

# Is NAFTA 2.0 Better than Nothing?

*Would Americans be better off if their government simply repealed NAFTA rather than replace it with the USMCA?*

◆ BY PIERRE LEMIEUX

**L**ate last September, the governments of the United States, Mexico, and Canada announced agreement on the United States–Mexico–Canada Agreement (USMCA) to replace the North American Free Trade Agreement (NAFTA). The standard reaction of free traders to the announcement was that the new deal isn't as bad as they had feared. A *Wall Street Journal* editorial put it succinctly: “The new trade deal could have been worse given Mr. Trump’s protectionist beliefs, but that’s about the best we can say for it.”

More interesting was the tepid response to the announcement from groups that are not known as free traders. The president of the International Brotherhood of Teamsters, a large American union with a Canadian presence, applauded the USMCA’s “considerable progress on workers’ rights,” but said that more information, notably on enforcement, was required “before the Teamsters can give it our unqualified support.” The United Auto Workers were pleased but not ready to give their blessing until all the details are released. The AFL–CIO, the largest labor organization in America, called the agreement “a good start,” but said they “simply do not have enough information at this time to know whether [it] is in the economic interests of the United States.”

In truth, nobody at that time had enough information to make such a judgment. The final language wasn’t set until November 30—after this article went to press—when representatives of the three governments were scheduled to sign the agreement. Until then, analysts made due with a draft “Subject to Legal Review for Accuracy, Clarity, and Consistency.” Even with the formal signing, the proposed treaty will still have to be approved by the

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legislatures of the three countries, and it is not certain what the new Congress will do with the deal.

The draft agreement is made of a preamble, 34 chapters, 15 annexes, and 33 “side letters”—all of which add up to 2,082 pages. The USMCA is an even more complex piece of legalese than the roughly 600 pages of NAFTA.

In comparison, free trade should be simple. Any pair of individuals or their intermediaries or corporate bodies should be free to exchange a good or service on their own terms. The very complexity of the USMCA suggests that it is not free trade.

### POSITIVE POINTS IN THE USMCA

The USMCA is often described as being very similar to NAFTA, which is why some people are calling it “NAFTA 2.0.” Among the things that have been substantially maintained is the dispute settlement mechanism of the original NAFTA’s Chapters

19 and 20, which allows each national government to challenge antidumping or countervailing duties before arbitration panels.

Much of what the USMCA does not borrow from NAFTA it copies from the Trans-Pacific Partnership (TPP), a trade agreement that the Trump administration abandoned and that the other 11 involved nations then rechristened the Comprehensive and Progressive Trans-Pacific Partnership (CPTPP) and signed. One lawyer’s estimate puts at two-thirds the number of chapters of the USMCA that can be traced to the CPTPP.

One can find positive changes in the USMCA, but they are small. One such change is a prohibition on currency depreciation intended to produce a trade advantage, although it may be difficult to disentangle such manipulations from ordinary monetary policy. Canadian and Mexican consumers will benefit from a higher threshold for importing small packages without tax or duty and with minimum clearance procedures. Agricultural trade is very slightly liberalized. Trade in digital products like music and e-books will be liberalized (as TPP proposed to do), although the liberalization will be accompanied by new regulations under the guise of consumer protection. Trade in financial services and telecommunications will also ostensibly be liberalized, though they too will be encumbered by exceptions and (as European bureaucrats would say) “harmonization”—that is, regulation.

### MORE TRADE REGULATION

Regulation is a general problem in the USMCA, even more than it was in NAFTA. One example is the extension of intellectual property protection (on copyrights and some patents, including “scent marks”), which will be accompanied by strengthened regulations and controls. More significantly, as the *Wall Street Journal* noted, “The new deal also takes a giant step toward politically managed trade by imposing new rules of origin and labor regulations.”

The USMCA tightens the previous rules of origin. These rules make it harder for intermediate goods imported from outside a “free trade” area like North America to stealthily benefit from the zone’s trade preferences when incorporated into final products traded within the zone. For instance, to move across North American borders without tariffs, cars will need to have 75% North American content, compared to 62.5% under NAFTA. North American car and truck manufacturers will also have to purchase 70% of





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their steel and aluminum on the continent in order to avoid tariffs.

