Tuesday, October 16, 2018

The North American Relationship: Preparing for the Future

Hosted by Carleton University's Initiative for Parliamentary and Diplomatic Engagement

Panelists

Hugo Perezcano Diaz, Deputy Director, International Economic Law, CIGI and former lead counsel for Mexico in investor-state dispute settlements
Meredith Lilly, Associate Professor and Simon Reisman Chair in International Affairs, Carleton University
Christine McDaniel, Senior Research Fellow, American Economy and Globalization, Mercatus Centre, George Mason University and former Deputy Assistant Secretary at the Treasury Department and senior trade economist in the White House Council of Economic Advisers

Moderator

Fen Osler Hampson, Chancellor's Professor, Carleton University and Distinguished Fellow & Director of Global Security & Politics, CIGI

Opening Remarks

Maureen Boyd, Director, Carleton Initiative for Parliamentary and Diplomatic Engagement

- The North American economic relationship was a featured panel earlier today at the 14th meeting of the North American Forum, a private, non-partisan institution that meets annually to engage 25 to 30 senior leaders from each of Canada, Mexico and the United States
- The North American Forum concentrates on ways of enhancing North American cooperation - in areas of competitiveness, trade, finance, energy, and defence and security
- This panel was put together by CIGI – the Centre for International Governance Innovation – an independent, non-partisan think tank that aims to bring clarity and innovative thinking to global policy making.
- Maureen expressed thanks to the North American Forum and to the Centre for International Governance Innovation

Primer Presentation

Meredith Lilly, Associate Professor and Simon Reisman Chair in International Affairs, Carleton University and former Foreign Affairs and International Trade Advisor to Prime Minister Harper opened the panel with a primer on the North American relationship.

- Canada's economic growth is projected to remain flat at 2% while its population ages
- The United States and Mexico are expected to be 'younger and stronger' with younger demographics and be half as dependent on immigration.
  - The U.S. and Mexico will be among the world's largest economies
  - The U.S. is expected to be a decade behind Canada with its dependency ratio

  - Mexico will see its old age dependency ratio rise from 10 to 22, which is still a very healthy ratio
- The U.S. can expect to remain an economic powerhouse. Although its growth will flatten out, its strong internal economy will protect it.
- China's future economy will present challenges for Canada as it wants to become a global leader in the same areas as Canada. For example, China wants to be a leader in artificial intelligence (AI) and robotics, which it is expediting through tactics like intellectual property theft. Chinese success in these areas would reduce its interest in importing such goods from Canada.
- Meredith highlights three points:
  - Canada has been in a privileged place in the last few decades but should not expect to maintain that
  - Canada must continue to trade
  - Canada is more isolated and dependent on trade than Mexico
- Canada should continue its pursuit of robotics and AI, but should not underestimate its capacity to produce natural resources. India will soon have the world's largest population and Mexico will have a middle class larger than Canada's entire population. These growing economies will need natural resources from Canada.

The panel discussion begins with questions from the moderator, Fen Hampson.

Fen asks Christine: *Does the USMCA put America first?*

Christine responds:
- President Trump has followed through with many of his campaign promises and his heated rhetoric plays well with his base. However, it is important to separate Trump's tweets from his actions.
- It is a good idea to modernize trade agreements and it is appropriate to review NAFTA
- Focusing on the positive elements, it is great that North America is sticking together.

Fen follows up by asking Christine: *What did the U.S. get out of the deal?*

Christine responds:
- USMCA is in many ways a mirror of TPP but only for three countries. Gains for U.S. consumers include greater market access. In terms of the automotive industry, U.S. workers are not winners and consumers can expect the prices of vehicles to rise.
- The biggest win from the agreement is that investor confidence is restored and North American trade is solidified.
- Fen and Christine agree that there are not any large gains for the U.S.

