

Intelligence MEMOS



From: Daniel Schwanen
To: The Rt. Honourable Justin Trudeau, Prime Minister and the Honourable Chrystia Freeland, Minister of Global Affairs
Date: October 3, 2018
Re: **NEW AGREEMENT WITH THE UNITED STATES AND MEXICO**

The agreement with the United States and Mexico –the newly dubbed USMCA – is a signal accomplishment.

Considering the circumstances under which Canada was negotiating – the threat of devastating duties on Canada’s auto industry, and great uncertainty about the continuation of the existing NAFTA – you deserve congratulations.

You kept the trade rules trilateral, key given the integration of the North American economy. You staved off toxic US demands, such as a five-year sunset clause, specific targets for US content in autos, further closing of US public procurement to Canadian suppliers, or the threat of duties on Canadian and Mexican goods to relieve US industry from third-country imports.

You essentially kept the NAFTA Chapter 19 dispute settlement mechanism on antidumping and countervailing duties intact, giving Canadians a better chance at impartial treatment and refund of duties improperly levied. The deal also introduces among the three countries some beneficial elements of the Trans-Pacific agreement, such as those facilitating regulatory cooperation and trade for small and medium sized enterprises. Alleviating the threat of US tariffs on Canadian autos on grounds that they constitute a threat to US national security is another success.

As for Canadian concessions on dairy, poultry and eggs, and for US wines in B.C. stores, and the higher de minimis thresholds for courier shipments, those are good for Canadian consumers and Canada’s economy. Indeed, further liberalization could further free Canada from the shackles of supply management in agriculture, and alleviate what will be an awkward differential treatment for postal and courier shipments, and non-matching values for taxes and duties at the border.

Tougher rules of origin on autos – requiring more North American content, and more from higher-wage workers under penalty of reverting to WTO tariffs – will raise costs for industry and consumers, but will not particularly disadvantage Canada. The rationales for lengthening the marketing exclusivity period for biologic drugs – where transparently the US sought a higher return from consumers in other countries for the R&D investments in those drugs – and for extending the period of copyright protection, are less clear-cut from the narrow perspective of Canada, which is a net payer to owners of intellectual property, but the costs of both have been exaggerated.

The biggest disappointment is the maintenance, for now, of the Section 232 tariffs imposed by the United States on steel and aluminum from Canada, and which gave rise to Canadian retaliatory tariffs. This tariff standoff imposes huge costs on both US and Canadian industry. Canada should take its time ratifying the USMCA agreement until the issue is resolved.

Looking ahead, Canadians will need to understand some major institutional changes under the USMCA, such as: the net impact on investor confidence of the commitment to review the agreement every six years, potentially leading to its abrogation within 16 years; the demise of the investor-state dispute mechanism that Canada has consistently sought in its other trade agreements; the clause requiring Canada and Mexico to notify the US of any intent to negotiate with non-market economies (read: China); and the intriguing new chapters on competitiveness and external macroeconomic policy coordination, also essentially aimed at taking a common approach to combating market-distorting policies by other countries (read also: China).

It is clear that some of these provisions, notably those around dispute settlement, will require good will to function. Canadians should hope that debates in the United States over the merit of this agreement, which are now shifting to the Congress, will help reduce the possibility of arbitrary trade policy decisions from the White House, that as the IMF reminded us a few days ago, have undermined growth prospects for the global economy and for Canada.

Congratulations on getting us this far. Keep it up. There is more to do.

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