The Path to NAFTA 2.0

Gary Clyde Hufbauer
Reginald Jones Senior Fellow, PIIE

70th CSG West Annual Meeting
North America Summit VIII
Tacoma, Washington

August 16, 2017
NAFTA Timeline in the US Congress

• On May 18, 2017 US Trade Representative Lighthizer sent 90-day notice to Congress of intent to renegotiate NAFTA.

• On July 17, 2017 US negotiating objectives were published, 30 days before negotiations start.

• Around August 17, 2017 new talks will formally begin.

• If an agreement is reached, the president must notify Congress and wait 30 days before signing.

• Once the implementing legislation is delivered to Congress, the House and Senate have 90 legislative days for an up or down vote on the entire package (“fast track”).

• On July 1, 2018 “fast track” negotiating authority will expire but the Trump administration can request a 3-year extension which will be granted unless either the House or Senate disapproves.
Shift in US Trade Policy under Trump Administration

• For the first time since 1930, trade was high-profile in the US election—US trade policy now constrained by anti-globalization sentiment.

• Four priorities announced to ensure level playing field for US companies and workers:
  1. Defend US national sovereignty;
  2. Strictly enforce US trade laws;
  3. Use leverage to encourage other countries to open their markets to US exports, and enforce intellectual property rights;
  4. Negotiate new and better trade deals—first up, NAFTA.

• “Fairness,” as defined by the administration, is the overarching theme: (1) Bilateral trade balance; (2) Mirror image reciprocity.

• Preference for bilateral talks rather than regional/multilateral initiatives.

• Aggressive use of US unfair trade statutes and national security reviews to impose restrictions on imports like steel.
Since 1993, US-NAFTA trade increased by a factor of 3 to $1.2 trillion in 2016

billions of dollars

US Trade with Canada and Mexico

- Two-way US trade with Canada is practically balanced; US trade with Mexico shows a persistent bilateral trade deficit.
- If energy is excluded from the total trade balance, the US runs a large trade surplus with Canada.

<table>
<thead>
<tr>
<th>US trade in goods and services, 2016</th>
<th>Canada (US$ billion)</th>
<th>Mexico (US$ billion)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Exports of goods and services</td>
<td>322</td>
<td>262</td>
</tr>
<tr>
<td>Exports of energy</td>
<td>17</td>
<td>22</td>
</tr>
<tr>
<td>Imports of goods and services</td>
<td>314</td>
<td>324</td>
</tr>
<tr>
<td>Imports of energy</td>
<td>56</td>
<td>9</td>
</tr>
<tr>
<td>Trade balance on goods and services</td>
<td>8</td>
<td>-62</td>
</tr>
<tr>
<td>Trade balance on goods and services excluding energy</td>
<td>47</td>
<td>-75</td>
</tr>
<tr>
<td>Trade balance on goods</td>
<td>-17</td>
<td>-69</td>
</tr>
</tbody>
</table>

Note: Energy includes coal, crude oil, petroleum products, electric energy and other energy products.

Source: US Bureau of Economic Analysis and US Census Bureau
US Trade with Mexico and Canada, By Product, 2016

**US-Mexico Trade**

- **Services**: Imports from Mexico = -23.5, Exports to Mexico = 31.1
- **Manufactures**: Imports from Mexico = -246.6, Exports to Mexico = 173.9
- **Energy**: Imports from Mexico = -8.9, Exports to Mexico = 20.2
- **Agriculture**: Imports from Mexico = -25.9, Exports to Mexico = 19.7

**US-Canada Trade**

- **Services**: Imports from Canada = -29.6, Exports to Canada = 54.2
- **Manufactures**: Imports from Canada = -156.2, Exports to Canada = 199.2
- **Energy**: Imports from Canada = -58.1, Exports to Canada = 15.5
- **Agriculture**: Imports from Canada = -33.8, Exports to Canada = 26.8

*Source: World Bank’s WITS database.*
What Did NAFTA Achieve?

• Economic Payoff
  – Benefits flow **both** from larger exports and larger imports of goods and services. US two-way trade is some $635 billion larger on account of NAFTA.
  – A $1 billion increase in trade generates GDP gains of $200 million for countries like Canada and US; for Mexico it generates GDP gains of $500 million.
  – For a US household of 3 persons, the payoff is $1,200.

• Political Payoff
  – A new foundation for US-Mexican relations.
  – Fostered Mexico’s transition from a one-party system of state capitalism to a multiparty, market-oriented system.
Impact of NAFTA on US Workers

• More than 400,000 workers lost jobs involuntarily between 1994-2002 because of NAFTA according to Department of Labor – 50,000/year

• Represented less than 2% of the 31 million total jobs lost involuntarily over that period—most jobs were lost because of automation and other nontrade factors.

• However, Hakobyan and McLaren (2016) found that 1.3 million workers experienced slower wage growth of 5% or more during 1990s because of import competition from Mexico.

Trade agreements have little net effect on national employment but do contribute to “churn” in the job market. They are not a leading cause of stagnant wages for non-college American men.
Negotiating Objectives

- Seek reciprocal and balanced trade – reduce bilateral trade deficit with Mexico.
- Secure commitments not to impose customs duties on digital products.
- Include labor and environment provisions in the core of the Agreement and enforce these obligations.
- Remove all restrictions on “Buy America” preferences at the state and municipal level.
- Eliminate NAFTA Chapter 19 Review of AD and CVD determinations.
- Eliminate the NAFTA global safeguard exclusion.
- Reduce or eliminate barriers to US investment in all sectors in the NAFTA countries.

These demands will be strongly resisted by Mexico and Canada.
Alternates to Successful Negotiation: US-Canada

- In talks fail, President Trump has threatened to withdraw from NAFTA.

- If Trump abrogated NAFTA, US-Canada trade relations would largely revert to terms of Canada-US FTA of 1989 (CUSFTA).

- CUSFTA would carry on most of the bilateral trade preferences.

- However, the deal did not address problems that have provoked Trump’s criticism of NAFTA – in particular, Canadian import barriers on dairy and a few other products.

- Canada and Mexico would continue to apply NAFTA to their bilateral trade.
Alternates to Successful Negotiation: US-Mexico

- Mexico and the United States would revert to most favored nation (MFN) tariff treatment like other WTO members.
  - US applied MFN tariffs average 3.5%, Mexican MFN tariffs average 7%.

- But Mexico’s high bound rates—the upper threshold committed to in the WTO—gives it great latitude to raise tariffs beyond MFN.
  - More than 90% of US exports to Mexico (by value) are in products with bound rates above 30% (Amiti and Freund 2017).

- Terminating NAFTA would severely disrupt North American supply chains.
Thank you!