International Agri Insights

with Professor Bill Bailey

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If at first you don’t succeed, tri, tri again

In this latest edition of International Agri Insights, our US-based expert, Prof. Bill Bailey, gives his insider’s take on the new trade agreement between the US, Canada and Mexico.

- US, Canada and Mexico have surprisingly reached agreement on tri-lateral trade talks.
- Although agriculture is a small part of the agreement, it has generated much attention.
- The agreement is similar to what Mexico and Canada accepted in the new Trans Pacific Partnership and puts a potential brake on increased trade with China for US, Mexico and Canada exporters.
- The agreement will have very limited impact on New Zealand agricultural exports.

US, Canada and Mexico agree to USMCA aka NAFTA 2

To paraphrase a well-known expression, “The Agreement has expired. Long live the Agreement.” In this case, the North American Free Trade Agreement (NAFTA) has expired and the United States-Mexico-Canada-Agreement (USMCA), referred to by some as NAFTA 2, has just arrived.

A key trade issue, discussed here a number of times over the past 12 months, has been the uncertainty created by recent trade conflicts centered around cars and steel between the US, Canada and Mexico. That uncertainty was partially lightened with a tentative agreement between the US and Mexico that was reached in August and (in a surprising reversal of negative public statements) the US and Canada agreement reached in early October. The result is the United States-Mexico-Canada-Agreement (USMCA). (*A side note, the author was in the US Marine Corps (USMC), so I am a little partial to the name of the Agreement*). The Agreement was reached after some last-minute, reasonably focused (frantic) talks at the end of September. Talks between the US and Canada, at least in the public press, were doomed to fail. The relations between US President Trump and Canadian President Trudeau had become somewhat chilly. But, skilled negotiators and open negotiations resulted in a truly last-minute agreement just before midnight on the 30th of September, the deadline that the US had set for reaching an agreement. With no agreement, it would have been a US and Mexico only Agreement (USMA), with Canada on the sidelines.

Although approval by the various legislatures may take time

While all three countries have now decided on new trade rules between them, implementation of the Agreement remains uncertain since approval is needed by each country’s legislature. There is political uncertainty in the US with the potential for a change in legislative leadership, resulting from the November 6 elections, a real possibility. Furthermore, during the US Congressional review, which is part of the process, changes to the Agreement might be made, slowing the approval process down even further. While it is assumed the USMCA will roll into effect over 2019, even that broad assumption may be incorrect.

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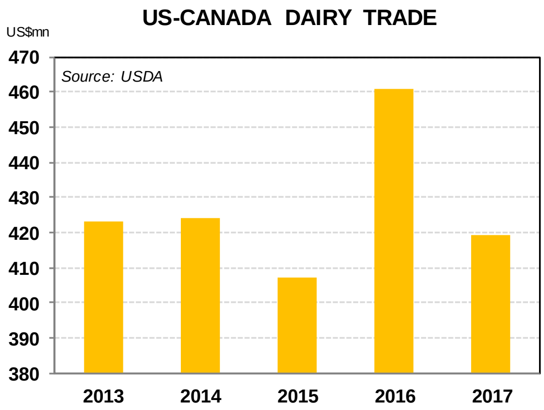
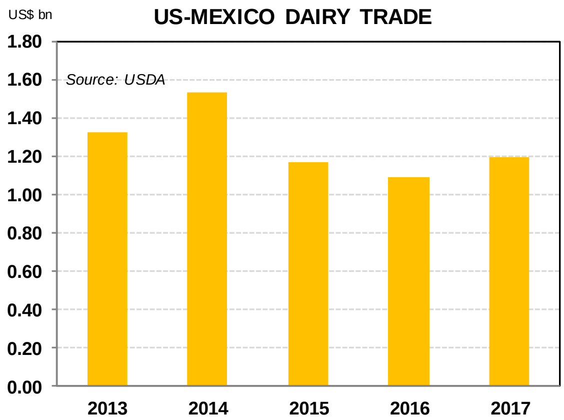
USMCA includes Canadian "concessions" on dairy market access

Canadian dairy policy had been a key factor in the ongoing challenges the US and Canada faced in bringing their trade negotiations to a conclusion. Broadly following the guidelines requested by the US dairy industry, Canada agreed to:

a) eliminate its Class 7[1] milk policy;
b) increase, from 3.25% to 3.59% of total Canadian dairy sales, the non-tariff dairy import level, which if exceeded triggers huge tariff increases for a variety of dairy products imported into Canada; and
c) raise the support price for ultra-filtered milk so that US dairy producers may be slightly more competitive in the Canadian market.



