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NAFTA, CETA and the TPP – Significant challenges and opportunities

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Canadian companies that engage in cross-border trade and investments in the United States and internationally should pay close attention to the unprecedented and drastic changes in the international trade landscape that have taken place over the past year, as they will likely have a profound impact on their business strategies. These include the renegotiation of the North American Free Trade Agreement (NAFTA), the implementation of the Canada-European Union Comprehensive Economic and Trade Agreement (CETA) and the potential revival of the Trans-Pacific Partnership (TPP) among 11 countries (TPP-11) excluding the United States.

Success of NAFTA renegotiations is uncertain

Canadian businesses engaged in cross-border trade likely spent much of the latter half of 2017 watching the NAFTA renegotiations, which are now well under way between Canada, the U.S. and Mexico. Both Canadaand the U.S. revealed their core objectives for renegotiations over the summer. There were some obvious differences in the objectives, most notably in the areas of government procurement as well as trade remedies where, for example, Canada opposed, and continues to oppose, the U.S. proposal to eliminate the Chapter 19review of domestic anti-dumping and countervailing duty decisions.

The first round of negotiations took place in Washington in August and since then four additional rounds of negotiations have taken place, with the fifth round of talks ending on November 21. The last two rounds have resulted in a stalemate with few indications that the final two rounds will provide the basis for the emergence of a modernized NAFTA.

At the end of the fourth round of negotiations, both the Canadian and Mexican officials rebuked the U.S. administration for its negotiating approach. These officials accused the U.S. of trying to “turn back the clock 23 years” by seeking to claw back so-called “unfair advantages” provided to Canada and Mexico in the negotiations leading to the finalized NAFTA. The Canadian and Mexican negotiators took issue with U.S. proposals, such as a sunset clause that would lead to the expiry of NAFTA in five years unless renewal was agreed to by the parties, the elimination of Chapter 19, restrictions on Canadian and Mexican businesses looking to participate in U.S. government procurement and a requirement that automobiles subject to NAFTA have a 50% U.S. value content. At the end of the fourth round, the ambitious goal of finalizing the renegotiated and modernized NAFTA before the year-end was abandoned.

The fifth round saw no major breakthroughs. In fact, U.S. officials argued that Canada was not properly engaging in the talks, refusing to submit counter-proposals to the U.S. proposals. Canadian officials responded, stating that they were advocating for a “facts-based” approach to get a better understanding of the U.S. proposals.

As negotiations proceed, it is clear that any revised NAFTA emerging from these renegotiations will have a profound impact on Canadian companies and on investors with ties to cross-border trade between Canada, Mexico and the U.S. Should the agreement be successfully renegotiated, it is likely that some of the more contentious U.S. proposals, including those discussed above, will be included in some form. However, if renegotiations fail or look to be failing, U.S. President Donald Trump may file notice of the U.S. withdrawal from NAFTA. Though it is unlikely that the President can withdraw from the agreement in its entirety without approval from Congress, President Trump may be able to increase tariffs without Congressional approval, allowing him to force imports from Canada and Mexico to be subject to customs duties while Congress debates a potential withdrawal from NAFTA.

The uncertainty in relation to whether NAFTA will survive, and in what form it will be in should it survive, should serve as a catalyst for Canadian companies to diversify their trade ties, with greater emphasis placed on trade with Europe and Asia. This year saw significant developments in trade with both of these regions.

CETA grants greater market access to the EU for Canadian companies

CETA, which came into force provisionally on September 21, 2017, grants Canadian businesses much greater access to the European Union (EU), the largest single consumer market in the world.

CETA's greatest impact will be on existing tariff levels between Canada and the EU, with 99% of these tariffs ultimately being eliminated by the agreement. This includes tariff reductions related to major sectors of the Canadian economy. For example, tariffs on oil and gas imports into the EU were as high as 8%, and now have been eliminated. Similarly, tariffs of up to 4.5% on automotive parts, 11-25% on fish and seafood and up to 10% on both forestry and metal products have all been eliminated under CETA.

CETA has also opened up procurement by EU governments at all levels. Though the procurements available to Canadian companies have been limited to a specific list of goods and services that are considered high-value… this provides far greater access than had previously existed.

One of CETA's other key benefits is the increased mobility that is available to business executives from Canada and the EU. Four categories of visas have been created for these executives, including a visa that will allow an intra-company transferee to move to the EU (or Canada) for up to three years.

TPP gains new vigour

Trade with Asia also promises to become more accessible. The TPP, thought all but dead when President Trump withdrew the U.S. from the agreement in January, seems to be showing signs of new life. The remaining 11 nations that were party to the TPP, including Canada, have reached an agreement on the core elements of a new pact known as TPP-11. This agreement would allow Canadian businesses greater access to markets in Australia, Brunei, Chile, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore and Vietnam. U.S. withdrawal has reduced the overall economic size of the deal, but the TPP-11 nations still have a combined GDP of US$12.4 trillion and include some of the world's fastest-growing economies. This could present Canadian businesses with some significant new opportunities to grow abroad.

Though a trade agreement of this size and scale would generally take years to negotiate, much of the agreement will be based on the text of the original TPP, finalized in 2015. As a result, a much shorter timeline to completion can be expected. Canadian businesses should continue to monitor developments on this front.

Conclusion

The changes in trade and investment rules that began in 2017 can be expected to continue for the near future, and will be disruptive to the current trade and investment arrangements forged by businesses.

As long as the future of NAFTA remains uncertain, and perhaps in any event, Canadian businesses should focus on diversifying their trading relationships to take advantage of the new preferential access to the EU market based on CETA, and the potential for greater access to much of the Asian Pacific Rim through the TPP-11 and other trade arrangements.