

You're Fired! - Why Not Negotiate a NAFTA Alternative?

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Contentious political divisions over the macroeconomic impact of the North American Free Trade Agreement (NAFTA) on trade unions, labor, productivity, and capital shares have sharply juxtaposed free trade's "winners" and "losers." Calling NAFTA a "free trade agreement" (FTA) is highly misleading to the public, as many of the most harmful elements of the agreement are the non-trade aspects, such as labor standards, investor-state dispute mechanisms, environmental and safety regulations. NAFTA must be renegotiated in the interest of protecting sensitive trade industries while retaining the surplus value added within each member's domestic economy. This can be done through renegotiating NAFTA into a plurality of industry-specific selective trade agreements.

This article covers NAFTA member's historical positions, their current positions in the NAFTA 2.0 negotiations and examines the possible negotiating scenarios as proposed by the *Peterson Institute for International Economics*, which could affect the outcome of the renegotiations. COHA has proposed policies to improve NAFTA, which can be enacted by following a selective trade liberalization model such as the Canada-U.S. Auto Pact.

There are many challenges to renegotiate NAFTA as a fair trade agreement. For instance, the growing necessity of Mexico and Canada to gain an upper-hand in the upcoming negotiations, not to be denied an adequate trade deal, is being sabotaged by the mainstream media's inadequate coverage of NAFTA's non-trade elements. Many of NAFTA's non-trade elements have been shoehorned into the agreement, such as Chapter 11 Investor State Dispute Settlement (ISDS).ⁱ Chapter 11 allows for the protection of investor rights, in which investors can receive monetary reward from a NAFTA government that has violated investors' rights. Chapter 11 ISDS is contentious because it solves such disputes by a trade tribunal and not through due-process of national courts. For example, the Canadian Broadcast Corporation (CBC) seems too preoccupied with covering the NAFTA renegotiations as "apocalyptic economic suicide." Meanwhile, Justin Trudeau frantically runs around gaining support from state governors to maintain NAFTA in its current form.ⁱⁱ This narrative is misleading, as it portrays NAFTA as Canada's economic life-support, which is far from the truth.

Realistically, if NAFTA was terminated tomorrow it would only affect 1.47 percent of Canada's total exports to the United States.ⁱⁱⁱ As well, NAFTA has only had a small impact on the United States economy, as total trade with Mexico and Canada accounts for less than 5 percent of U.S. GDP at the time the agreement was ratified.^{iv} It was also predicted that NAFTA would only have a 0.1 to 0.5 percent increase in U.S. GDP upon full implementation.^v This suggests that NAFTA is surely more than just free trade; it is a set of legal rules that aim at increasing corporate profits at the expense of American, Canadian, and Mexican citizens. Therefore, a NAFTA alternative is necessary to retain the benefits of trade, but reject the corporatist nature of NAFTA 2.0.

American, Canadian, and Mexican Perspectives on 1990's NAFTA Negotiations

In the face of a hostile U.S administration, characterized by the "twitter-diplomacy" of President Donald Trump, it is easy to forget the strategic grassroots organization throughout the 1990s and early 2000s in North America that fiercely opposed the idea of having further economic integration with the United States, which has been primarily dictated by corporate special interests. One of the U.S. trade officers who was negotiating industry-specific business concerns in NAFTA commented on the negotiating process of the U.S. Sectoral Advisory Committee (SAC) as "When you let a dog piss all over a fire hydrant, he thinks he owns it... [the executive branch] carried the hydrants to the dogs."^{vi} This is in reference to the power corporate lobbyist had over NAFTA's legislation and the executive branch of the United States government during the original NAFTA negotiations. It is important to remember that during the ratification of NAFTA the Clinton administration made many side concessions to individual congressman who originally opposed the NAFTA deal, in order to build stronger bi-partisan support for the trade agreement.

