

# NAFTA and Its Renegotiation

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*For presentation at Adult Learning Institute*  
*Oakland Community College*  
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# Outline

- NAFTA
  - What it is
  - What have been its effects
- Renegotiation
  - Timeline
  - Issues
  - Autos
  - Prospects

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# NAFTA

- North American Free Trade Agreement among US, Canada, Mexico
- FTA =
  - Zero tariffs on imports from partners
  - Unchanged tariffs on imports from outside
  - Rules of origin (ROOs) to qualify for zero tariffs



# NAFTA

- History
  - Negotiated under George H.W. Bush
  - Approved by Congress under Clinton
  - Went into effect 1994
  - Followed at end of 1994 by Peso Crisis
    - Mexico's currency fell by half
    - Mexico plunged into recession

# Outline

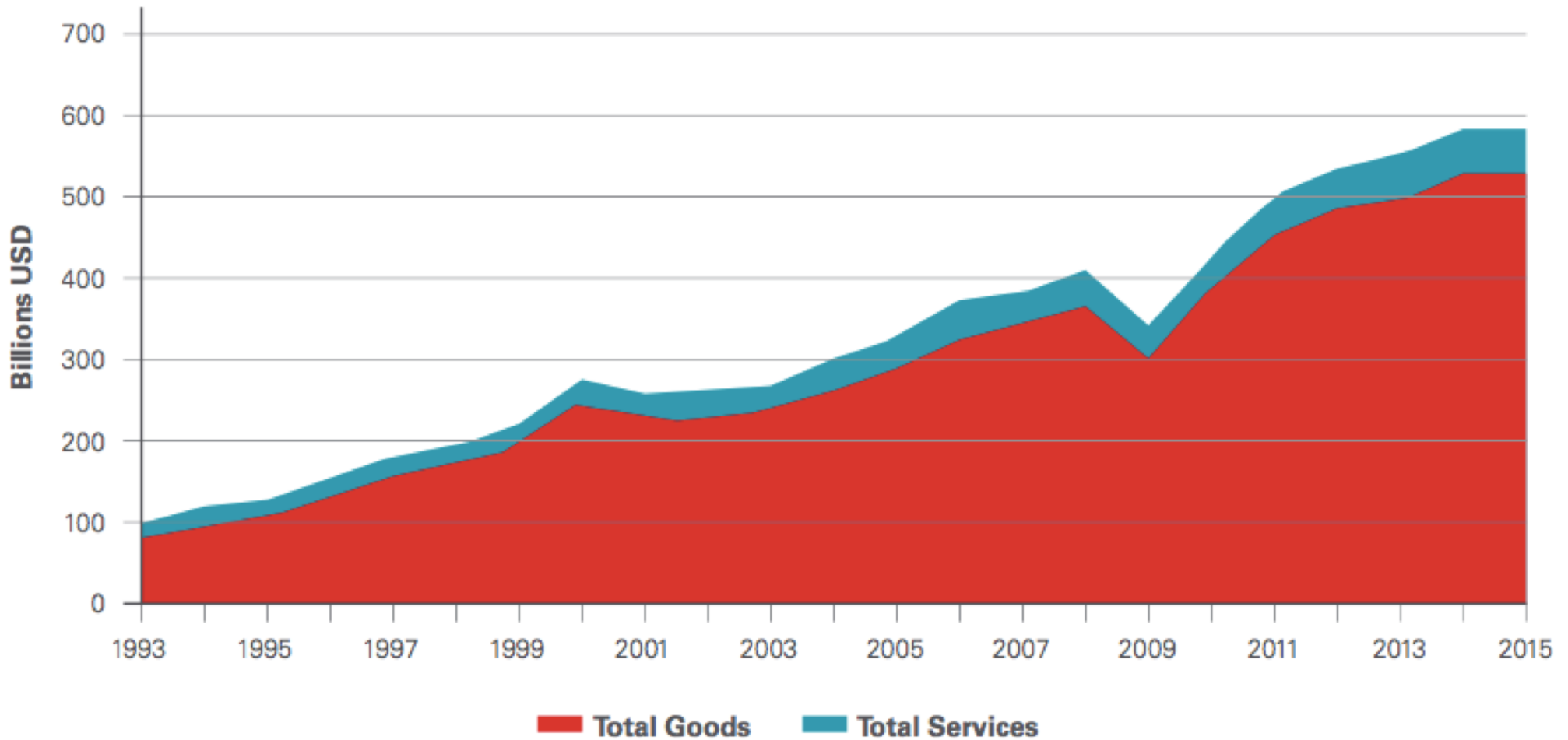
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# NAFTA Effects

- Trade
  - Grew massively across N. America
  - US bilateral trade with Mexico became deficits: US imports > US exports



**Figure 1. U.S.-Mexico Trade in Goods and Services (1993-2015)**



*Source: U.S. Census Bureau for goods trade; U.S. Bureau of Economic Analysis and OECD for services trade. See endnote two for more details.*

From: Wilson, Christopher, *Growing Together: Economic Ties between the United States and Mexico*, Wilson Center, March 2017.

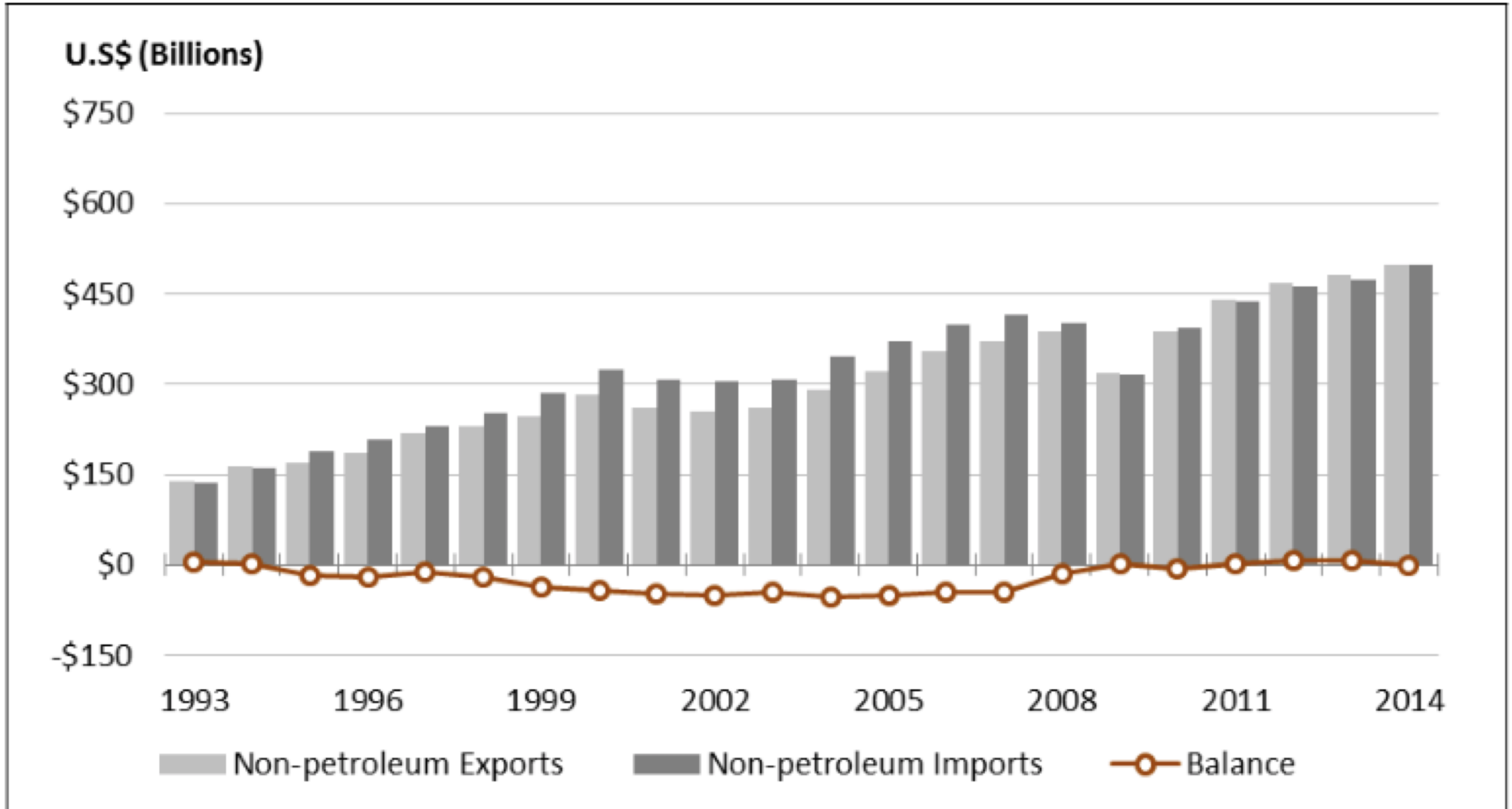
## Figure I. U.S. Merchandise Trade with NAFTA Partners: 1993-2014

(billions of nominal U.S. dollars)

