

Enforcement, Displacement, and Informality: Labor Market Adjustment under the USMCA's Rapid Response Mechanism

Research Question

Does strict enforcement of labor provisions in trade agreements encourage a transition to the formal sector or drive workers into the informal economy?

Introduction & Theory

The first-of-its-kind **Rapid Response Labor Mechanism (RRM)** in the **United States-Mexico-Canada** agreement (USMCA) represents a model for future trade agreements by providing a facility-specific enforcement process for labor disputes.

- Despite its potential, the empirical impacts of this mechanism are still unknown. There remain concerns about the RRM's effects on workers' welfare and informal employment.
- Recent estimates place the global informal workforce at over **two billion individuals**.
 - Informal work is closely related to dangerous working conditions, inequality, and increased poverty.
 - In a study of 28 developing and emerging countries, the **poverty rate for informal workers** was found to be **5x higher** than that of formal workers in eight countries and **10x higher** than formal workers in three countries.
- The RRM is an excellent case to study the effect of labor provisions because the USMCA preserved NAFTA's tariff structure, removing the confounding effects between trade liberalization and labor regulation found in many agreements.

Hypotheses

H1a: Cities with RRM investigations will experience an *increase* in individuals reporting permanent or unionized employment contracts compared to cities that do not, or have not yet, had an investigation.

H1b: Cities with RRM investigations will experience a *decrease* in non-agricultural informal employment compared to cities that do not, or have not yet, had an investigation.

H2a: Cities with RRM investigations will experience a *decrease* in individuals reporting permanent or unionized employment contracts compared to cities that do not, or have not yet, had an investigation.

H2b: Cities with RRM investigations will experience an *increase* in non-agricultural informal employment compared to cities that do not, or have not yet, had an investigation.

Methodology

This study utilizes a **time-series cross-sectional sample of 38 Mexican cities** to isolate the localized effects of labor enforcement due to an RRM investigation.

- Treated cities are identified by matching GPS coordinates of investigated facilities to the nearest city in the sample within a 50-kilometer commuting distance.
- The temporal range of the data spans from the first quarter of 2015 to the third quarter of 2025.

Cities with RRM investigations were matched with similar looking cities that had not had an RRM investigation on a variety of potentially confounding covariates. After matching, we estimated a **difference-in-differences (DiD)** analysis between treated cities and their matched controls.

The DiD model calculates the **Average Treatment Effect on the Treated (ATT)** by comparing changes in outcomes before and after an RRM investigation for both groups.

Results

Results show that RRM enforcement causes short-term worker displacement as firms shed formal labor to offset immediate or anticipated cost increases due to unionization efforts.

- At the city-quarter level, RRM investigations lead to an immediate **reduction in the number of individuals reporting permanent or unionized employment contracts by about 3%**.
- This displacement is followed by an increase in **non-agricultural informal employment** by just over **one percentage point** in the quarter following the onset of an RRM investigation.
- Moreover, outcomes that trend closely with informal employment also increase in the following quarter, such as an increase of almost **two percentage points** in respondents reporting a **lack of access to mandatory employer-registered healthcare (IMSS)**.

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Figure 1 illustrates the geographic distribution of RRM event sites across Mexico under the USMCA framework.