Meanwhile, in Canada the Liberal opposition in 1989 fiercely opposed the NAFTA idea on economic grounds. However, as soon as the Liberals, led by Jean Chretien, won the 1993 federal election they made a u-turn on their opposition to NAFTA, bustling full speed ahead with ratifying the agreement.

In Mexico, under the Partido Revolucionario Institucional (PRI) President Carlos Salinas de Gortari's strong influence among the executive, legislative, and federal government officials - along with the ironclad control over the trade union federation Confederación de Trabajadores de Mexico - suppressed all possible resistance from the indigenous or independent labor alliances within Mexico's legislature.

On January 1, 1994, NAFTA was cheerfully celebrated by the business elites in North America, signifying a movement towards further trade liberalization and reducing non-trade barriers in favor of capital gains.^{vii} Upon signing NAFTA, former President Bill Clinton remarked, "Now we must recognize that the only way for a wealthy nation to

grow richer is to export, to simply find new customers for the products and services it makes.”^{viii} Clinton's remarks of an export-oriented growth model as the only way to grow a nation's wealth is a narrow-minded approach to increasing societal wealth. However, recent anti-FTA sentiments in the United States coupled with unsavory U.S.-Mexico relations, and a naive Canadian government, begs the question: is NAFTA the only policy alternative towards North American economic integration? This is the question that this paper will seek to answer amongst the current NAFTA 2.0 renegotiations.

NAFTA's 2.0 Positions and Future Negotiating Scenarios

The release of Trump's 17-page *Summary of Objectives for the NAFTA Renegotiations* provides a “subpar” America First solution, particularly for Canada and Mexico. Trump's call for tighter North American rules of origin, asymmetrical investor-protection rules, and abolishment of NAFTA's Chapter 19 dispute settlement mechanism is sure to irritate America's closest trading partners.^{ix} Chapter 19 dispute settlement mechanism allows Canadian and Mexican government to go to an independent bi-national panel to work out trade dispute with the United States. As well, the entirety of Trump's negotiating strategy is hypocritical - the executive director of the Sierra Club stated, “Based on today's ‘plan,’ one could be forgiven for concluding that Trump's opposition to the TPP was merely political theater.”^x The Canadian Foreign Affairs Minister, Chrystia Freeland, seems determined to “defend” a Canada-E.U. Comprehensive Economic Trade Agreement (CETA) style NAFTA 2.0, which has eroded Canada's system of supply management, according to NDP MP Tracy Ramsey.^{xi xii} However, Trudeau's so-called “sunny-ways” strategy appears anything but reassuring for Canadians.^{xiii} In Mexico, the Mexican government wants to maintain the benefits gained from NAFTA while at the same time seeking to modernize the agreement – specifically seeking higher labor market integration, free access for goods and services, and energy security.^{xiv}

The first round of negotiations, out of six rounds, started on August 16th in Washington D.C. The *Peterson Institute for International Economics* has outlined four possible scenarios that could play out during the negotiations, given Trump's erratic rhetoric when it comes to trade policy (i.e. his threat to terminate NAFTA on April 27, 2017 followed by his decision to modernize the 23-year-old trade agreement). The first scenario is that Canada and Mexico would capitulate to the U.S. demands; however, this is very unlikely given the “one-sided” nature of Trump's demands. Secondly, the “modernizing” NAFTA approach would mean stronger labor and environmental standards, holding private companies to the same standard as state-owned corporations, and the allowance of free flow of digital services. However, this second scenario is unlikely as this would ruin Trump's protectionist “America First” political ideology. The third scenario is the termination of NAFTA. Although full-out termination