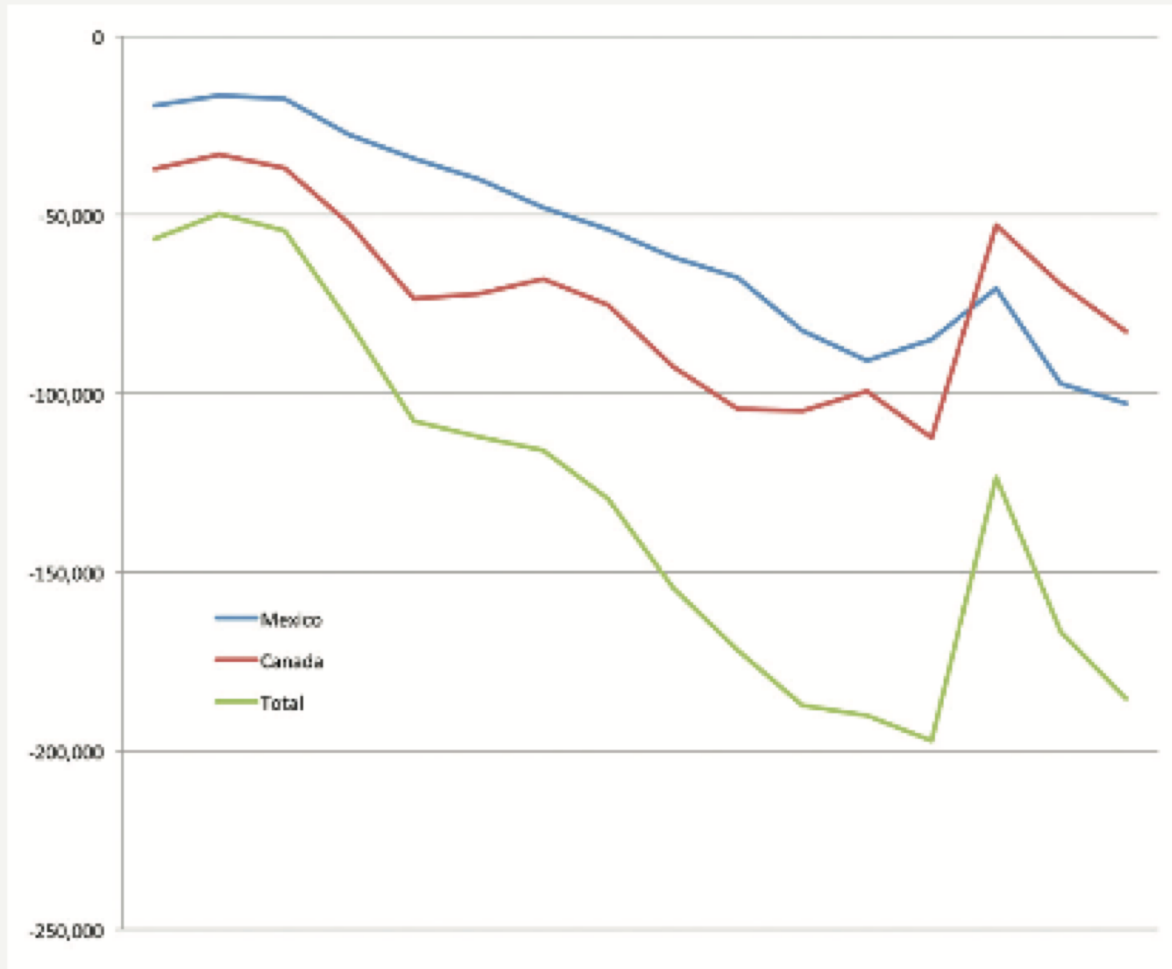


**Figure 2. Non-Petroleum Trade with NAFTA Partners: 1993-2014**

(billions of nominal U.S. dollars)



## Trade Deficits with NAFTA Countries, 1996-2011 (USITC Dataweb)



**U.S. trade deficits increased after NAFTA came into effect.**

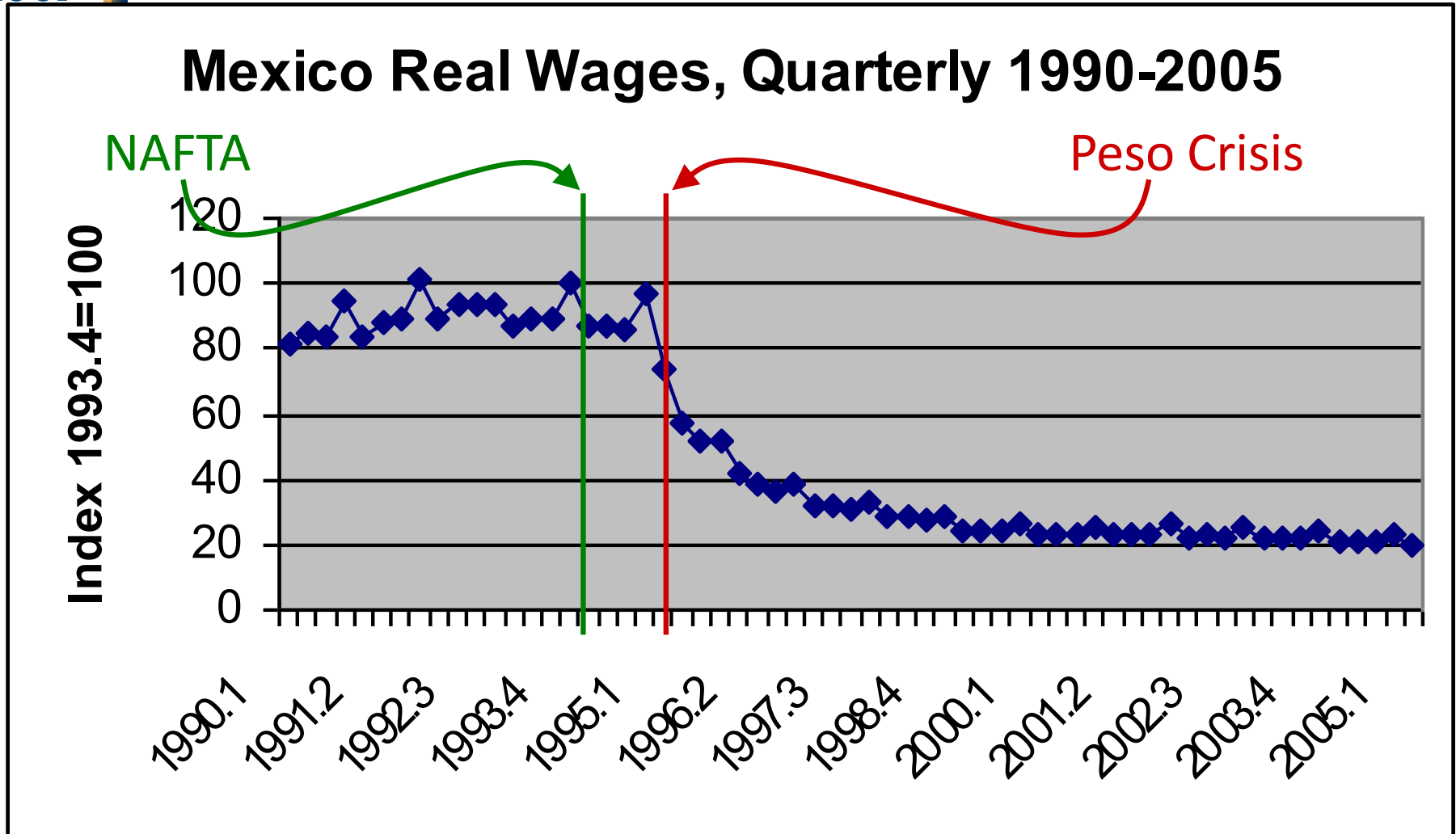
# NAFTA Effects

- Wages
  - Fell in Mexico
  - No effect on average in US

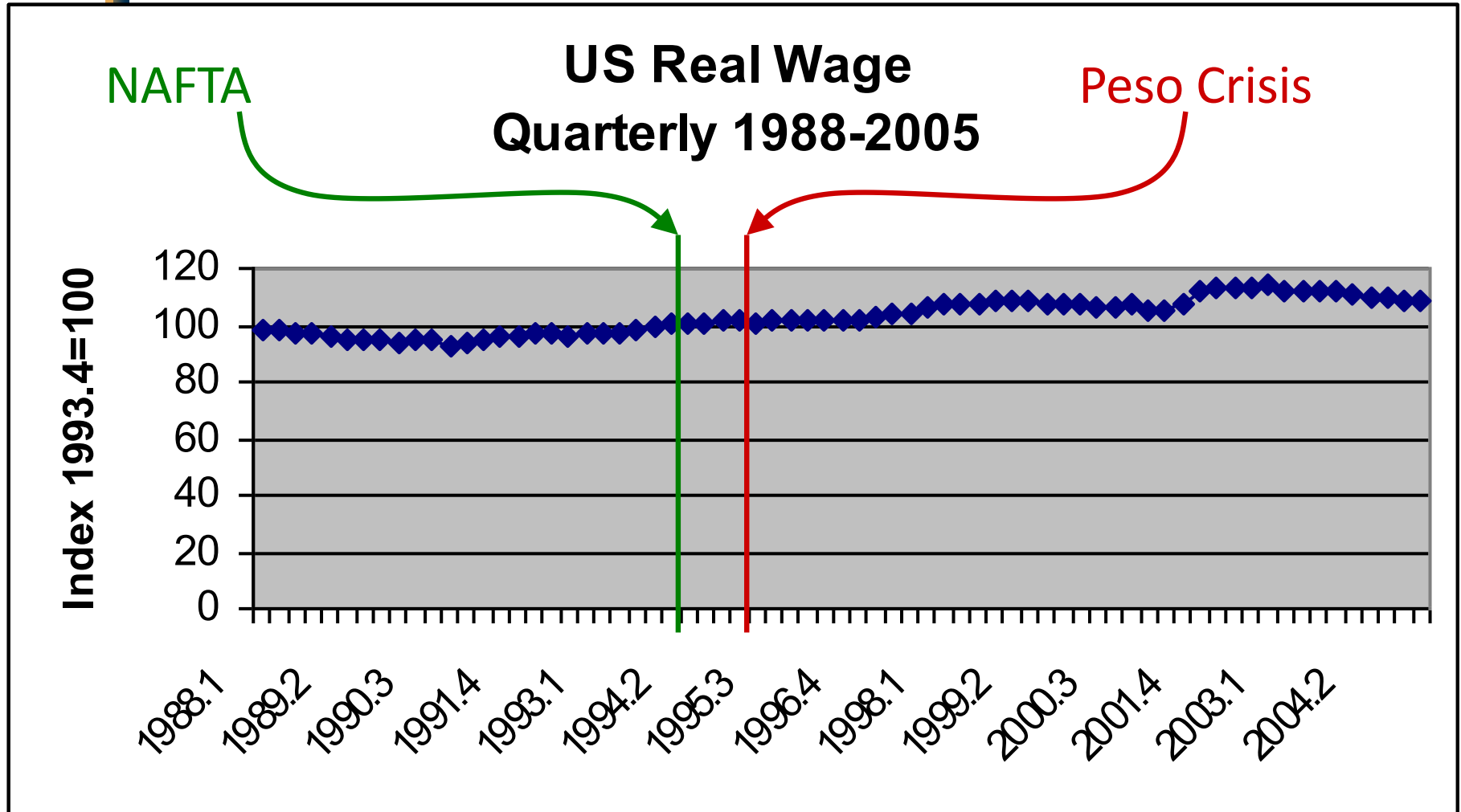


# What Happened: Mexico

## Real Wages Plummeted!



# What Happened: U.S. Real Wage: No Change



# NAFTA Effects

- Employment
  - No effect on overall US employment or unemployment
  - Pockets of disruption across US

# What Happened: U.S.

Unemployment: No effect (or fell)

