ability to leverage skillsets.

Second, the US and Mexico can facilitate a targeted upskilling of the workforce. Mexican workers could be trained and skilled to fill occupational niches in the US labor market which haven’t been filled by US workers. Additionally, investment can be made to upskilling Mexicans to accommodate new supply chains in emerging industry sectors and those that are relocating to Mexico to improve resilience and reduce the risk of vulnerability to geopolitical shocks coming from China. Regionally, the US, Mexico, and Canada can look toward common standards, certifications, and training in many areas that would provide mutual benefits and a stronger industrial base. The initial work undertaken to create a common certification framework for certain manufacturing skills, as envisioned by the North American Strategic Competitiveness Organization (NASCO), offers a starting point for the kind of bilateral vision, public-private engagement, and common standards-setting efforts that can help effectuate targeted worker
mobility, upskilling, and more opportunity.\(^7\)

Third, more targeted US Foreign Direct Investment (FDI) in Mexico can broaden the production base and expand the pool of skilled workers in key segments, helping to grow the regional economy. To train and tailor the labor market to global needs, Mexico needs more FDI. FDI within an ally-shoring framework necessitates a corresponding workforce strategy to ensure the skills and capacities are available to support emerging American supply chain opportunities over time. Making a strong and lasting link between FDI and labor market requirements can ensure that both Mexico and the US reap greater benefits from US government-backed equity investments that support the pivot of critical supply chains. The US could help by allocating some of its investments through the US Development Finance Corporation (DFC) towards infrastructure and smart, secure border facilitation in Mexico. Seed funds could be used to match and incentivize more private sector funding tied into complementary investment in worker training and skills building to support critical industries.

Fourth, the region must shift the US–Mexican workforce policy from a defensive one (solely protecting domestic workers) to an affirmative one. The workforce flow between US and Mexico has been disrupted by limits on visas and a failure to update worker programs that keep up with growing labor demands. Looking forward, reactive workforce policies aimed solely at deterring cross-border movement will reinforce immigration pressures on the US southern border by contributing to a growing unemployed and underemployed labor force in Mexico. Both countries can benefit from a labor policy that meets the workforce needs of US employers and expands Mexican businesses and employment opportunities. This helps firms on both sides of the border to remain competitive by providing more good jobs for both US and Mexican workers.

Fifth, and last, ally-shoring can score three political goals with a single policy—reducing US inflation, building supply chain resilience, and effectively addressing the immigration political “emergency.” Including labor supply in ally-shoring does more than make the workforce “supply” chain more reliable. Encouraging the sorely needed changes to immigration and migration policy that can quickly meet US employer workforce needs also serves to both curb inflation and reduce migration pressures on the border.

Recommendations for Actions and Public Policies

Ally-shoring addresses pressing social, demographic, and economic pressures within North America, while simultaneously reaping huge benefits for US national security, US global foreign policy, and regional stability. Ally-shoring brings vulnerable supply chains and critical factories away from autocratic regimes and non-democratic countries to allies, close to home, reducing carbon costs and boosting commercial transparency. To achieve these goals, tangible actions and public policy proposals are needed. For instance, the US should:

1. Create a US-Mexico-Canada CEO Dialogue. A public-private sector proposal exchange mechanism, to identify – among other things – critical supply chains and transformational sectors that can be “ally-shored” or “friend-shored.” This mechanism could similarly be used to support expanded co-production with tighter, less costly, more resilient supply chains, enhancing employment opportunities across the region.

2. Identify the most acute US occupation skill needs and enact emergency changes to immigration/visa policies to address shortfalls in key sectors and occupations. This would help protect the health of key stressed US employment sectors like hospitality, health care, and trucking. This will also address the dramatic loss of manufacturing workers in the US while tapping into the pipeline of emerging young workers in Mexico.

3. Enhance public and business-led training programs. Mexican workers should get the skills needed to work in occupations where there is US employer demand and critical occupational shortages and in skills that would help companies relocate operations from China.

4. Address the acute gap in skilled agricultural workers with an enhanced guest worker program. Our highly integrated agricultural co-production system is most productive and efficient when skilled agricultural workers are able to move to work on both sides of the border – movement now stymied. Absent a more robust agricultural worker program including more permanent visa status for workers, as contemplated in H.R. 1603, labor will remain scarce on both sides of the border.
5. **Point-based immigration method.** Canada has innovated a point-based immigration methodology, called the Comprehensive Ranking System which provides opportunities for skilled workers based on scores they can achieve by having valuable education levels, work history, and skills. The US should assess the viability of a similar approach to address American inflation, supply chain, and immigration pressures.

6. **Harmonize business and professional certifications.** A recommendation of the US Mexico Foundation’s 2021 report on Advancing Labor Mobility, harmonization in areas of US shortage and Mexican surplus (e.g., accounting) can enhance the US–Mexico workforce particularly in areas that afford virtual work. The North American Strategic Competitiveness Organization’s (NASCO) trilateral certification pilot serves as an interesting model for industry-driven cross-border skills development in North American manufacturing.

7. **Coordinate US Development Finance Corporation (DFC) investments in Mexico to support a stronger workforce.** DFC investments can be linked more fully to enhanced workforce training, upskilling, and mobility in Mexico. Enhancing workforce skills also contribute to stronger national security. Higher incomes in Mexico and Central America mean better jobs, reduced pressure on the border, less incentives for organized crime, and more opportunities to move workers out of the informal sector and out of poverty. Key sectors for DFC and other FDI-sponsored workforce upskilling could include: (1) electronics, where Mexico has been trying to improve its supply chain participation and reduce dependency on China; (2) tier 1 and 2 suppliers in the automotive industry; and (3) opportunities to develop new supply chains in transformative exports.

The long-range planning required to manage complex global supply chains efficiently, ensuring the availability of workforce, skills, and mobility requires **long-term planning and partnerships.** The mismatched and disjointed labor markets between the US and Mexico are a critical obstacle to the region’s growth, particularly for the US. With an aging population, increased labor shortages in multiple industries, supply-chain bottlenecks, and an unstable dependency on long-distance and non-democratic trading partners, the US economy faces increased inflation, supply chain vulnerability, and immigration pressures in the southern border.
Mexico’s complementary workforce force dynamics present a unique opportunity to build a cross-border win-win, investing in the region’s well-being and prosperity. And in an economy in which, as Brookings colleague Joseph Parilla points out, so much of the bilateral trade is actually in intermediate goods—or components of a co-produced finished product, removing obstacles to greater production including occupational skill shortages helps to expand businesses on both sides of the border. Working to harmonize the US-Mexico labor market can strengthen both countries’ economies, enhance US border security, help extinguish the inflation fires, and counter the economic power of autocratic governments abroad, making America stronger, safer, more stable, and more secure.
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