Fen asks Hugo: ***Why was Mexico in such a rush to negotiate the agreement and why does it see itself as a winner?***

Hugo responds:

- Hugo does not see any of the three countries as winners of the agreement but is happy to see a trilateral agreement.
- USMCA has some wins for all three countries but pretty much remains status quo.
- For example, the new agreement is neither a win for Mexican autoworkers nor an improvement to NAFTA.
- The regulatory burden has led enterprises to hire more lawyers and consultants than engineers.

Fen asks Meredith: ***Some say the U.S. forced Canada to make an agreement. What did Canada get out of the deal?***

Meredith responds:

- An agreement is important for economic stability and certainty. However, Canada is still far from achieving certainty, especially considering the agreement has not yet been ratified.
- Meredith proposes that the only reason Canada signed on to the agreement is out of serious concern that it would be subject to U.S. auto tariffs.
    - Trump threatened Canada and Mexico with auto tariffs on multiple occasions.
    - The credibility of these threats is demonstrated in the Korea/U.S. trade agreement which outlines new voluntary export restraints and delayed tariff phase in period for trucks.
- The alternative to the NAFTA agreement was not the old NAFTA, it was a removal of NAFTA plus the imposition of tariffs. To some extent, Canada's back was against the wall.

Fen asks Hugo: ***Mexico was prepared to give up Chapter 19's dispute settlement mechanism. Chapter 19 was make-or-break for Canada. Now that you've seen the agreement, when it comes to the dispute mechanism, does it matter? Or does the U.S. do what it wants to do, anyways?***

Hugo responds:

- First of all, it is important to distinguish that there are three dispute mechanisms.
- Mexico's decision was to leave the dispute mechanism as it was, so it got what it wanted, but it is not a functioning mechanism.
- Investor-state dispute mechanism means something different in Mexico than it does in the U.S. or Canada. In Mexico, it was a safeguard for maintaining stability. The mechanism as a part of the FTA is above state and federal law. However, the mechanism has become watered down.

- Trump is a critic of free trade and NAFTA. His ideology is more government intervention in economic activity which may be a problem for Mexico.
- With regard to Chapter 19, Hugo thinks that Mexico wrongly threw in the towel. In a protectionist era, it is easy to believe that there will be an increase in anti-dumping cases, while at the same time the WTO dispute settlement mechanism is under strain. Something like Chapter 19 would allow states to resolve these disputes more quickly than going through the WTO.
- Mexico will benefit from Canada fighting for Chapter 19 to be included in USMCA.

Fed asks Christine*: How have the sections on intellectual property rights played out in the United States? Do people care?*

Christine responds:

- Intellectual property rights are already in existence in Mexico, Canada, and the U.S., so integrating it into the USMCA was not a big stretch.
- Biologics are extremely expensive to develop and consequently the industry argues for a longer data exclusivity time period. TPP asked for 12 years of exclusivity, which is twice as long as the five to seven-year standard enacted in most countries.
- The U.S., unlike Canada, was intent on attaining a long period of exclusivity.
- Intellectual property rights are intricately linked with the regulatory regime. Since regulatory regimes vary on a state-by-state basis, the intellectual property rights regime of one state may not necessarily apply in another state.
- The U.S. negotiated for USMCA to include a 12-year exclusivity period but ultimately agreed upon a 10-year period.

Fen follows up by asking Christine*: Is the agreement good for big pharma?*

Christine responds:

- Longer intellectual property rights are not necessarily beneficial to get bio-similars on the market as soon as possible.

Fen asks Meredith*: You spoke about dairy quotas at the North American Forum, where you added up all of the dairy quotas over various trade agreements. Is this really death by a thousand cuts for the dairy industry?*

Meredith responds:

- Canada's commitment at the beginning of the negotiations was that it would defend Canada's supply management system. By the end of the negotiations, Canada had granted the U.S. access to 3.6% of its dairy market.
- The difficulty here is that in a very short period of time, Canada has granted a cumulative 10% of its access to the dairy market through CETA, TPP, and USMCA. The sector has yet to adjust to this.