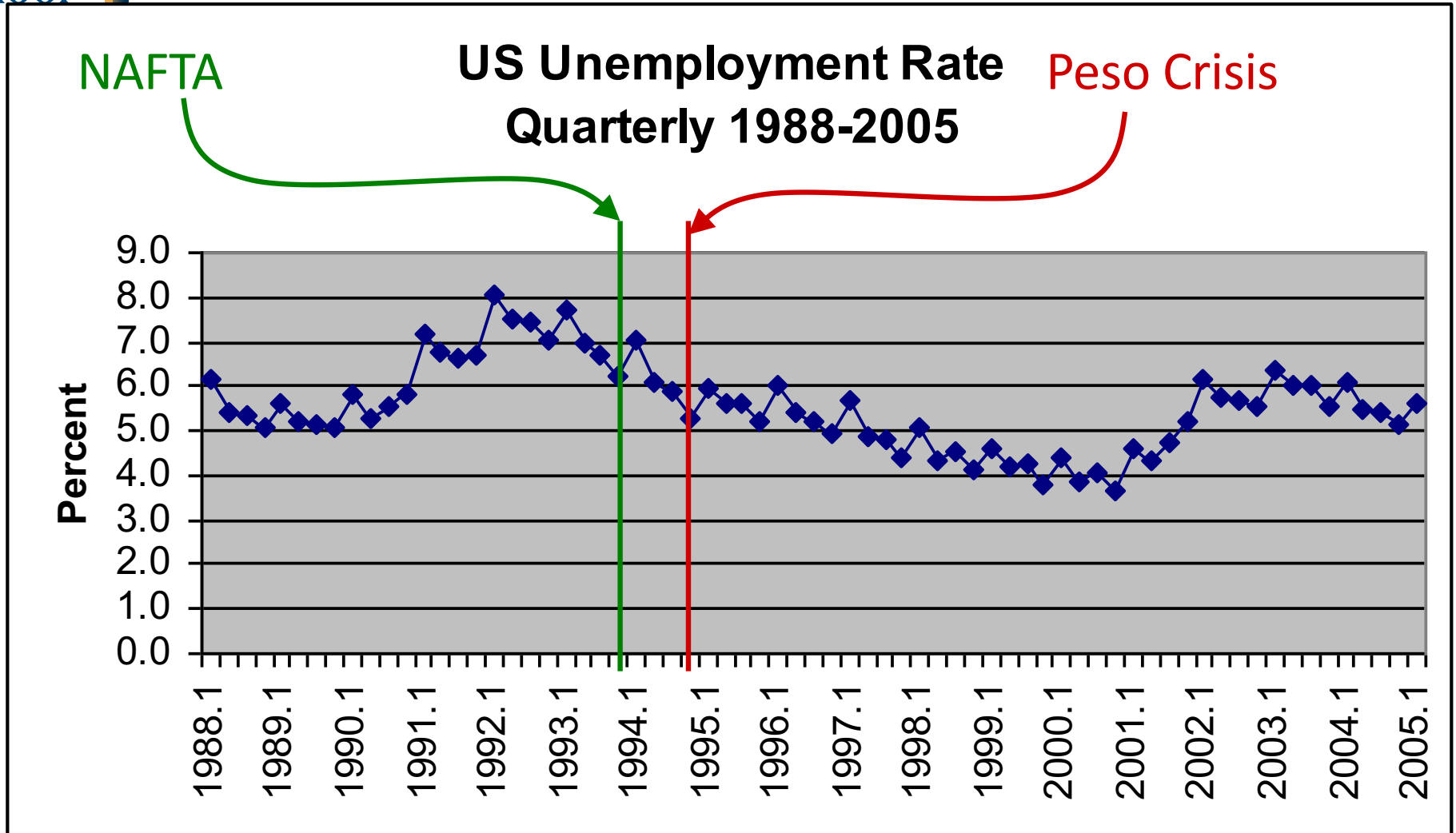


TABLE 3.—MOST AND LEAST VULNERABLE CONSPUMAS, EXCLUDING AGRICULTURE

State	Counties/Cities	$loc\tau_{1990}^c$ (%)
<b><i>A: Top Ten Most Vulnerable Conspumas</i></b>		
Georgia	Catoosa, Dade, Walker	4.74
North Carolina	Alamance, Randolph	4.41
South Carolina	Oconee, Pickens	4.24
South Carolina	Including Cherokee, Chester, Chesterfield, Clarendon	3.67
South Carolina	Anderson	3.62
North Carolina	Cabarrus, Rowan	3.54
North Carolina	Alexander, Burke, Caldwell	3.51
South Carolina	Including Abbeville, Edgefield, Fairfield	3.47
North Carolina	Cleveland, McDowell, Polk, Rutherford	3.46
Indiana	Gary	3.32
<b><i>B: Top Ten Least Vulnerable Conspumas</i></b>		
D.C.	Washington	0.09
Washington	Kitsap	0.19
Virginia	Arlington	0.21
Maryland	Calvert, Charles, St. Mary's County	0.23
Montana	including Flathead, Lincoln, Missoula, Ravalli	0.27
Maryland	including College Park, Hyattsville, Prince George's	0.28
Virginia	Alexandria	0.29
Montana	Including Big Horn, Blaine, Carter, Chouteau	0.30
South Dakota	Including Aurora, Beadle, Bennett, Brule, Buffalo	0.30
Iowa	Calhoun, Hamilton, Humboldt, Pocahontas, Webster	0.30

# NAFTA Effects

- Supply chains
  - US manufacturing moved inputs to low-cost locations across N. America
  - US firms became more competitive with firms abroad

# NAFTA Effects

- Consumers
  - As always with freer trade, the ultimate beneficiaries are consumers
    - Lower prices for
      - Imported consumer goods
      - Domestically produced goods and services that use cheaper imported inputs
    - Greater variety of goods to choose from
  - These gains are hard to measure
    - One indicator may be the low rates of price inflation experienced under NAFTA

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# NAFTA Renegotiation

- Donald Trump
  - Trump opposed NAFTA as early as 1993
    - “The Mexicans want it, and that doesn't sound good to me.”
  - As candidate in 2016
    - “The single worst trade deal ever approved in this country”
  - After inauguration Jan 23, 2017

**WSJ: President Donald Trump Makes Revised Trade Deals an Early Priority**

Two days after taking office, Nafta renegotiation and a potential bilateral pact with the U.K. are on the agenda

# NAFTA Renegotiation

- Donald Trump
  - April 26: Threatened to pull out of NAFTA completely
  - April 27: Decided not to, and to renegotiate instead
  - May 18: Formally launched renegotiation

# NAFTA Renegotiation

- August 16, 2017: Negotiations began
  - Round 1: Aug 16-20, Washington, DC
  - Round 2: Sep 1-5, Mexico City
  - Round 3: Sep 23-27, Ottawa
  - Round 4: Oct 11-15, Washington, DC
  - Round 5: Nov 17-21, Mexico City
  - Round 6: Jan 23-28, Montreal
  - Round 7: Feb 25 – Mar 5, Mexico City
  - Round 8: Planned for Apr 8, Washington, DC, on hold
    - “High-level” meetings happening instead
    - Aim to finish by early May

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# Renegotiation Issues

- Issues (US)
  - Trade imbalances
  - Reciprocal duty-free market access
  - Rules of origin
  - Regulations
  - Services
  - Digital trade
  - ISDS
  - State-owned enterprises
  - Labor standards
  - Chapter 19
  - Procurement
  - Currency manipulation
  - Sunset clause

# Renegotiation Issues

- Other Issues (Canada)
  - Gender rights
  - Indigenous rights
  - Freer movement of professionals
  - Dairy & poultry
  - Cultural exemptions

# Renegotiation Issues

- Other Issues (Mexico)
  - Avoid increased US tariffs on Mexico's exports (80% of Mexico's exports are to the US)
  - Anti-corruption
  - Energy, financial services and telecommunications
  - Guest worker program in US

# Issues in More Detail

- Trade imbalances
  - The US top priority is to “Improve the U.S. trade balance and reduce the trade deficit with the NAFTA countries.”
  - That is not something that can itself be written into the NAFTA agreement
  - So the question will be which changes in the agreement might do this
  - One possibility is a “trigger mechanism” that raises tariffs if goal of reducing deficit is not met
  - Most economists agree that trade deficits
    - Are not the result of trade policies
    - Don’t mean deficit country is losing
    - Result from spending more than income



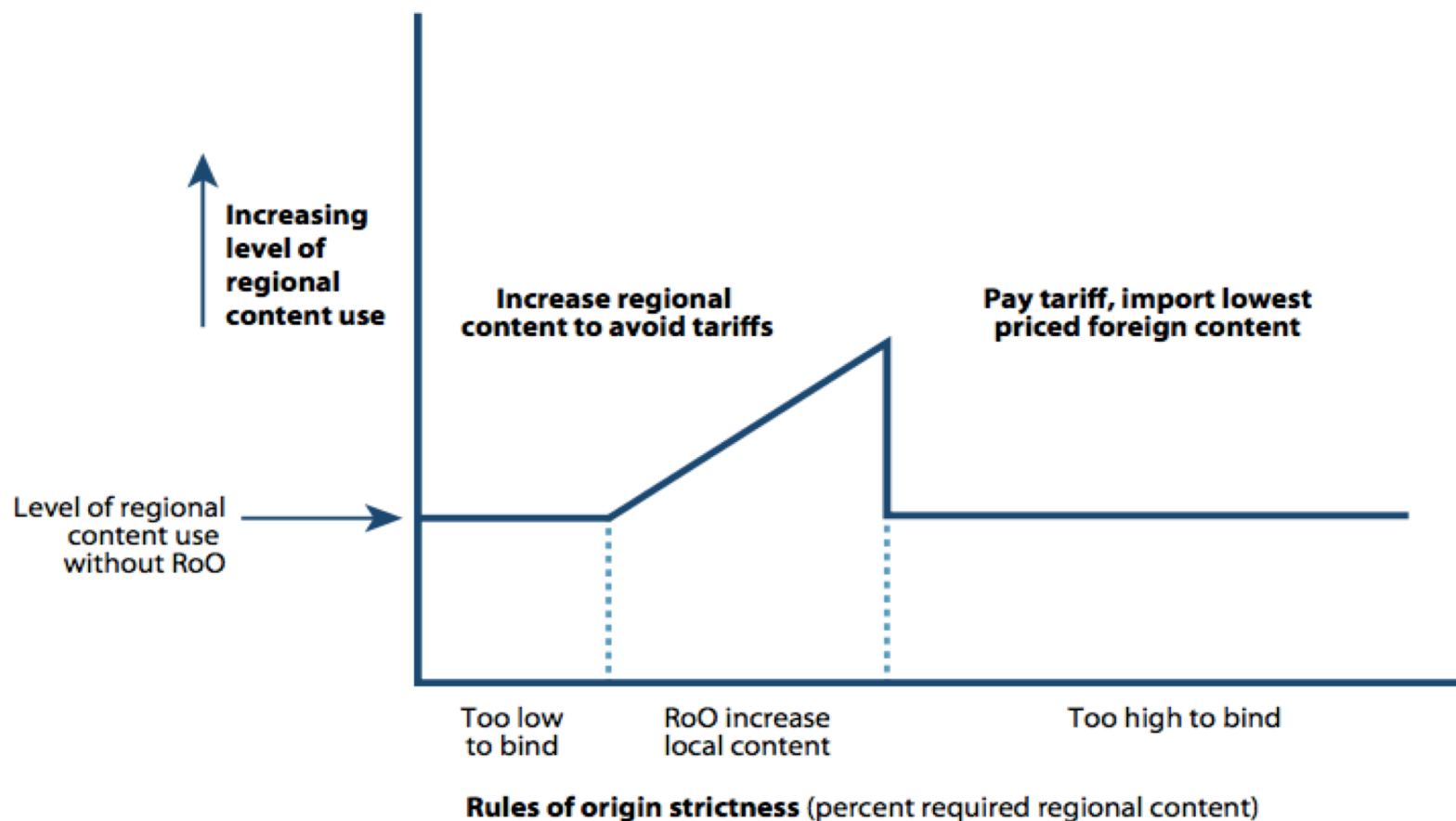
# Issues in More Detail

- Rules of origin
  - The TPP would have reduced the requirement for North American content in autos from 62.5% to below 50%.
  - The new NAFTA will almost certainly increase this requirement for autos and other products, to 85%.
  - The question will be: how much, and how disruptive will it be
  - If too high, some producers will revert to sourcing from outside NAFTA
  - Lighthizer wants “higher NAFTA content and substantial (50%) American content”.
    - That would be unprecedented in an FTA
    - That has now been dropped, in favor of other more complex requirements (e.g., % from high-wage labor)

# How Tighter Rules of Origin Can Increase Imports

For  
School

Figure 2 Regional content and rules of origin at the firm level



RoO = rules of origin

From: Freund, Caroline, "Streamlining Rules of Origin," Policy Brief 17-25, Peterson Institute for International Economics, June 2017.

