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## Opinion

### Trump, Trudeau and NAFTA 2.0: Tweak or Transformation?

AMELIA HADFIELD and RUPERT POTTER\*

President Donald J. Trump and Prime Minister Justin Trudeau's first meeting was bound to make waves. Social media was fixated by which of the two statesmen best managed the handshake. The Prime Minister was generally applauded for avoiding being hauled into the President's physical sphere of influence. Images showed the two leaders at press podiums, and in armchairs by the Oval Office desk: separate but generally comfortable. It wasn't exactly the chummy camaraderie Trudeau enjoyed previously with President Barack Obama. And while there was no high-vaunting rhetoric to match John F. Kennedy's 1961 encomium that 'geography has made us neighbours, history has made us friends, economics has made us partners, and necessity has made us allies', the focus on renegotiating the North American Free Trade Agreement (NAFTA) certainly accentuated the challenges of geography and economics.

NAFTA is historic in terms of setting the rules for regional trade. Coming into force in 1994 as the first free trade agreement between two developed and one developing country, NAFTA created a trilateral bloc for free trade in goods and services. At first blush, the numbers appear impressive. Between 1993 and 2015, merchandise trade between the three countries has tripled to US\$1 trillion, with Canadian exports to the US growing annually at 4.6%. NAFTA as a whole accounts for more than a quarter of the world's GDP.<sup>1</sup> Canada and the US together constitute the world's largest bilateral trading relationship, comprising US\$ 663 billion in goods and services in 2015, of which Canada purchased US\$ 337 billion,<sup>2</sup> and with US\$2 billion in trade crossing the US-Canada border each day.

NAFTA's overall impact however is debatable, and arguably uneven. On the one hand are observers suggesting that "since the Canada-U.S. Free Trade Agreement came into force in 1989, Canada's two-way trade in goods and services with the United States has more than tripled,"<sup>3</sup> followed by a marked increase with NAFTA itself that has proved beneficial to all three economies. Others suggest that the previous agreement has 'had a much bigger impact on Canada's economy than NAFTA', that Canada's trade with Mexico is negligible, and that NAFTA's effect on the US itself has been small.<sup>4</sup> From these perspectives, NAFTA appears in need of an

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<sup>1</sup> Claire Brownell, 'NAFTA: It's less important to Canada than you might think', *Financial Post*, February 9, 2017, <http://business.financialpost.com/news/nafta-its-less-important-to-canada-than-you-might-think>.

<sup>2</sup> Office of the US Trade Representative, <https://ustr.gov/countries-regions/americas/canada>.

<sup>3</sup> Government of Canada, [http://can-am.gc.ca/relations/commercial\\_relations\\_commerciales.aspx?lang=eng](http://can-am.gc.ca/relations/commercial_relations_commerciales.aspx?lang=eng). The reference here is to the previous bilateral agreement between the US and Canada which lasted between 1989-94.

<sup>4</sup> Brownell, *supra*.

overhaul given the deeply uneven effects of free trade. Trump played on such misgivings effectively, portraying NAFTA to rust belt city voters as being ultimately responsible ‘for the loss of their high-paying manufacturing jobs’, driven by frequent shifts in production from the US to Mexico.<sup>5</sup>

While such changes are rather more likely to involve currency differentials, automation, and inward investment, along with broader globalising trends in goods, services and capital, the ‘No-to-NAFTA’ message proved compelling. Trump has now committed the US to re-negotiating NAFTA. He does so against the backdrop of severely impaired relations with Mexico (alleging NAFTA as directly responsible for the US’s \$63 billion merchandise-trade deficit), a more positive relationship with Canada, and the need to make good his election promises in trade terms, rather than merely as incendiary bombast.

Taken together, this made for a predictably mottled statement in which despite the US’s ‘very [sic] outstanding trade relationship with Canada’, and a status-quo view to ‘affirm the importance of building on this existing strong foundation for trade and investment and further deepening our relationship’, Trump felt compelled to state that he would be ‘tweaking... certain things’. Interesting that this moderates the more bullish language of the White House website: “If our partners refuse a renegotiation that gives American workers a fair deal, then the President will give notice of the United States’ intent to withdraw...”<sup>6</sup>.

So what are the possible outcomes? Four scenarios present themselves:

- i. Continuation with the status quo (unlikely);
- ii. Minor revisions to NAFTA (possible);
- iii. A new bilateral US-Canada bilateral FTA (possible);
- iv. Withdrawal and return to WTO rules (threatened but less likely).

Key to Canadians is ensuring that trade and investment conditions do not worsen while avoiding any sense of being bullied by Trump (or more diplomatically, pressured). In doing so, they have both vulnerabilities and strengths.