- Problematic concerns include that this newly granted access disproportionately impacts Quebec. Alternatively, Ontario's loss is slightly offset by its win with the auto industry.
- USMCA now requires provincial support to implement these measures and there is no guarantee that Quebec's newly-elected provincial government will cooperate.
- The 10% of access touches all three legs of the supply management stool.
    - Supply management has three pillars: protection from foreign imports, control of the supply, and control of prices. These three pillars (or legs of the stool) must balance.
    - Meredith expressed concern that it is becoming difficult to support the system and afford to compensate the farmers accordingly.
    - Consumers will not see lower prices because the system is still in place. Instead, maintaining this system will prove to be extremely costly to tax payers.

Fen asks Christine*: What will happen next with USMCA? Will it sail through without too much difficulty? Will it be ratified soon?*

Christine responds:

- Christine does not see USMCA having a hard time passing but "you never know"
- It may depend on midterms. The House may pick up a few Democratic seats and the Senate may pick up a couple of Republicans. Regardless, it is hard to see how either Democrats or Republicans would choose to not support USMCA.

Fen asks Meredith: *Steel and aluminum tariffs remain and there is no agreement or timetable to remove them.*

Meredith responds:

- There is currently no agreement to end the steel or aluminum tariffs.
- Based on the way these types of events have unfolded historically, Canadians may be waiting quite a while before tariffs are removed even though it was a negotiating tool.
- If removing these tariffs was not done as part of the USMCA negotiations, then the tariffs take a long time to unravel.

Fen follows up by asking Meredith*: Should Mexico and Canada use ratification as leverage to have the tariffs removed?*

Meredith responds:

- Canada and Mexico should certainly coordinate a unified position.
- Although Canada and Mexico technically do have leverage since USMCA has not yet been ratified, there is a danger that Trump would counter by threatening to tear up the agreement.
    - **Christine** disagrees and says that Congress would not allow Trump to tear up the agreement.
    - **Hugo** thinks the agreement will be ratified by all three countries. However, there is a chance that tariffs will remain in place in a different sense. For example,

there may be duty-free quotas for a certain volume of steel, aluminum or cars. Mexico and Canada have agreed that if the U.S. imposes tariffs on autos then they will implement a quota. Therefore, tariffs may not completely disappear but we will compromise on a quota.

- Meredith says Canada's best hope to have tariffs eliminated is for U.S. businesses to express to their government that tariffs are hurting Americans.

Fen asks Christine: ***The China clause will draw a red line for many other trading partners with the U.S. This is rallying other countries in Europe and Japan to really stick it to the Chinese. Do you read it that way?***

Christine responds:

- No, Christine does not read it that way. This is a continuation of a longstanding U.S. position on non-market economy issues that largely pertain to China. If you go back, President Bush pursued an engagement strategy that was continued by President Obama until the global financial crisis. After the crisis, the U.S. position turned to teaming up with like-minded allies to set stronger rules on State-Owned Enterprises, intellectual property rights, cyber security, cyber theft, and subsidies. TPP was intended to set stronger rules on these issues and rein in China that way but Trump pulled out of the agreement.
- The plan was to implement section 3.1 against China on IP, with the support of U.S. allies, followed by Section 232 tariffs. However, following discussions within the White House, it was decided that 232 tariffs would be imposed first and that significantly changed things (to put it mildly).
- The U.S. must team up with like-minded countries on issues such as intellectual property.
- In regards to the China clause (it's a non-market economy clause), it is not a bad idea to have Canada and Mexico on the same page before one of the countries signs a FTA with a non-market enterprise.

Fen asks Meredith: ***Is Canada's biggest problem getting its products and energy to market?***

Meredith responds:

- Meredith believes that the idea of a FTA with China is an old idea that does not make very much sense 20 years in the future.
- China's economy will have plenty of problems. Canada should work very hard to sell China health services. However, it is unlikely that China would be interested in buying Canadian robots.
- The current government's position towards this new clause is to say that there is no infringement on Canadian sovereignty, but we need to think critically about it. There is a reason the clause is there – it is there because the U.S. wants it there and it does not want Canada to sign a FTA with China. It is a geopolitical difference of opinion.
- Canada is now being called upon to choose between China and the U.S.
- The U.S. will likely ask other countries to sign this type of a clause in future agreements.