This will raise costs on North American consumers. We know this because, if manufacturing more parts and materials in America did not increase costs, manufacturers would already be doing it. Costs will thus increase, notably for small cars built in Mexico with large parts such as transmissions and engines imported from the rest of the world. Examples include the Nissan Sentra, the Volkswagen Golf compact, the Honda Fit, the Fiat 500 subcompact, and the small Mazda3. It seems that “fairness”—a term used in one form or another some three dozen times in the agreement—is consistent with hitting consumers who buy small cars. What about the poor and the environment?

The USMCA will protect unionized American (and Canadian) workers against competition from poorer Mexicans. North American car manufacturers will be obliged to ensure that about 40% of the value of their cars is produced by labor earning at least

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\$16 an hour. That is well below this sector’s wages in the United States and Canada, but above the wages currently paid in Mexico. In other words, the USMCA imposes a minimum wage on a large proportion of Mexican autoworkers. As a post by Stan Veuger of the American Enterprise Institute quips about the USMCA negotiations, “All this for a Mexican minimum wage increase?”

It is true that car importers could avoid these new restrictions by simply paying the 2.5% tariff approved by the World Trade Organization. But car parts or unfinished cars crossing borders several times along integrated North American supply chains would presumably be hit by the tariff more than once. Moreover, the U.S. government could then impose the 25% tariff it has threatened, or any amount of a “national security” tariff.

The effort to undermine the competitiveness of Mexican workers extends beyond the automobile industry. The USMCA mandates that each member government “shall adopt and maintain statutes and regulations, and practices thereunder, governing acceptable conditions of work with respect to minimum wages.” Iain Murray of the Competitive Enterprise Institute notes that the agreement will force the Mexican government to implement the “core rights” promoted by the International Labor Organization (ILO), including union recognition and mandatory collective bargaining. We can only hope that the Teamsters are right to fear an ineffective enforcement.

Why did the Mexican government accept these restrictions? One reason may be that the collapse of NAFTA would have impoverished Mexico and presented a political challenge to its government. Another reason is that many people on the left claim that restricting the employment choices of poor workers, as labor regulations do, constitutes a triumph of social justice.

If rational ignorance did not exist and all voters read Chapter 23 of USMCA, many would be surprised to learn that the three governments involved “affirm their obligations as members of the ILO, including those stated in the ILO Declaration on Rights at Work and the ILO Declaration on Social Justice for a Fair Globalization (2008).” Aren’t these leftist causes ostensibly in contradiction with the Trump government’s official agenda? The answer is that the populist right, just like the populist left, has no libertarian or classical liberal philosophy, and is as willing to use organized labor for its own power-aggrandizement purposes.

Similar observations could perhaps be made about the USMCA’s Chapter 24 on the environment. It states that “a healthy environment is an integral element of sustainable development.” The three governments “recognize that emissions of certain substances can significantly deplete and otherwise modify the ozone layer in a manner that is likely to result in adverse effects on human health and the environment.” The Trump administration believes that? For good measure, the three governments

also “recognize the importance of promoting corporate social responsibility.”

#### A POLITICAL TAKEOVER?

The preamble of the USMCA is interesting in itself. It dutifully qualifies free markets and competition with the fairness ideology as it speaks of “freer, fairer markets” and “fair competition.” It is certainly not a coincidence that environmental and labor regulation will mainly impede Mexican competitors. How is that much different from what Barack Obama or Hillary Clinton would have negotiated?

An original and questionable innovation of the USMCA is to practically prohibit any of the three governments (“the Parties,” as they are called in treaty legalese) from concluding a free-trade deal with a non-market economy, which everybody recognizes is aimed at China. Article 32.10, par. 4 decrees:

Entry by any Party into a free trade agreement with a non-market country shall allow the other Parties to terminate this Agreement on six-month notice and replace this Agreement with an agreement as between them (bilateral agreement).