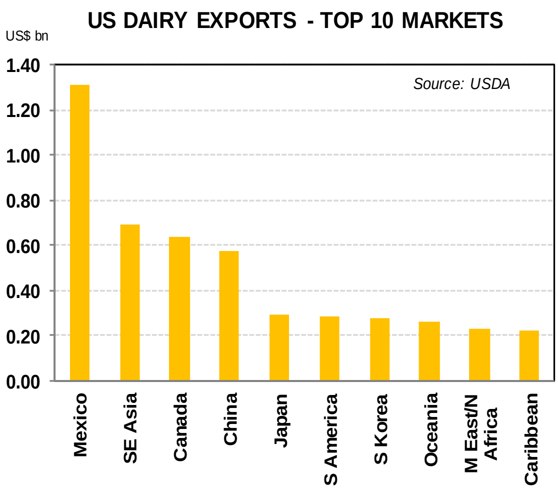
Canada has also agreed to limit its exports of skim milk powder, milk protein concentrate and infant formula to specific levels or the products will face export surcharges.



While Mexico is a much larger US trading partner for dairy products than Canada, there are few dairy product trade restrictions between the US and Mexico. As a result, Mexico is the largest market for US dairy exporters. One issue that did arise with the US-Mexico agreement was that US cheese makers could still sell certain cheeses that have geographic indications, such as Swiss, mozzarella, gouda, and edam. Mexico had recently agreed to European Union demands that certain cheeses, with a geographic identity, could only originate in Europe. However, during USMCA negotiations, some exemptions for US origin cheeses were accepted.

Notably, future trade agreements with China have been made more difficult

A key part to the Agreement (which has frequently been overlooked), is the stipulation that if one country wishes to start free trade negotiations with a "non-market" country, the other parties must be permitted to review the agreement and, if it is not to their liking, the USMCA could be replaced, within six months with a bi-lateral agreement between the two other countries. Experts interpret "non-market" as China and the clause has the potential to effectively freeze current Canada-China trade at current levels.



There will be very limited impact on NZ agricultural exports

According to the US Trade Representative's (USTR) office, the most significant change to Canadian agricultural import policy is a slight increase in the amount of milk, cheese and

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[1] *Class 7 milk is predominately skim milk powder and, as a consequence, Class 7 imports from the US are subject to import tariffs. The tariffs make US imports non-competitive with domestic Canadian production.*

cream the US can ship tariff-free into Canada. Since Canada is the third largest market for US dairy exporters, but less than half the size of the Mexican market, such a move to relax tariffs is noteworthy. But the increase in the Tariff Rate Quota (TRQ) total from 3.25% of total dairy sales to 3.69% over 6 years, simply recognizes population growth, and is not seen as a true opening of the Canadian dairy market. As one well-known US dairy analyst noted, the total impact on the US dairy industry, estimated at a $70 million increase in sales to Canada, isn't going to be very noticeable, since US dairy industry total exports were valued at $5.5 billion in 2017. But new sales opportunities, however small, are always welcomed by US exporters. What is important to New Zealand dairy farmers is that the increase in TRQ levels is limited only to US imports.

While some assess the impact of the USMCA on US dairy farmers as being minimal, to Canadian dairy producers – who see their tightly protected domestic industry now opened up, albeit ever so slightly – the changes are very significant. The head of one major Canadian dairy producer organization said they were "quite disappointed." He added "the deal will result in reduced (Canadian) milk production because the markets will be filled with subsidized products from the US, and Canadian farmers won't be able to compete fairly." An important aspect of Canadian dairy being part of the USMCA is that it was excluded from any changes in the earlier NAFTA. The new requirements in USMCA are viewed by Canadian dairy farmers as potentially the first step for additional trade changes to the Canadian dairy industry.

Another issue the US tried to resolve in the negotiations centered on how disputes between the three countries would be resolved. Under the previous NAFTA rules, when disputes arose, often based on a change of governmental rules after a company had invested in that country, they were handled by an independent international dispute tribunal. The US wished to make the process a domestic issue – American courts would handle trade disputes that affect the US. While Mexico had agreed to the US position, Canada wished to maintain some form of independent international tribunal. The Canadian position was accepted and the current dispute rules will remain unchanged.

Congress still has the final say

President Trump must take the USMCA to the US Congress for its approval. Congressional leadership has stated (because the Congressional review process is lengthy) USMCA will not be voted on by the US Congress until 2019. But Congressional leaders have given the assurance that the vote would move to the head of the 2019 legislative line. Postponing the vote until next year means that President Trump may have to get it through a divided Congress, should the Democrats regain a majority after the November 6 national Congressional elections.

About the author

William C Bailey was Chair of Agribusiness at Massey University for 13 years. He has written weekly world dairy market columns for ASB Bank for almost 15 years. He currently is President of Topker Consulting, specializing in agricultural market research and supply chain issues relevant to agriculture. He retired as Dean, College of Business and Technology, at Western Illinois University, in Macomb, Illinois, in July, 2017. Bill spent 5 years in the US Marine Corps and received his PhD in Agricultural Economics from the University of Missouri. Before shifting to New Zealand, Bill was Chief Economist for the US Senate Committee on Agriculture, Nutrition and Forestry, served as Deputy Undersecretary of Agriculture and was Vice President and Director of Research for World Perspectives in Washington, DC. His beer of choice is Tui. Contact Bill: topkerconsulting@gmail.com Phone: +1 309 333 5117

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