# Issues in More Detail

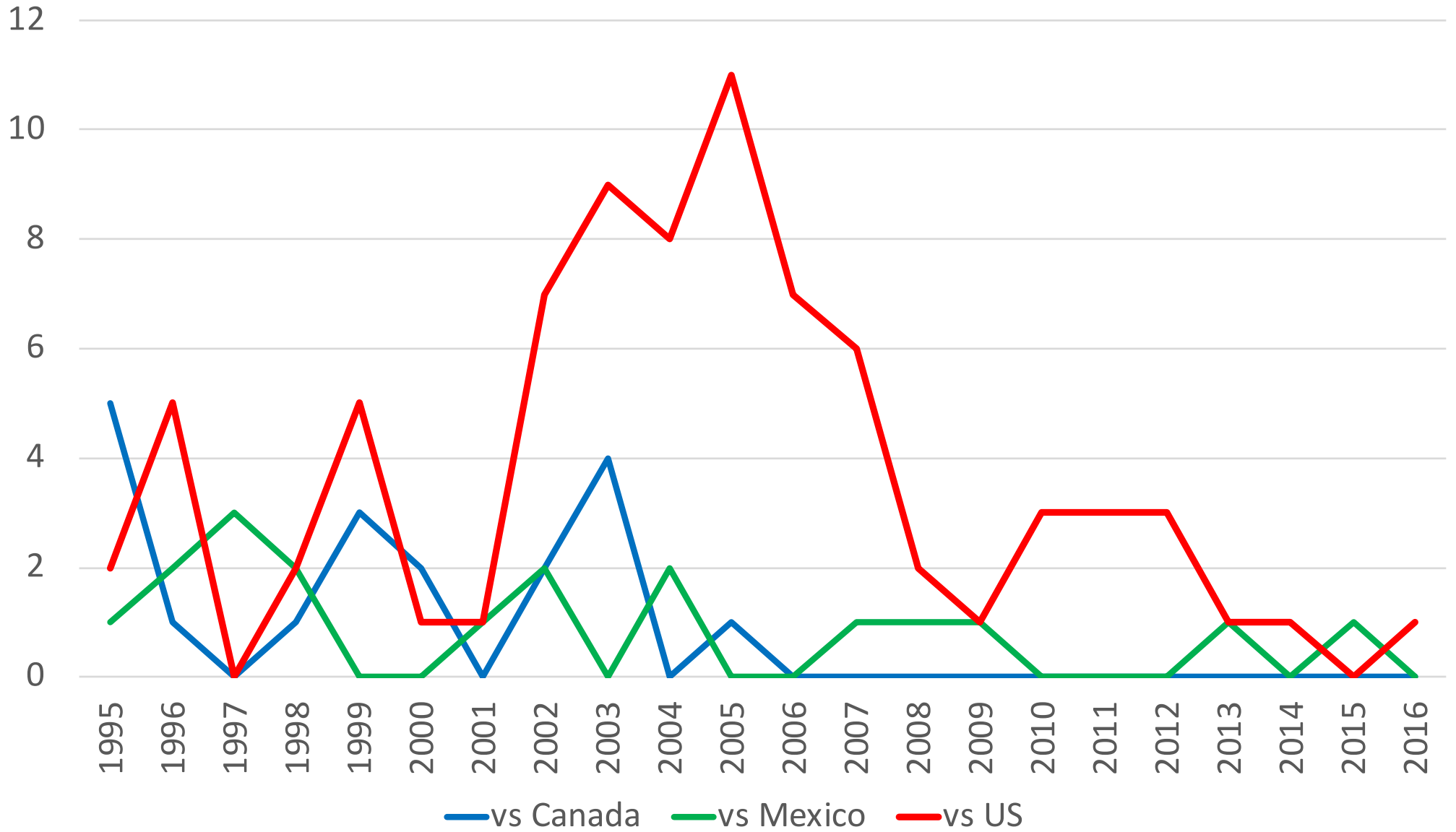
- ISDS = Investor-State Dispute Settlement (Chapter 11 of NAFTA)
  - U.S. has so far never lost an ISDS case
  - Trump seems to want it retained (as do US large corporations)
  - USTR wants to eliminate it (as does the AFL/CIO)
  - Canada & Mexico want to keep it, and may just allow US to “opt out”

# Issues in More Detail

- Chapter 19
  - This now allows NAFTA countries an appeal against AD & CVD actions
  - Canada insists on keeping it
  - US wants it removed
  - You can see why from the data below



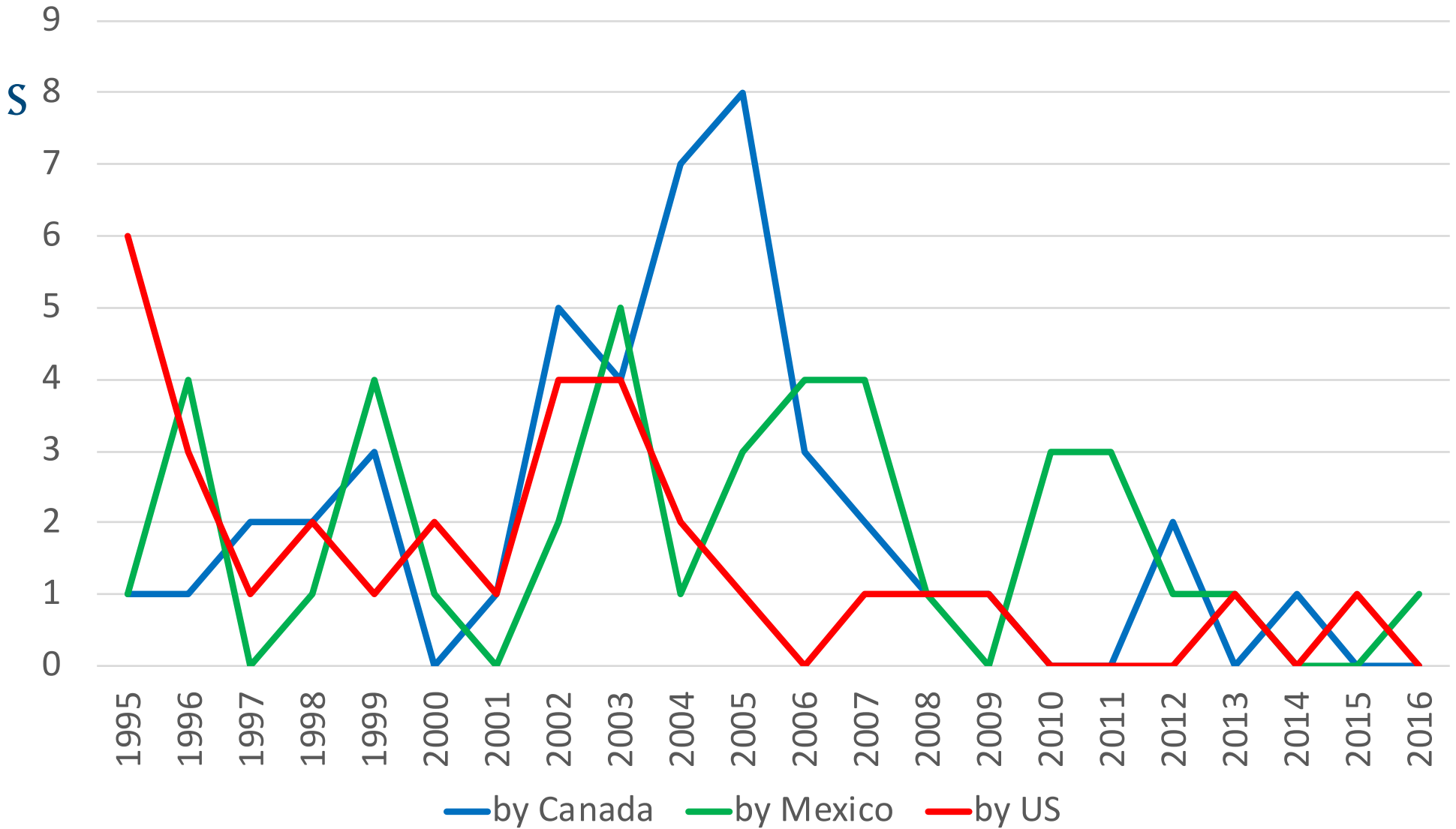
# Targets of Chapter 19



— vs Canada — vs Mexico — vs US



# Users of Chapter 19



# Issues in More Detail

- Dairy & poultry
  - Canada wants to keep its “supply management system for dairy and poultry”
    - Supply management allows farmers to act collectively to manage supply and price
  - Canada has a 270% tariff on dairy imports (with a small quota tariff-free)
  - This was exempted from liberalization in NAFTA

# Issues in More Detail

- Sunset Clause
  - US wants the renegotiated NAFTA to expire after some period (5 years)
  - To be renewed only with another renegotiation
  - This would undermine its usefulness to investors, which may be the point