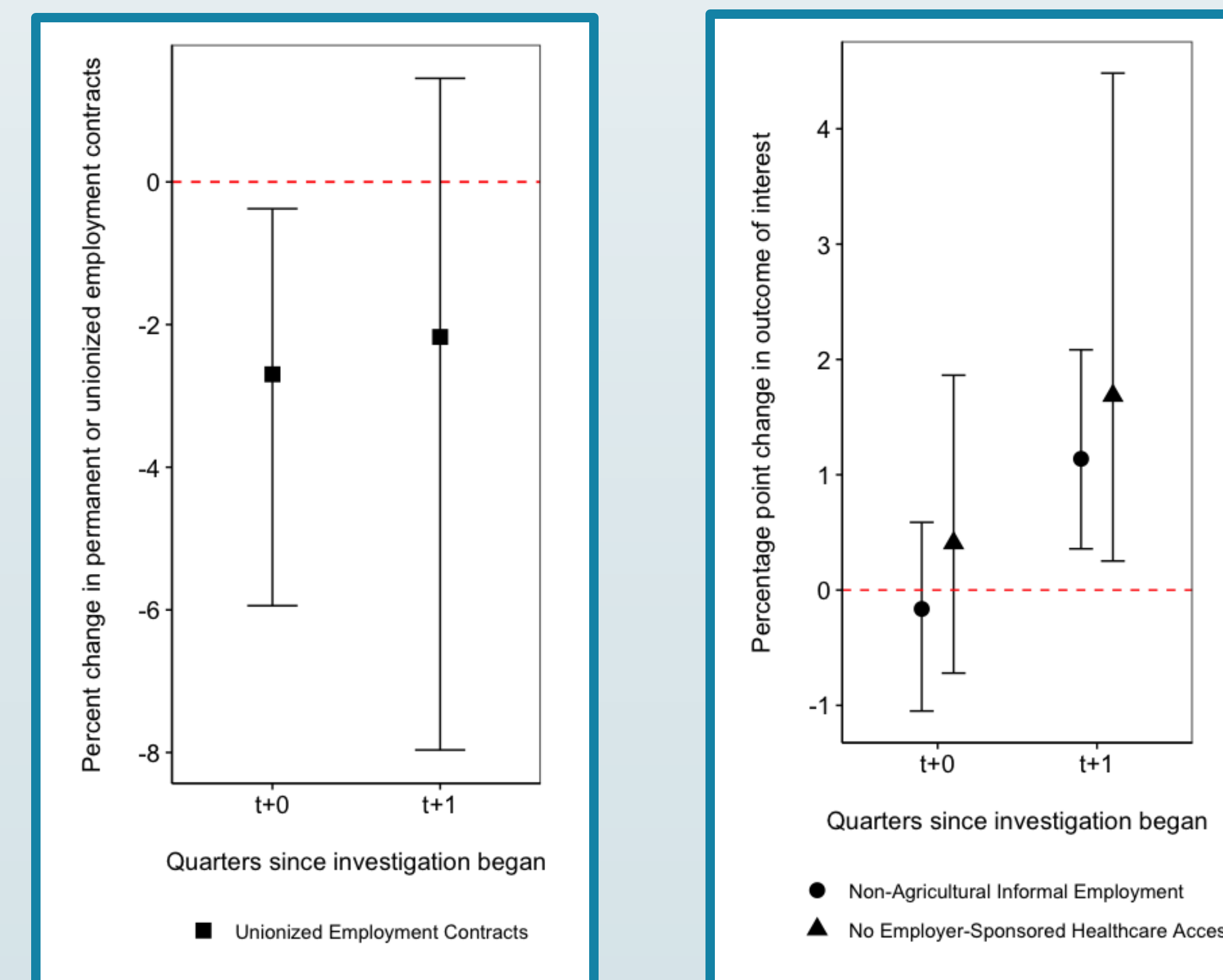


Figure 2 illustrates the short-term outcomes of RRM enforcement, showing declines in unionized contracts and IMSS access, alongside increases in informal work.

Figure 3 illustrates the short-term outcomes of RRM enforcement, showing declines in unionized contracts and IMSS access, alongside increases in informal work.

Conclusion

Approximately three quarters after the onset of an investigation, there is a **two-percentage point increase** in workers reporting additional, **non-mandated employment benefits**.

The RRM is an incredibly unique mechanism that serves as a potential template for future international trade agreements looking to protect collective bargaining rights.

Unlike previous slow-moving, superficial legislative labor provisions, the RRM allows for **rapid, firm-level enforcement** that forces immediate recourse.

However, future policy evaluations must extend beyond individual facility compliance to monitor **broader localized spillover effects** that allows firms to displace workers and into the informal economy.

References