might sound radical, it is entirely within the scope of possibilities given Trump's threats last April. Nonetheless, the third scenario would not be a bad option for Canadians, as the Canadian government would be able to revert to the suspended 1989 Canada-United States Free Trade Agreement (CUSFTA). If Trump refuses to accept a CUSFTA agreement, the Canadian economy would only see modest losses.^{xv} If Trump makes good on his promise to terminate NAFTA, the Mexican economy would see a substantial decline in its foreign direct investment (FDI) - resulting in a decline of the peso. The fourth scenario would be to muddle through the challenges of NAFTA making compromises between the merits of protectionism and liberalization.^{xvi} This outcome seems the most probable, given the Canadian government's naiveté towards Trump's so-called willingness to "negotiate," and the growing hostility between Trump and President Peña Nieto over U.S.-Mexico immigration. Agreeing on compromises when it comes to NAFTA is not new. For example, one of the main reasons the Mulroney government signed onto NAFTA in 1992 was the independent binational nature of the Chapter 19 dispute settlement mechanism, as it allowed some labor protection within NAFTA's dubious set of industry-friendly regulations. According to a *Canadian Report of the Standing Committee on Foreign Affairs and International Trade*, "[the Chapter 19 dispute settlement process] was the bare minimum Canada would accept in negotiations [...] without [it] Canada would not have signed the FTA."^{xvii} It is possible for NAFTA's trading partners to compromise on trade when it is at the benefit of their own special interests; however, when it is at the cost of losing their support from their political base they turn inwards. With the current nature of Trump's foreign relations, it is fair to expect everything and nothing.

COHA's Policy Recommendations

In the meantime, while the "three amigos" are bickering over the NAFTA renegotiations, the *Council on Hemispheric Affairs* has already proposed solutions to progressively "modernize" NAFTA, to protect labor standards, environmental regulation, eliminate corporate friendly provisions and improve overall trading relations between Canada, the United States, and Mexico. On September 13, 2010, the *Council on Hemispheric Affairs* published the article *Negotiating A New NAFTA: What and Why This is Needed*. COHA set out three main objectives to "modernize" NAFTA, all of which are still highly relevant today: i) A new NAFTA (or NNAFTA) should allow governments to enact policies that target discriminatory trade and non-trade practices within a regional free trade agreement; ii) labor and environmental standards must be equitably standardized among Canada, the United States, and Mexico; however, this does not mean harmonization with U.S. regulation. This includes guaranteeing a common living wage, worker safety, and welfare criteria to aid the negative macroeconomic sectoral shifts in the North American economy; iii) Governments must proceed in a negotiating strategy that is fair and equitable to all parties involved.^{xviii}

Given these policy recommendations, determining the benefits of NAFTA is ambiguous, because all partners in the trilateral agreement heavily participate in intra-industry trade, or “production sharing operations.” Production sharing operations occur when value is added to imported products, such as non-processed and semi-processed raw materials, through manufacturing and then exported again to other countries.^{xix} Heavy reliance on intra-industry trade between Canada, Mexico and the United States has resulted in a considerable amount of inflow of foreign domestic investment (FDI), but unfortunately, foreign investment has not been retained in the respective countries. Most of the surplus value added to the goods are exported and re-sold internationally. The effects of production sharing operations are most heavily felt in Mexico, as their exploitative special exporting process zones (or EPZs) keep little foreign investment within the domestic economy, as goods produced within EPZs are exported from Mexico after being processed. In Canada there has been a substantial increase in FDI because of NAFTA, but Canada’s total share of North American FDI has declined because of the increasing outflow of FDI to the rest of North America. Similarly, the U.S. economy has suffered under NAFTA. The United States now imports more than it exports to NAFTA partners as a result of major shifts in the U.S. economy from a manufacturing-based economy to a service-based economy. In addition, Clinton’s Trade Adjustment Assistance (TAA) program, intended to aid laborers affected by NAFTA, has provided little assistance to a disenfranchised American populace. On all sides of the bargaining table, the governments of the United States, Mexico, and Canada should be optimistic about “modernizing” a less than adequate NAFTA agreement. However, Canadian and Mexican officials must stand strong against a less than adequate Trump administration. Despite the chance for compromises to be made at the upcoming negotiations, it may be worth the costs incurred to terminate NAFTA and revert to selective trade liberalization.

Canada-U.S. Auto Pact 1965: Selective Trade Liberalization, A NAFTA Policy Alternative?

