Trump's reality-TV trade deal

By Dean Baker
October 3, 2018 – *CEPR*

Not surprisingly, Donald Trump is boasting loudly about his big new trade deal with Canada and Mexico. He touted the package, now called the United States, Mexico, and Canada Agreement, or USMCA, as "the biggest trade deal in the United States' history" and promised that it would "transform North America back into a manufacturing powerhouse."

In reality, there is not much in this package that was not also in the Trans-Pacific Partnership (TPP), from which Trump removed the United States shortly after taking office. And progressives should oppose Trump's "historic" new trade deal for the same reasons they opposed the TPP.

Before getting into specifics, though, some basics on trade would be useful. Trump routinely refers to trade deals as pacts in which some countries are winners and others (the United States, in his story) are losers. The scorecard is the bilateral trade deficit. By this measure, Trump could denounce negotiators in the Obama, Clinton, and two Bush administrations as "stupid," since the United States ended up with deals that left this country with enormous trade deficits. But this fundamentally misrepresents our trade negotiators' agenda.

To take the case of NAFTA, US negotiators were quite explicitly negotiating a pact that would make it as easy as possible for US corporations to set up factories in Mexico in order to take advantage of its relatively low-cost labor. Much of the deal was about establishing rules on investment that ensured US corporations their factories could not be expropriated and that Mexico would not be able to prevent them from repatriating profits back to the United States. We even set up a special extra-judicial process, the Investor-State Dispute Settlement (ISDS) mechanism, which gave corporations an extra safeguard to protect their investments.

Since a major purpose of NAFTA was facilitating the outsourcing of factory jobs to Mexico, we should recognize that the US trade deficit with Mexico is evidence of the deal's success, not its failure. The same applies to other pacts, most importantly the agreement that allowed China to enter the World Trade Organization.

While the millions of manufacturing workers who lost their jobs in places like Ohio, Pennsylvania, and Michigan were very big losers from China's entry into the WTO, companies like GE and General Motors, which were doing the outsourcing, were very happy with the outcome. The same applies to retailers like Walmart, which used low-cost supply chains in China to undermine their domestic competitors.

With this background in mind, we can ask who will win and who will lose from USMCA. Here we can pretty much go back to the story with the TPP.

Like the TPP, the USMCA includes a variety of measures that strengthen and lengthen patent and copyright monopolies as well as related protections. This is good news for the industries that benefit from these protections, especially the prescription-drug industry, but it's bad news for pretty much everyone else.

During his campaign, Trump frequently denounced the outrageous prices the pharmaceutical companies charge for drugs. He has a strange way of clamping down on the industry, though; apparently, it's to make people in Canada and other countries pay more for their drugs.

People who own stock in pharmaceutical companies should expect to see higher profits and therefore higher stock prices, but pretty much everyone else is harmed rather than helped in this deal. Locking in stronger protections (yes, this is protectionism, the opposite of free trade) makes it more difficult for people in the United States to seek out lower-cost drugs elsewhere.

Also, as a matter of basic economics, a larger US surplus on licensing fees for patents means a larger trade deficit in everything else, other things being equal. That's because, contrary to what is often reported in the media, what is being protected is not "our" intellectual property; it is the intellectual property of a relatively small number of large corporations. The more money they get from our trading partners, the less money our trading partners have to spend on US manufactured goods and other items made here.

The USMCA also includes rules on the digital economy that are likely to benefit behemoths like Amazon, Google, and Facebook, to the detriment of other countries. One of the key issues in negotiations was whether such companies would be required to have a physical presence in countries where they do business. If they were, it would facilitate legal action against those that do things like assist in tax evasion or in manipulating elections. The final USMCA deal prohibits countries from requiring such a physical presence. This is a dangerous precedent, since the rules in the USMCA are likely to be carried over to other trade deals.

The final USMCA language also ended up retaining the ISDS, although it does limit the mechanism's scope to a more narrow range of issues, such as when an industry dumps goods below cost. This is definitely a plus, since the ISDS had been used to challenge a wide range of laws and regulations affecting the environment, consumer safety, and workers' rights.

There are also provisions on currency management. While neither Mexico nor Canada had deliberately reduced the value of their currencies against the dollar in order to make their goods more competitive, the section on currency values can be a useful precedent for future trade pacts.

Trump has talked a lot about bringing back manufacturing jobs. This trade pact, however, is unlikely to make that happen. While it does include some changes that may make a small difference at the margin, such as raising the North American content threshold that allows cars to qualify for tariff-free access (from 62.5 percent to 75 percent), it is likely to have only a minimal effect on trade patterns. Many cars already meet this threshold. In cases where they are far from the threshold, companies can still opt to import a car into the United States and pay a 2.5 percent tariff. That is a modest penalty that is dwarfed by the size of currency fluctuations.

Some people may wrongly take consolation in the USMCA requirement that 40–45 percent of the value added in vehicles must come from workers who make at least $16 an hour. This is essentially saying that this portion of the value-added must come from the United States or Canada, since $16 an hour is well above the pay of Mexican autoworkers.

If the purpose was to raise the pay of Mexican autoworkers, a target in the range of $10 to $12 an hour would have been much more realistic. As it is, the deal does include some stronger wording on labor rights, but the enforcement mechanism is nothing like the ISDS available to investors. The best hope for Mexican workers in this respect is their newly elected president, the left-populist Andrés Manuel López Obrador, not the USMCA.

It is important to recognize that the manufacturing jobs lost to imports over the past two decades are like toothpaste out of the tube; they are not coming back. While reducing the US trade deficit would increase the number of relatively high-paying manufacturing jobs available here to workers without college degrees, most of these jobs will not be in the rust-belt states that were big job losers. And a much smaller percentage of the new jobs will be unionized.

OK, so the new NAFTA may not be a big boon to manufacturing, but at least we will sell more milk to Canada, right? Milk exports to our northern neighbor seem to loom large in Donald Trump's head, but not in the real world. Canada's market for dairy products is a bit more than $3 billion. We already have a surplus of $600 million in dairy trade with Canada. This means that if we captured half of the Canadian market—a huge achievement—we would increase our dairy sales to Canada by about $1.1 billion. This is equal to roughly 2.5 percent of our industry's current production and 0.006 percent of US GDP.

In Trump's reality-TV world, the USMCA may amount to a historic accomplishment. In the real world, it won't change very much at all. Perhaps, if he keeps blustering about the Great Milk Conquest (GMC), it will help Trump carry Vermont in 2020.