# Outline

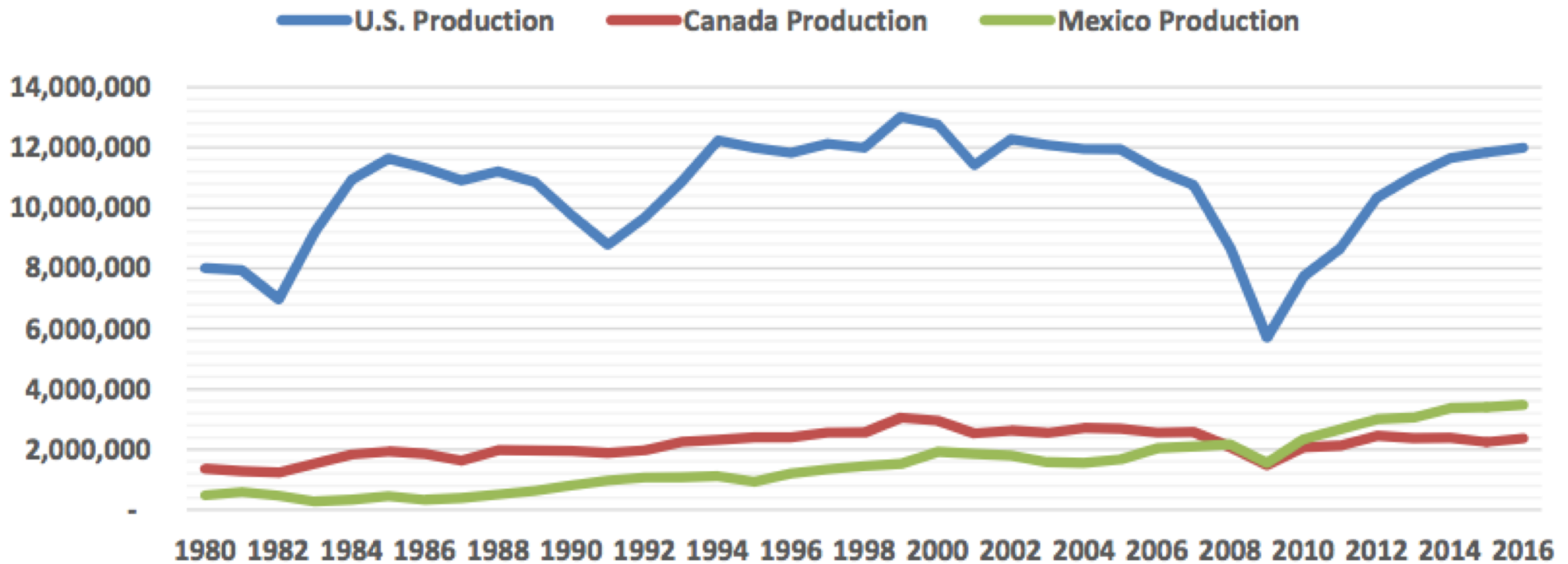
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# NAFTA and the Auto Sector

- Effects of NAFTA
  - Supply chains extended across NAFTA countries
    - True in much of manufacturing, but especially in autos
  - Producers became more competitive with producers outside NAFTA
  - Some plants closed or moved, and US jobs were lost

# NAFTA and the Auto Sector

Figure 1: U.S., Canada, and Mexico Light Vehicle Production: 1980-2016



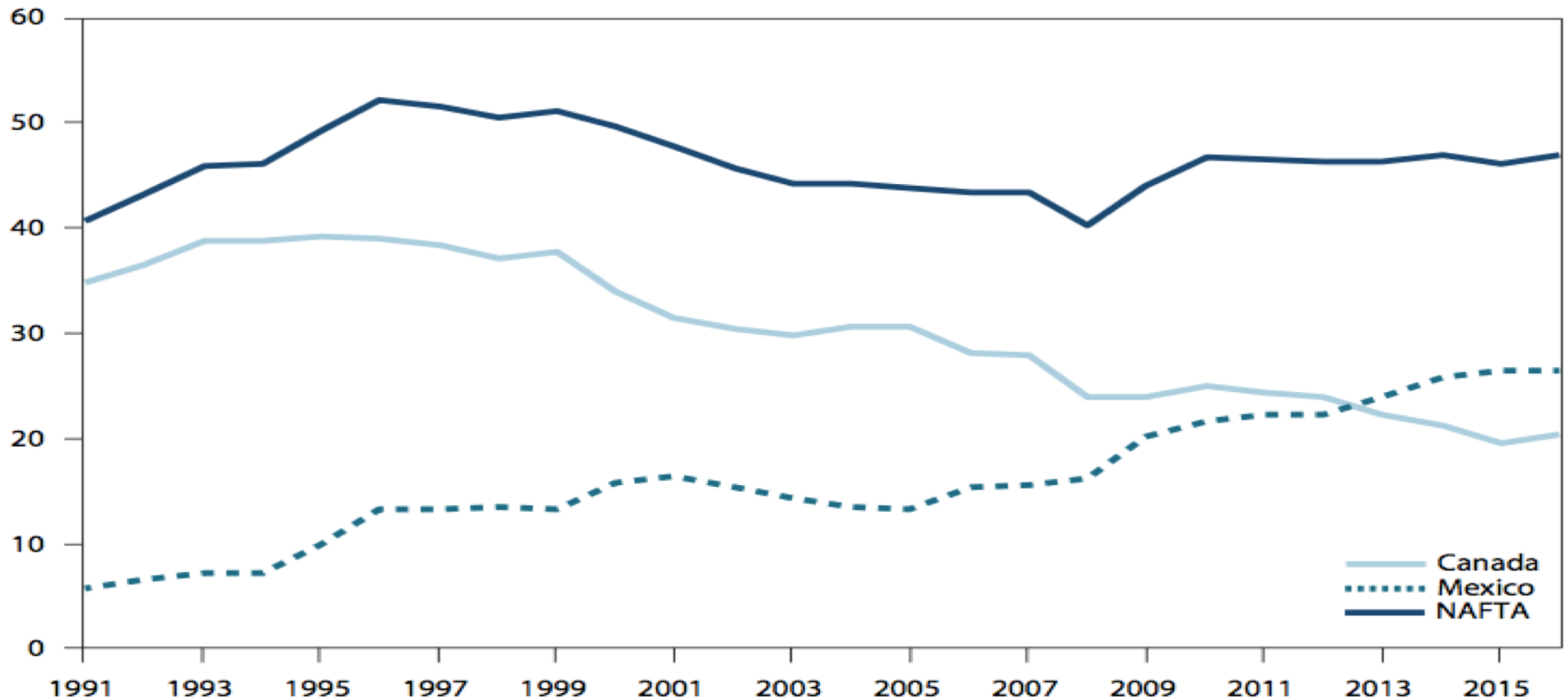
Source: Ward's Automotive

From: CAR, "NAFTA Briefing," January 2017

# NAFTA and the Auto Sector

**Figure 6** Share of US imports in the transport sector, by country

import share

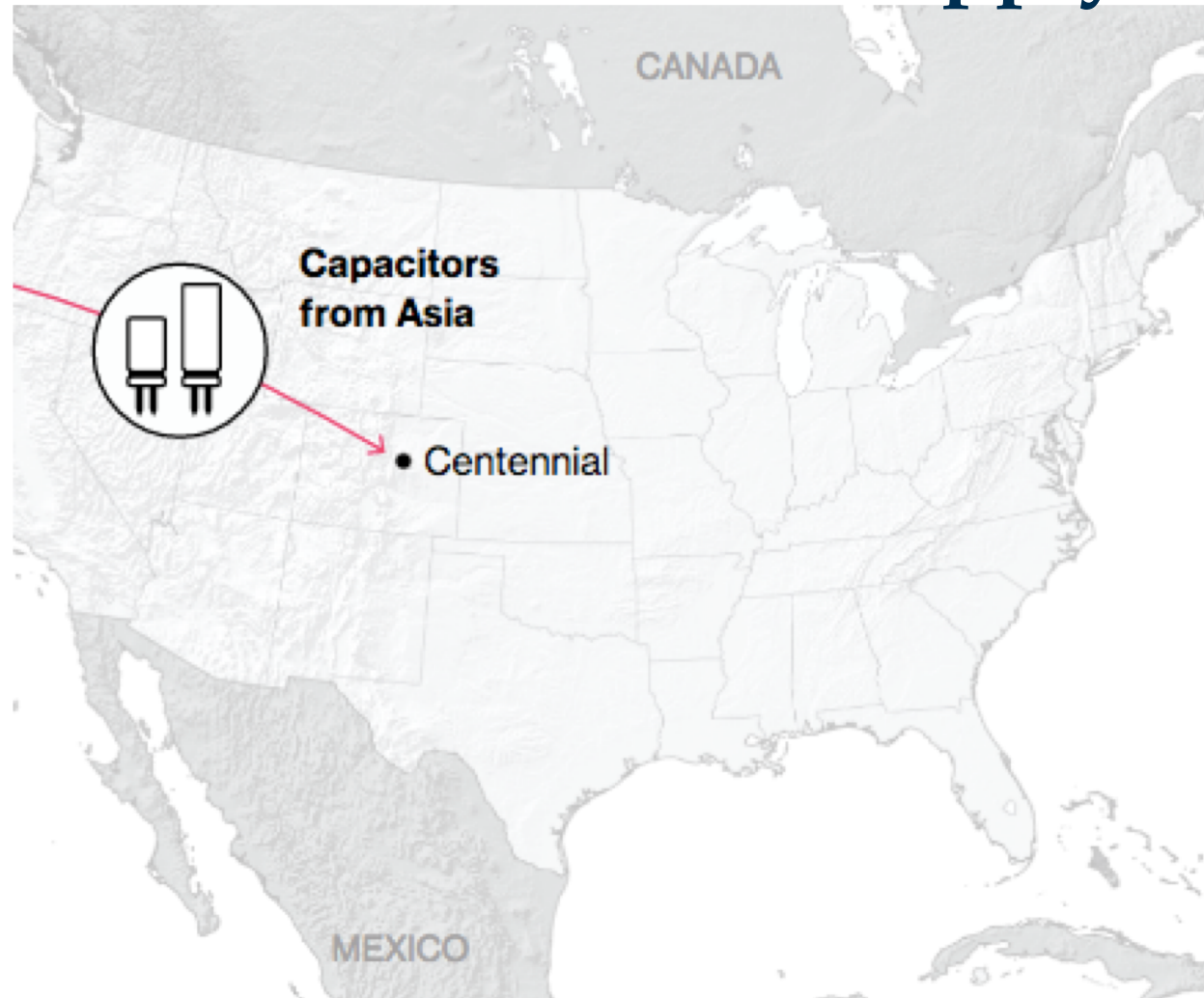


NAFTA = North American Free Trade Agreement

Sources: World Bank, World Integrated Trade Solution, and author's calculations.