The Canada-U.S. Auto Pact of 1965 is a good example of how protected intra-industry trade can benefit each trading partner. The Canada-U.S. Auto Pact was “designed to permit North American (primarily U.S. multinational) producers to rationalize production facilities” by removing U.S. and Canadian tariffs on trans-border shipment of vehicles and equipment parts.^{xx} For producers to participate in the Auto Pact, manufactures had to achieve a minimum level of status of origin, which required 50 percent of the product to be manufactured in either the U.S. or Canada. In addition, for the product to qualify for duty-free preferential treatment, manufactures had to maintain a ratio between the net sales of vehicles made in Canada and the net sales of vehicles sold in Canada. This was in addition to trade regulation, which required that the value added to vehicles must be maintained at (or above) the level of origin in the base year (1964).^{xxi} In contrast to the deregulatory nature of NAFTA, such regulatory

requirements ensured that manufacturing in both countries was maintained at a certain level. Although it may seem unrealistic, it is in the best interest of Canada, Mexico, and the United States to revert to bilateral selective trade liberalization agreements, which primarily aim to protect sensitive trade industries while at the same time retaining an inflow of FDI within the domestic economy, by limiting the ability for manufacturers to exploit the surplus value gained through domestic manufacturing. A 1986 *National Bureau of Economic Research Working Paper No. 1953* found that “Canada-U.S. Auto Pact selective trade liberalization provisions did not substantially improve the efficiency of Canadian automobile production relative to U.S. production,”^{xxii} as it only improved Canadian automotive efficiency by 3 percent between 1970 and 1979.^{xxiii} The Canadian and American automotive industry was oligopolistic, which has restricted the ability for manufacturers to achieve the highest possible efficiency from the Canada-U.S. Auto Pact. In 2001 the Auto Pact was determined to be illegal by the World Trade Organization, but by then NAFTA had effectively replaced previous free trade agreements.

Conclusion

Despite the failure of the Auto Pact to reach its full potential, selective trade liberalization agreements should be advocated as a means of replacing NAFTA. It is necessary for NAFTA members to tread lightly in the upcoming negotiations not to inflict further damage upon the North American economy while considering policy alternatives.

If selective trade liberalization agreements were to replace NAFTA - in the event Trump terminates NAFTA - it would be necessary for each respective industry to critically examine the macroeconomic costs and benefits, and be transparent with employees, of the impact of free trade on unemployment before Canada, the United States and Mexico collude into any further negotiations. There is no doubt that there are macroeconomic benefits to gain from David Ricardo’s trade theory of comparative advantage, but to truly reap the benefits from international trade, it is necessary to examine all the variables at play. Either way, NAFTA renegotiations are going to bring about change for the better, or for the worse.

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ⁱ “NAFTA’s Chapter 11: Corporate Cases,” *Public Citizen*, 2017, <https://www.citizen.org/our-work/globalization-and-trade/naftas-chapter-11-corporate-cases>. NAFTA Chapter 11: “If a company believes that a NAFTA government has violated these new investor rights and protections, it can initiate a binding dispute resolution process for monetary damages before a trade tribunal, offering none of the basic due process or openness guarantees afforded in national courts.”

ⁱⁱ Katie Simpson, “Liberals to step up NAFTA charm offensive in Washington come September,” *CBC*, August 3, 2017, <http://www.cbc.ca/news/politics/liberals-nafta-washington-us-trade-renegotiations-1.4232349>.

ⁱⁱⁱ Scott Sinclair, Pierre Laliberte, “What is the NAFTA advantage?” *Canadian Centre for Policy Alternatives*, June 2017, https://www.policyalternatives.ca/sites/default/files/uploads/publications/National%20Office/2017/06/What_is_NAFTA_Advantage.pdf.

^{iv} Angeles Villarreal, Ian F. Fergusson, “The North American Free Trade Agreement (NAFTA),” *Congressional Research Service*, May 24, 2017, <https://fas.org/sgp/crs/row/R42965.pdf>.