I have argued before that there is no reason to fear the competition of a non-market country. (See “Peter Navarro’s Conversion,” Fall 2019.) Isolating China imposes a cost to all individuals and

corporations that would have freely traded with Chinese partners. It also increases the risk of a military confrontation.

The USMCA makes continental trade more dependent on politics and more subject to political uncertainty. The agreement includes a 16-year sunset clause if it is not specifically renewed. Neither Canada nor Mexico is seriously protected against future tariffs that the U.S. government could (again) impose under the excuse of “national security.” Although the three national governments will still be able to bring trade disputes before USMCA arbitration panels, a private foreign investor from within the area will not generally be able to do so, as was possible under NAFTA.

The Trump administration’s trade war has generated much political uncertainty. One case in point: companies that could move their factories to the United States, as Trump wants, would face “political risk” if they do so. What if their imports (automobile parts, for example) are hit by new American tariffs? Johan Gott, a principal with global management consulting firm A.T. Kearney, notes that “these companies are now seeing an element of political risk to operating in the U.S.”

For a country’s residents, the main benefit of free-trade agreements is not so much to save them from foreign governments’ protectionism as to protect them from their own Leviathan—and any state is a potential Leviathan. A free-trade treaty ties the hands of one’s own government, which is a benefit not a cost. Many changes in the USMCA increase the power of the national governments involved—and perhaps mainly the U.S. government—over their own citizens, instead of better circumscribing it.

The rechristening of NAFTA as the USMCA betrays the political character of the renegotiations. In his 2016 campaign, Trump called NAFTA the “worst trade deal maybe ever signed anywhere,” which was at best a politician’s exaggeration. The president will now be able to cynically claim that he has repealed NAFTA while, in fact, he has accentuated its worst features.

### A FUZZY BOTTOM LINE

It is quite clear that the original NAFTA was more favorable to free trade than the USMCA. That the expression “free trade” has been deleted from the latter’s name is not benign. This raises the question whether the USMCA is better than no trade deal at all—that is, better than even a repeal of NAFTA with no replacement.

One argument for a positive answer—that NAFTA 2.0 is better than no NAFTA—is the symbolism of the alternative. A repeal of NAFTA by President Trump would have boosted the idea that the world is entering a new age of protectionism. It also would have struck another blow to the international standing of the United States and the idea of liberty that it still represents for many. We cannot know for sure how the USMCA will play out, and it might not be as bad as it seems.

There also are arguments to support a negative answer: that no NAFTA would be better than a fake one under the name of USMCA. One problem is that the new agreement strengthens the false ideas that export is the justification of free trade and that the goal is to protect corporations and other producers (including government cronies).

Despite occasional lip service to “consumer welfare,” one is hard-pressed to find in the USMCA’s 2,082 pages a clear reference to the benefits to consumers of international trade. Benefits to consumers always seem to flow from regulation and the protective intervention of benevolent governments. But in reality, the state acts on behalf of domestic producers, not consumers. *National governments negotiate on behalf of their producers.*

The USMCA thus deepens the fundamental misunderstanding in debates about free trade. As free traders know, the real benefits of free trade accrue to consumers—most of whom are

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also producers, but they produce in order to consume, not the other way around. Managed or regulated trade, on the contrary, is based on the idea that every freedom to import that a government gracefully grants its citizens must be matched by a “concession” from foreign governments, as if the value of trade resides in exports. Free traders tend to adopt the concession vocabulary in order to persuade the other side, but in doing so they undermine the true economic and ethical arguments for free trade.

It would thus be better for the vast majority of people in the three countries of North America if Congress rejected the USMCA and stopped Trump from abrogating NAFTA. Assuming that this is not a feasible option, the preferable alternative between a bad USMCA and no agreement at all is difficult to decide. It seems to me that a supporter of economic freedom and free trade could take either side of the issue.

I don’t emphasize the alternative of unilateral free trade because it is not politically feasible now. The question at hand boils down to which of the alternatives on the political table has the best chance of moving us toward—instead of away from—an ideal world where every individual, at least among our fellow citizens, is free to trade as he wishes, to individually make his own deals at home or abroad with whomever is willing and able to trade.