Fen invites the audience to ask questions.

The first member of the audience comments:

- Section 32 has geopolitical consequences and the world has taken note. This may ease the position of the North American partners of the U.S. but it may make life harder for India and China.
- Soon, when China and India will be the largest consumers in the world, countries will want to have agreements with these two economies.
- It goes without saying that the future of Canada will lie in natural resources. However, he disagrees with Meredith and believes that China might be interested in buying Canadian robots in the future.
- In regards to intellectual property, it would have been in Canada's interest to extend the patent protection period.
  - Strong IP rules attract R&D which leads to huge value added in industries such as the pharmaceutical industry.
- In regards to supply management, other countries have discontinued supply management. For example, Australia eliminated its supply management framework and has become the world's largest dairy exporter. Although compensation to Canadian farmers is necessary, it may be worthwhile to eliminate the system in time.

Meredith responds:

- With regard to intellectual property, Meredith thinks that if Canada has robotics and AI to trade with China in the future, a lot of this will have to do with intellectual property and patent protection.
- However, extending patent protections will make pharmaceutical drugs more expensive for consumers.

The second member of the audience asks: *Did anyone from the U.S. speak in favour of auto tariffs? Why do you think President Trump was serious about imposing these tariffs because I do not think Congress would allow that to happen.*

Meredith responds:

- President Trump has already taken action that damages domestic industry and he seems comfortable with that.
- The new auto rule of origin is not what the three countries wanted and will make production more onerous and expensive. It may inadvertently cause automakers to choose to pay the WTO tariff than to produce domestically. Therefore, the only way for President Trump to succeed in his American First manufacturing strategy is to do away with the WTO tariffs. Trump would have to bring in 232 tariffs against China and protect everyone who is inside of his 'great tariff wall' (i.e. Europe, Japan, Canada).

Christine responds:

- Comments on how many people have been wondering what the 'end game' is for autos. The U.S. seems to be interested in hybrid and electric vehicles. Maybe the U.S. will focus on ensuring that these two types of vehicles are made domestically.

The second member of the audience asks Christine a follow-up question: *Do you perceive a circumstance where Trump might sign the TPP?*

Christine responds:

- Christine agrees that this is a possibility. This administration wants stronger rules on state-owned enterprises, subsidies and intellectual property.
- If by next year we can get a plurilateral on state-owned enterprises and subsidies, then that could be the bridge to TPP
- Stresses that the issue is not with China per-say, the issue is with non-market economies that are so disruptive. Whenever the Chinese government decides to go after a particular priority sector, massive amounts of labour and capital pour into that sector. Subsequently, massive amounts of production from China flood into other countries and disrupt foreign markets. Ultimately this disruption leads to anti-trade rhetoric which makes the situation worse.
- Christine expressed how she would love to see trading partners come up with stronger rules on state-owned enterprises and subsidies to determine a more viable, sustainable solution. Afterwards, we can turn back to TPP.

Thank You by Maureen

- Maureen thanks all of the panelists, the moderator, MP co-sponsors, and program sponsors, noting the presence of representatives from TD
- Introduces Dr. André Plourde, Carleton University, Dean of the Faculty of Public Affairs.

Closing remarks by Dr. Plourde

- Dr. Plourde reflects on how this panel has reminded him that sometimes trade negotiations are depressingly not centered around concerns related to *consumers*. These agreements are ways of codifying non-tariff barriers. Calling these agreements a 'FTA' is almost a disrespectful way of using those words.
- In regards to Quebec, he believes it is death of one thousand cuts that will cost Canadian tax payers massive amounts of money without the kind of economic gains that Australia has experienced.
- Dr. Plourde expresses concern about potentially not seeing a TPP agreement.
- Expresses thanks to everyone.

Discussion summary prepared by **Claire Crawford**, Master's candidate, Norman Paterson School of International Affairs, Carleton University