^v Ibid.

^{vi} Laura Macdonald, Mildred A. Schwartz, “Political Parties and NGOs in the Creation of New Trading Blocs in the Americas,” *International Political Science Review*, April, 2002, Vol. 23(2), p. 135-158.

^{vii} Bob Herbert, “In America; Nafta And the Elite,” *The New York Times*, November 10, 1993, <http://www.nytimes.com/1993/11/10/opinion/in-america-nafta-and-the-elite.html>.

^{viii} “December 8, 1993: Remarks on the Signing of NAFTA,” *Miller Center*, 2017, <https://millercenter.org/the-presidency/presidential-speeches/december-8-1993-remarks-signing-nafta>.

^{ix} Gary Clyde Hufbauer, Euijin Jung, “Scenarios for Concluding the NAFTA Talks,” *Peterson Institute for International Economics*, July 24, 2017, <https://piie.com/blogs/trade-investment-policy-watch/scenarios-concluding-nafta-talks>.

^x Pete Dolack, “Trump’s Re-negotiation Proposal Will Make NAFTA Worse,” *counterpunch*, July 26, 2017, <https://www.counterpunch.org/2017/07/26/trumps-re-negotiation-proposal-will-make-nafta-worse/>.

^{xi} “Canada’s goals for ‘progressive’ NAFTA include labour and environmental standards, gender equality,” *Canadian Broadcasting Corporation (CBC)*, August 14, 2017, <http://www.cbc.ca/news/politics/nafta-negotiations-freeland-canada-goals-1.4246141>.

^{xii} Supply management, or government procurement, is the way in which governments source raw materials for the production of goods.

^{xiii} “Justin Trudeau’s ‘sunny ways’ a nod to Sir Wilfrid Laurier,” *Canadian Broadcasting Corporation (CBC)*, October 20, 2015, <http://www.cbc.ca/news/canada/nova-scotia/ns-prof-trudeau-sunny-ways-1.3280693>. “Sunny Ways” is in reference to Justin Trudeau’s 2015 election victory speech, which he made reference to Sir Wilfrid Laurier speech to build unity over French Catholic Schools disputes in Manitoba in the late 1800’s.

^{xiv} Gabriel Stargardter, “Mexico sets out NAFTA goals ahead of re-negotiation talk: document,” *Reuters*, August 1, 2017, <https://www.reuters.com/article/us-usa-trade-mexico-idUSKBN1AH4VW>.

^{xv} Scott Sinclair, Pierre Laliberte, “What is the NAFTA advantage?” *Canadian Centre for Policy Alternatives*, June 2017, https://www.policyalternatives.ca/sites/default/files/uploads/publications/National%20Office/2017/06/What_is_NAFTA_Advantage.pdf.

^{xvi} Gary Clyde Hufbauer, Euijin Jung, “Scenarios for Concluding the NAFTA Talks,” *Peterson Institute for International Economics*, July 24, 2017, <https://piie.com/blogs/trade-investment-policy-watch/scenarios-concluding-nafta-talks>

^{xvii} "Dispute Settlement in the NAFTA: Fixing an Agreement Under Siege," *Report of the Standing Committee on Foreign Affairs and International Trade*, May 2005, <http://www.ourcommons.ca/DocumentViewer/en/38-1/FAAE/report-9/>

^{xviii} "Negotiating A New NAFTA: What and Why This is Needed," *Council on Hemispheric Affairs*, September 13, 2010, <http://www.coha.org/negotiating-a-new-nafta-what-and-why-this-is-needed/>.

^{xix} Ibid.

^{xx} Melvyn Fuss, Leonard Waverman, "The Canada-U.S. Auto Pact of 1965: An Experiment in Selective Trade Liberalization," *National Bureau of Economic Research*, June 1986, <http://www.nber.org/papers/w1953.pdf>.

^{xxi} Ibid.

^{xxii} Ibid.

^{xxiii} Ibid.