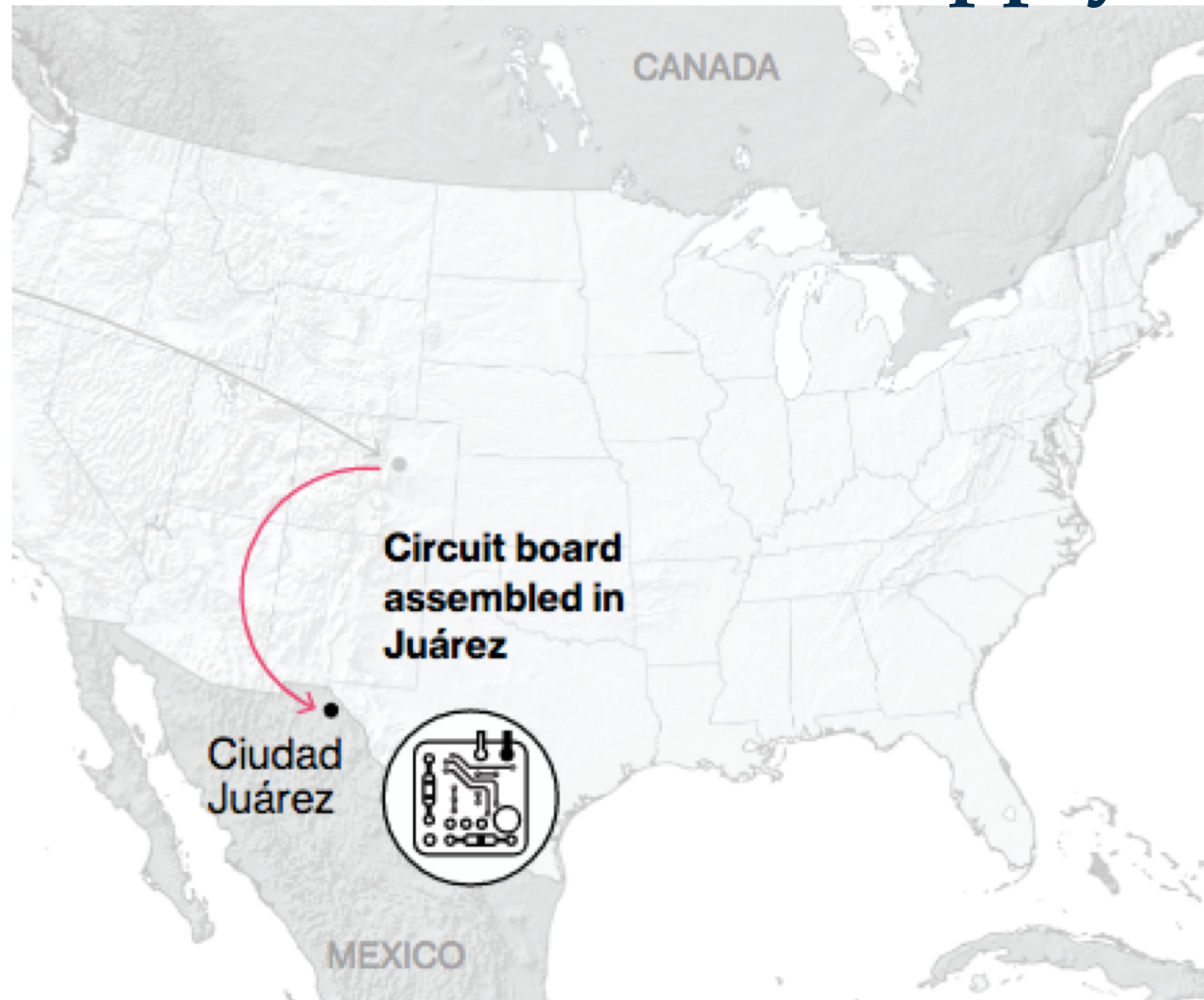
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# NAFTA and the Auto Supply Chain



Black, Diamond, and Merrill, "One Tiny Widget's Dizzying Journey Shows Just How Critical Nafta Has Become," *Bloomberg*, February 2, 2017.

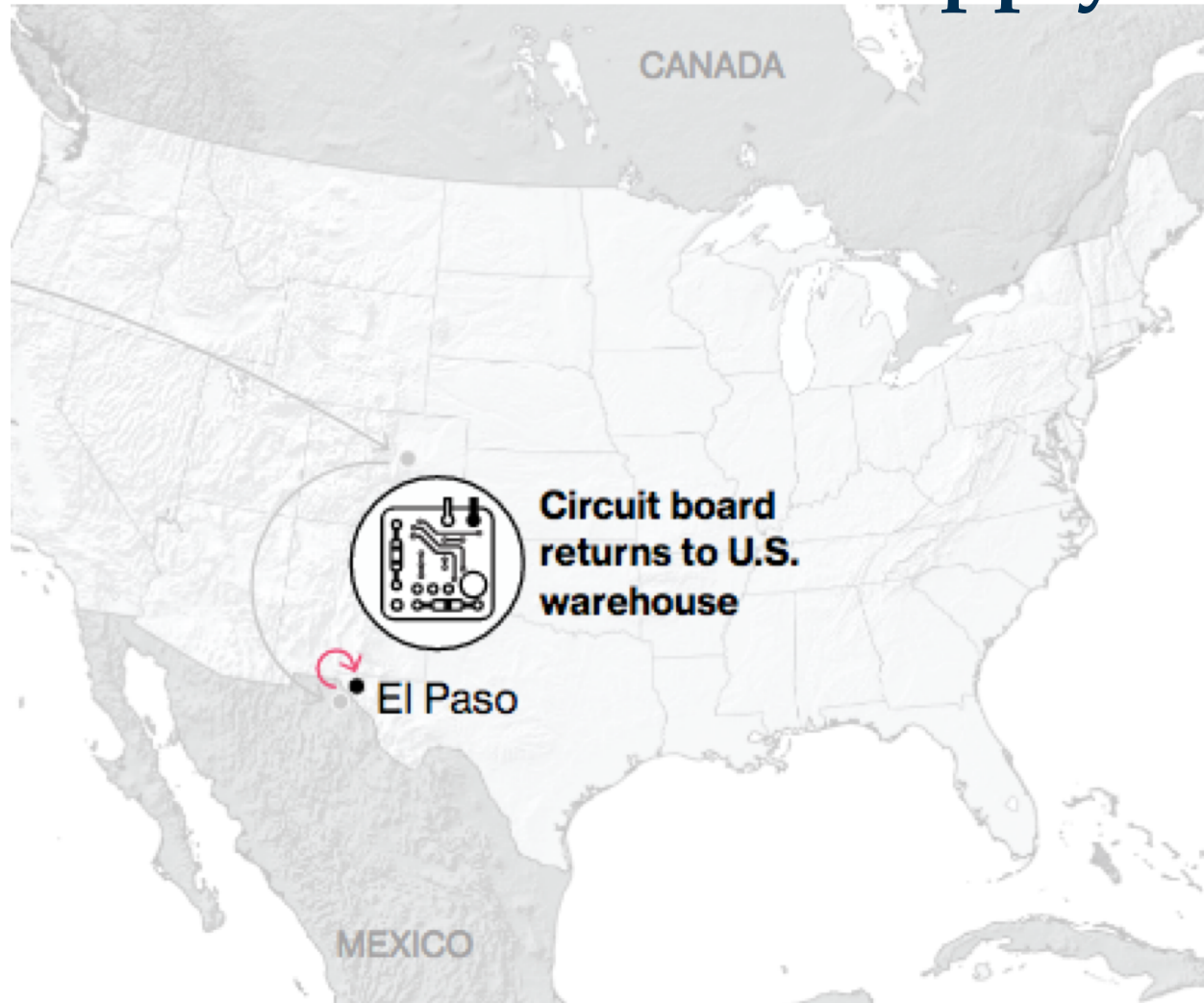
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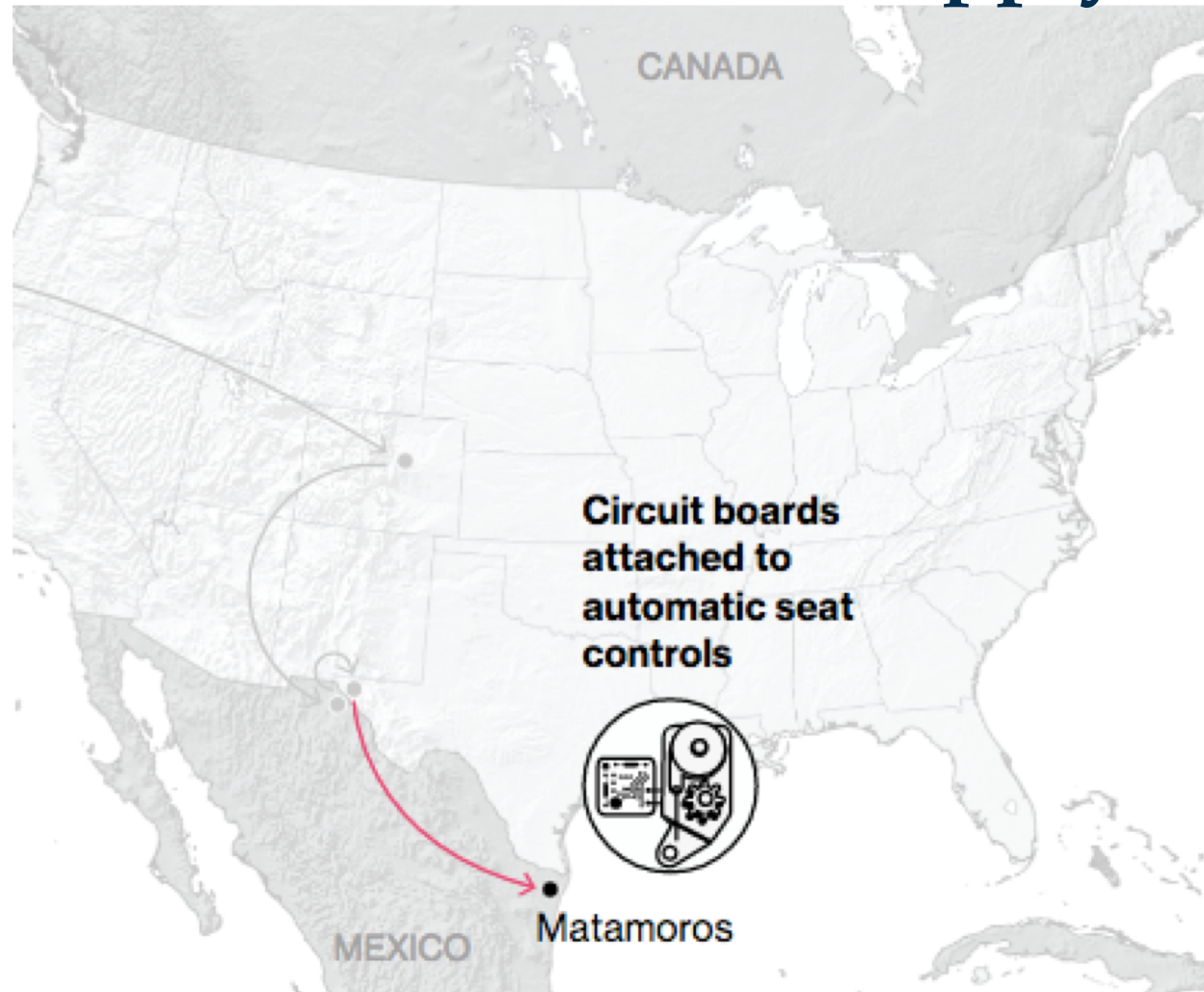