In terms of vulnerabilities, the impact of tariff and non-tariff barriers - if taken across the board – would arguably have a greater effect on Canadian GDP than that of the US. For Canada, bilateral trade with the US is more than 60% of its national total, while for the US, trade with Canada constitutes less than 20% of its GDP.<sup>7</sup> Sectoral weaknesses are another problem: including soft-wood lumber, oil and gas exports, and steel. The spike in American natural and shale gas production has provided challenging for Canadian producers. The promised go-ahead by Trump on the Keystone-XL pipeline transiting oil from the Albertan tar sands to US refineries on the Gulf Coast may grant Canada access to other markets for its oil and gas, but against a sluggish market, and in the face of recent US suggestions of transit tariffs.

In terms of strengths, Canada buys more from the US than any other country, represents the primary commercial customer in 35 US states, and has US\$351 million of direct investment in the US as at 2015,<sup>8</sup> with one study suggesting that over 8 million US jobs depend on Canadian trade and investment.<sup>9</sup> In diplomatic terms, Canada can also draw on its membership of the (as yet

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<sup>5</sup> Brownell, *supra*.

<sup>6</sup> The White House, <https://www.whitehouse.gov/trade-deals-working-all-americans>.

<sup>7</sup> US Trade Representative, <https://ustr.gov/countries-regions/americas/canada> and The United States Census Bureau, <https://www.census.gov/foreign-trade/statistics/highlights/toppartners.html>.

<sup>8</sup> Government of Canada, [http://can-am.gc.ca/rerelations/commercial\\_relations\\_commerciales.aspx?lang=eng](http://can-am.gc.ca/rerelations/commercial_relations_commerciales.aspx?lang=eng).

<sup>9</sup> Centre for Policy Studies, Victoria University, [http://www.copsmodels.com/pdf/canada\\_trade\\_2013.pdf](http://www.copsmodels.com/pdf/canada_trade_2013.pdf).

unratified) 11 state Trans-Pacific Partnership (from which the US withdrew in January 2017), and its newly-ratified Comprehensive Economic and Trade Agreement (CETA) with the EU. Nailing down a renewed, 'tweaks-only' NAFTA could represent a strong third platform for Canada in international trade. As argued recently by Canadian Foreign Affairs Minister Chrystia Freeland, while "...the TPP as a deal cannot happen without the United States being a party to it," if Canada somehow manages to resurrect it, the country could subsequently position itself as a conduit of Pacific-US-Atlantic trade.<sup>10</sup>

Against this backdrop, the US risks not only the stated *promise* of economic protectionism but the *prospect* of trade-based isolationism, having withdrawn from the 11 state Trans-Pacific Partnership, and failing with the EU to resurrect the Transatlantic Trade and Investment Partnership (TTIP). Scuppering NAFTA – despite its initial description by Trump as “the worst trade deal maybe ever signed anywhere...” - looks less and less sagacious. It also suggests that the third option of 'minor revisions' to NAFTA is the most likely. Strategic 'tweaks' could for example focus on tightening NAFTA's country of origin provisions, and its dispute settlement mechanism for non-NAFTA investors.

Whatever the approach, the optics remain critical. President Trump needs to be seen to protect US jobs, based on his ability not to destroy an unpopular \$2 in order to earn a popular \$1. Equally, Prime Minister Trudeau wants to remain flexible but not pliant. It's a tension which lies at the heart of Canada's broader foreign policy: the need for a positive collaborative relationship with the US, whilst establishing a distinctive Canadian influence and identity globally.<sup>11</sup> If negotiations fail and the deal is torn up, consumers and workers on both sides of the border are likely to suffer. Trump's anti-Mexico crusade could kick-start a Mexican recession which would hit both the US and Canada. Barriers will limit profitability, cause retrenchment, limit competition, and create unemployment. If however Trump supports in policy what he recently articulated in public, namely that 'more jobs and trade right here in North America is better for both the United States and it is also much better for Canada', then a renegotiated NAFTA stands a chance.<sup>12</sup>

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<sup>10</sup> Reuters, <http://uk.reuters.com/article/us-usa-trump-trade-canada-idUKKBN1582P3>.

<sup>11</sup> See Amelia Hadfield, 'Maple Leaf Zeitgeist? Assessing Canadian Prime Minister Justin Trudeau's Policy Changes', *The Round Table*, Vol. 106, 2017, pp. 23-35, <http://www.tandfonline.com/doi/full/10.1080/00358533.2016.1272954>.

<sup>12</sup> Robert Fife and Adrian Morrow, 'Trump vows to only tweak Canadian NAFTA provisions after Trudeau meeting', *The Globe and Mail*, February 13, 2017, <http://www.theglobeandmail.com/news/politics/trudeau-trump-sit-down-in-oval-office-for-first-face-to-face-meeting/article33998164/>.