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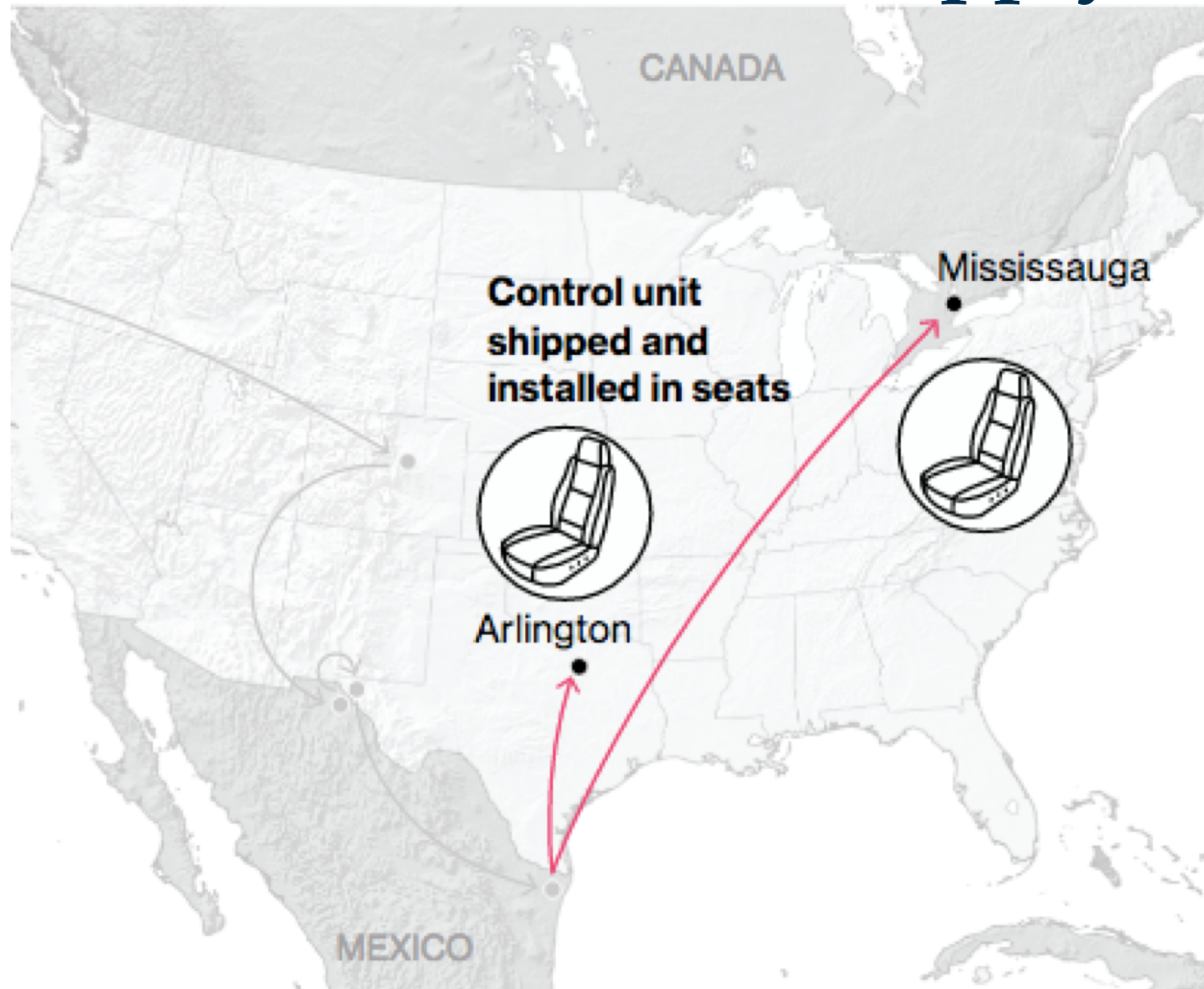
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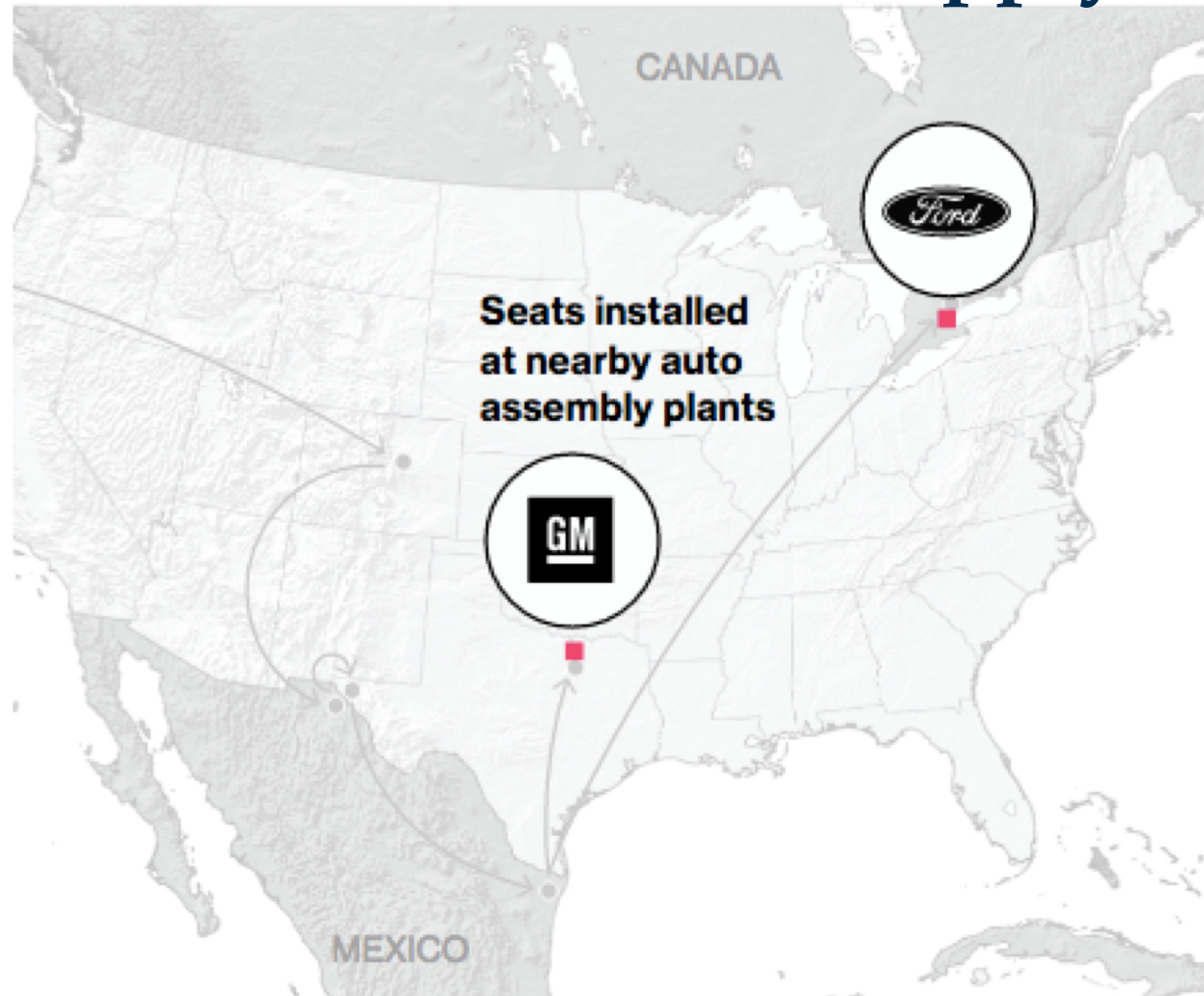


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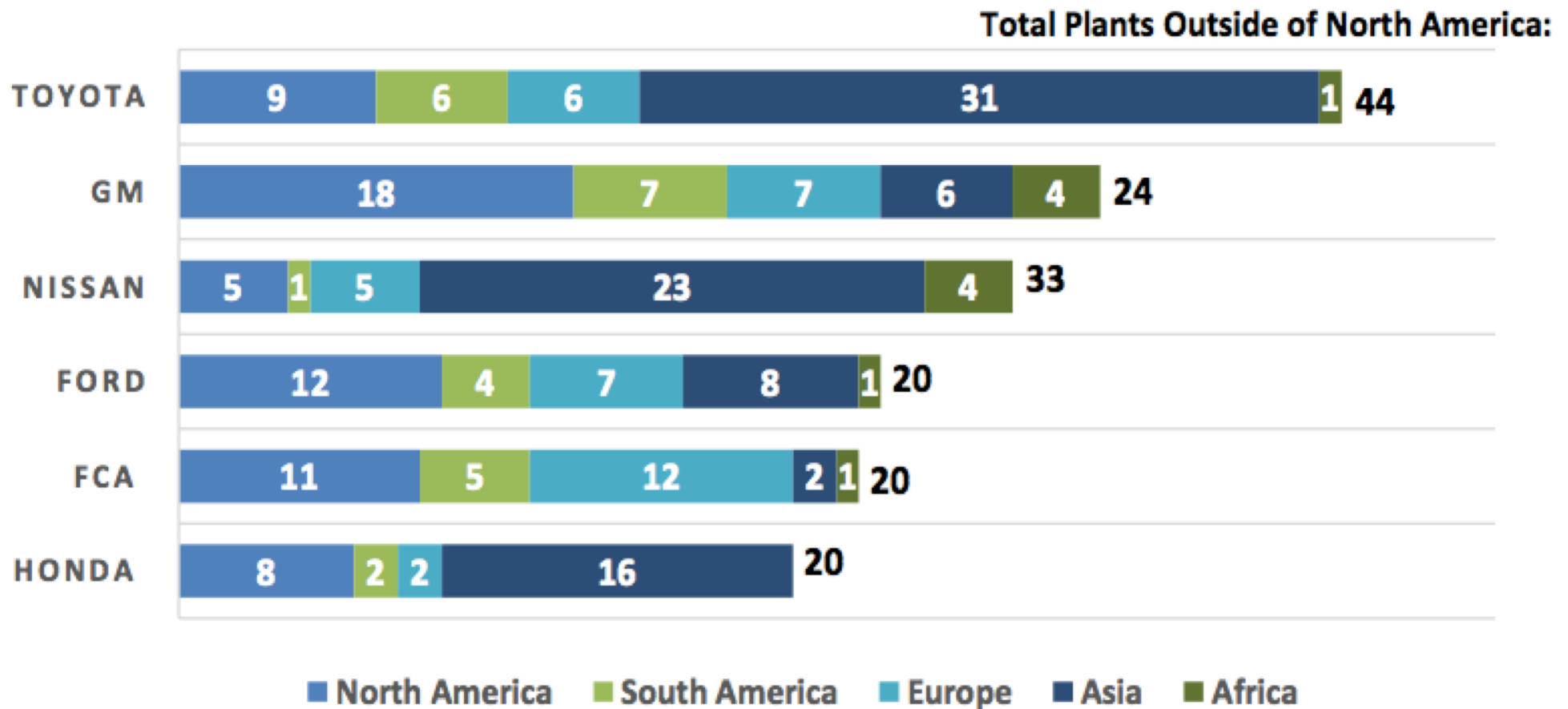
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# NAFTA and the Auto Sector

Figure 2: Global Locations of Top Six Automakers by Region, 2016

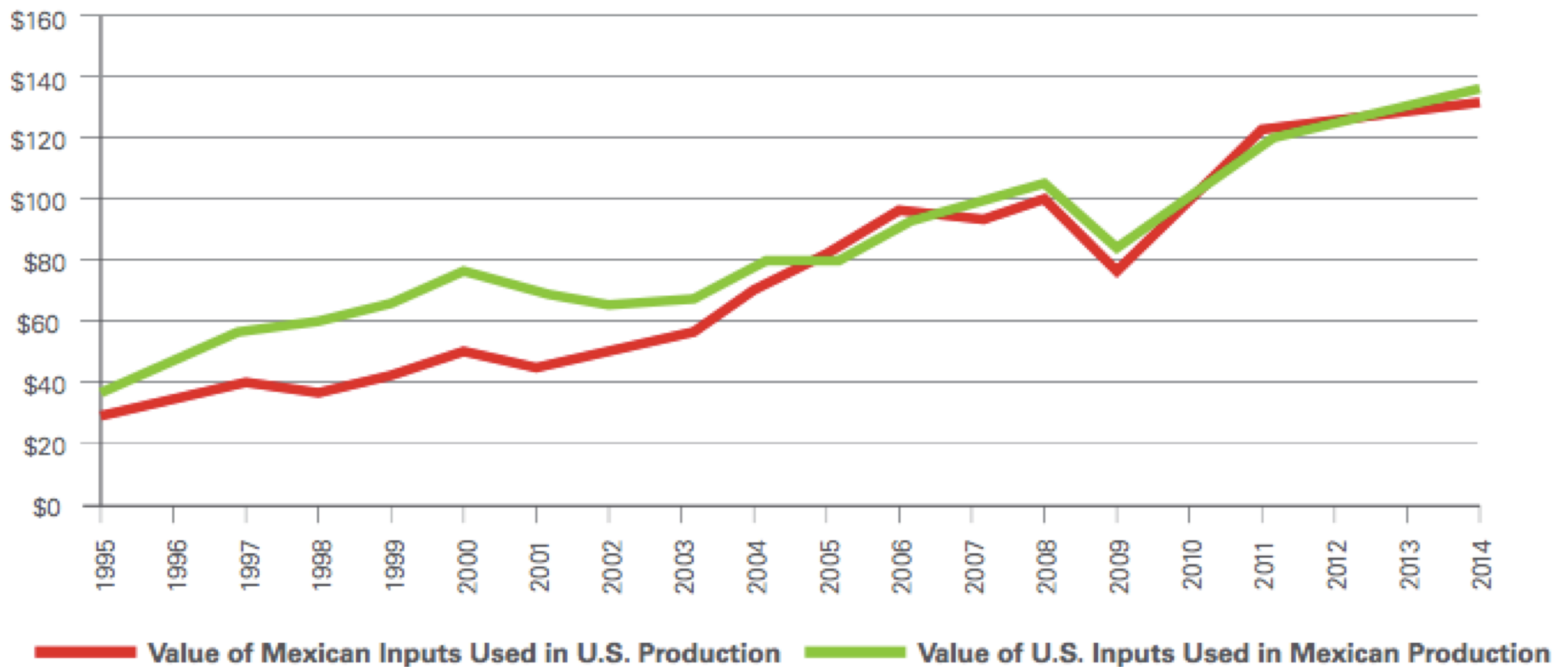


Source: Ward's Automotive

From: CAR, "NAFTA Briefing," January 2017

# NAFTA and Supply Chains

**Figure 2.** Value of Foreign Inputs for Domestic Production, Billions of USD (1995-2014)



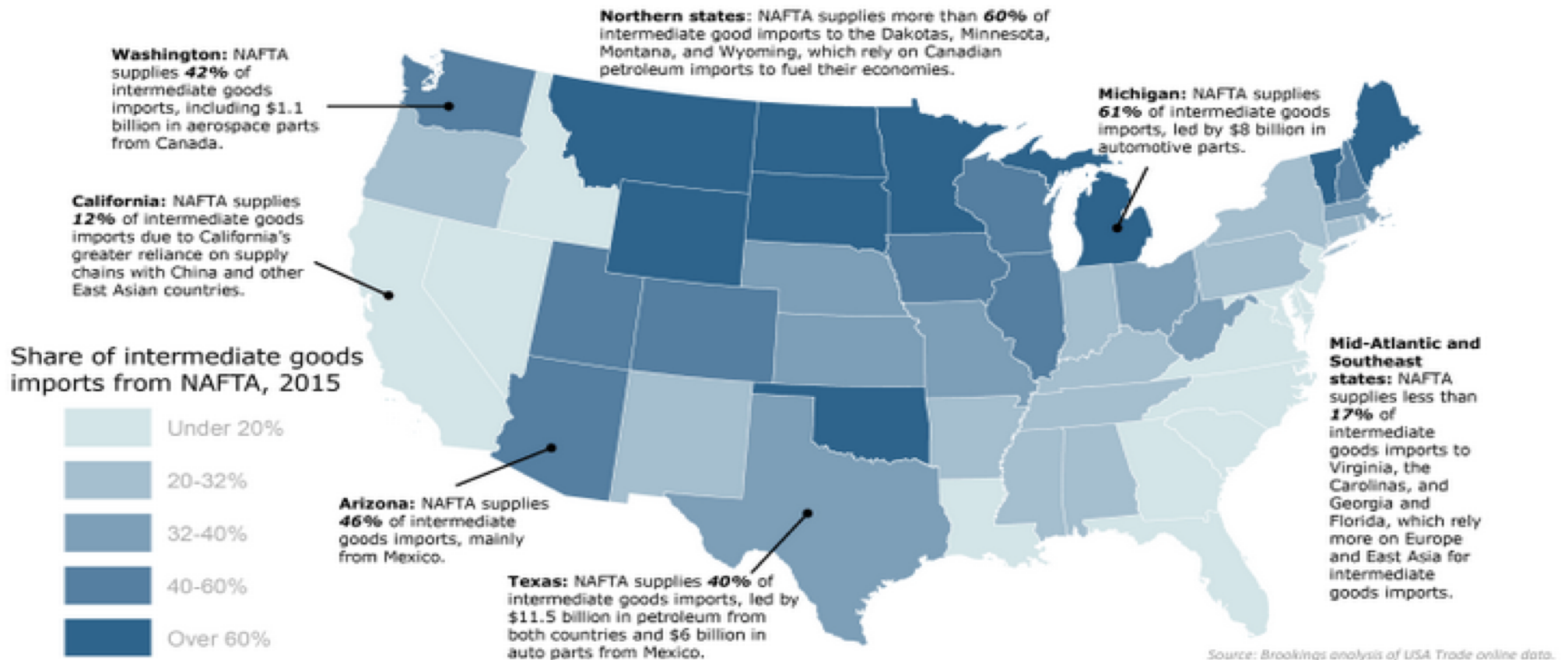
From: Wilson, Christopher, *Growing Together: Economic Ties between the United States and Mexico*, Wilson Center, March 2017.

# NAFTA and Supply Chains

## North American Production Platform

Half of U.S. imports from Canada and Mexico are intermediate goods that are then used in local production, a much higher share than for the European Union or China. From energy to autos, trade policy debates must recognize the unique reliance in many states on the North American supply chain.

 Metropolitan Policy Program  
at BROOKINGS



From: Parilla, Joseph, "How US states rely on the NAFTA supply chain," *The Avenue*, blog, Brookings, March 30, 2017.



# NAFTA and Supply Chains



From: Parilla, Joseph, "How US states rely on the NAFTA supply chain," *The Avenue*, blog, Brookings, March 30, 2017.

# NAFTA and the Auto Sector

- Effects of NAFTA Renegotiation or Failure
  - Tightening of Rules of Origin
  - Returning to MFN tariffs
  - Inputs that now cross borders will become subject to tariffs
  - Along supply chains, tariffs will be levied on tariffs
  - Some inputs will be re-sourced to within NAFTA or US, at higher prices
  - Others will be re-sourced to Asia/Europe, also at higher prices, as tariff preference is lost or foregone

# NAFTA and the Auto Sector

- Effects of NAFTA Renegotiation or Failure
  - All options raise costs
    - Reducing consumer welfare (higher prices for cars)
    - Reducing US producers' competitiveness with producers outside NAFTA
    - Some producers may, eventually, relocate outside NAFTA
  - Some options increase employment in US, others reduce it
  - Trade imbalance
    - with Mexico likely falls, but
    - with rest of world will likely rise



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# Renegotiation Prospects

- US has included demands that some say are “poison pills”
  - Demands that they know others cannot accept
  - Is the purpose to get a better outcome (as they view it) for US?
  - Or is the purpose to justify later pulling out of NAFTA?

# Renegotiation Prospects

- US is most eager to complete a deal before
  - TPA (Trade Promotion Authority = “Fast Track”) expires (not likely to expire)
  - Mexico’s presidential election, July 1, 2018
  - US midterm election season heats up

# Renegotiation Prospects

- Canada and Mexico have added incentive to agree:
  - Returning to prior tariffs will hurt them more than US
  - Trump exempted them from his metals tariffs conditional on NAFTA agreement
    - 25% on steel
    - 10% on aluminum
      - Canada is largest aluminum supplier to US and 2<sup>nd</sup> largest of steel after EU
      - Mexico is 4th largest supplier of steel

# Renegotiation Prospects

- Renegotiation was briefly complicated by Trump's stated desire to re-enter TPP, but that changed
- If deal is reached, will Trump approve?
- If not, will he pull out of NAFTA completely?