Trade Update

December 10, 2019

By Michael Anderson

Highlights

- **USMCA:** USMCA deal reached! USTR and Speaker Pelosi announce aim to vote on USMCA before December recess.
- **China Tariffs:** Deal on a phase one U.S. – China trade deal remains elusive despite reported progress.
- **WTO:** WTO Appellate Body ceases to function today creating uncertainty for the dispute settlement system. Industry groups, coordinated by Americans for Prosperity, sent a letter proposing three steps to WTO reform and urging President Trump to act quickly.
- **U.S. -EU Trade**: Trump and European Commission send mixed signals on potential trade talks while U.S. considers 100% tariffs on European imports under the Airbus ruling.

USMCA

- In this morning's press conference, Speaker Pelosi announced that Democrats have reached a deal with the Trump administration on the new North American trade agreement, pushing President Trump's major trade initiative closer to passage in Congress. Details of the agreement and timing of a vote are forthcoming at this writing.

- According to reports over the weekend, U.S. and Mexican officials resolved the major sticking points in their negotiations over changes to USMCA's labor and enforcement provisions, setting the stage for a final deal. Mexican Under Secretary for North America Jesús Seade met with Ambassador Lighthizer on Saturday to continue USMCA talks and indicated that he would likely return to D.C. Monday to conclude discussions. "We're doing well. I'm confident. We're close." Seade said as he left the talks on Saturday.

- Seade and Mexican Foreign Minister Marcelo Ebrard met with Mexican Senate leaders on Sunday afternoon to update them on negotiated changes to the deal. Ricardo Monreal, Mexican Senate Majority leader, expressed optimism that they would see formal USMCA text changes in the "next few days."

- In another sign a USMCA deal is close, AFL-CIO President Richard Trumka briefed the group's executive council yesterday afternoon on proposed changes to the USMCA text. Trumka characterized the results of many months of talks in an email to the Washington Post: "We have pushed them hard and have done quite well." The White House is reportedly anticipating that a deal will be announced this week in hopes of the House voting on USMCA before Christmas, according to Jessica Ditto, White House Deputy Communications Director.

- For context on the latest developments, last week a Mexican official said Mexico would consider agreeing to the U.S.'s demand concerning the "melted and poured" standard for steel, so long it is not implemented for at least five years after the ratification of the deal. Mexican Foreign Minister Ebrard, also made clear that Mexico would not agree to these standards for aluminum, as Mexico does not produce the raw inputs for aluminum, and thus Mexican aluminum would not fit the standard to be considered North American aluminum.

- Amb. Lighthizer and Mexican Under Secretary for North America Jesús Seade spent almost seven hours meeting last Wednesday to discuss the proposed changes. One major sticking point is proposal to allow American inspectors to Mexican workplaces has been decried as an affront to Mexican sovereignty. After the meeting Seade said, "For us, we are down to the bone. We have accepted 1,000 things. But there are a couple of suggestions that, depending on how you read it or what text you read, can be unreasonable." "People have to accept Ambassador Lighthizer is looking for a solution, as are we" Seade said. He noted that both negotiators are working on "creative" solutions to issues of labor enforcement. These past concerns appeared resolved according to the latest reports from discussion this past weekend.

(Amb. Lighthizer and Undersecretary Seade)

Section 232 Tariff Actions

- As noted earlier, President Trump announced by tweet on December 2nd that the U.S. is placing tariffs on steel and aluminum imports from Argentina and Brazil, alleging that the two countries “have been presiding over a massive devaluation of their currencies.” The Brazilian real hit a record low against the dollar the week of November 25th, while the Argentine peso has suffered a sharp decline against the dollar since the presidential elections in October, when President Mauricio Macri, a right-leaning former businessman, was rejected for a second term in favor of Alberto Fernández. Fernández is expected to return the country to Peronism, an Argentine political movement oriented towards economic autonomy, nationalism, and populism. The peso also underwent a sharp devaluation in 2018 as a result of high inflation and a combination of other factors.

(Argentine President, Mauricio Macri)

Auto Tariffs

- There is still no indication whether Trump will attempt to pull the trigger on auto tariff imports, despite Commerce Secretary Wilbur Ross’ recent comment that the door remains open. Sen. Pat Toomey and several legal experts have contended that the window has closed for auto tariffs, statements which are supported by a recent court ruling. Toomey contends that the Commerce Department “…must launch a new investigation” on whether auto and auto part imports constitute a national security threat prior to any tariff action.

- Some observers indicate that President Trump may keep the pressure on EU officials through other trade tools, including a section 301 investigation, which would examine EU subsidies and other programs in the auto sector. A former EU official characterize the potential strategy as creating “a situation that, for another year, would give the president leverage over the EU.”

Section 301 Tariff Actions

Digital Services Tax - France

- As noted earlier, the Trump Administration has found discriminatory tax treatment for U.S. internet firms under a section 301 investigation into digital services taxes in Canada. The report published by USTR’s sets out the findings of the investigation. A USTR press release stated,

  ‘“USTR’s decision today sends a clear signal that the United States will take action against digital tax regimes that discriminate or otherwise impose undue burdens on U.S. companies,” Ambassador Robert Lighthizer said. “Indeed, USTR is exploring whether to open Section 301 investigations into the digital services taxes of Austria, Italy, and Turkey. The USTR is focused on countering the growing protectionism of EU member states, which unfairly targets U.S. companies, whether through digital services taxes or other efforts that target leading U.S. digital services companies.”’

- USTR announced possible imposition of 100 percent duties on up to $2.4 billion worth of French products — including cheese, Champagne, handbags, cosmetics and fine dinnerware under section 301 authority, unless France agrees to drop or modify the country’s new digital services tax unfairly aimed at American internet giants. The proposed retaliation could also include fees or market restrictions on

French services companies operating in the United States.

Tech and IP Policies - China

- According to National Economic Council Director Larry Kudlow, the U.S. and China are "working around the clock" and are "close to a trade deal. "The final strokes are not there, we're coming down to short strokes," he said. "Now, some of the most delicate matters have to be adjudicated, discussed, analyzed and evaluated. And then it will be presented to President Trump, and he'll take a look at it." Kudlow added that "great progress has been made."

- Prior to Kudlow's statement, President Trump said during last week's NATO meeting in London that he "like[s] the idea of waiting until after the election for the China deal." Chinese demands for the elimination or roll back of existing tariffs, President Trump's signing of the bill supporting the Hong Kong protesters, and U.S. demands for specifics on Chinese agricultural product purchases have all contributed to a breakdown in progress towards a signing of the deal.

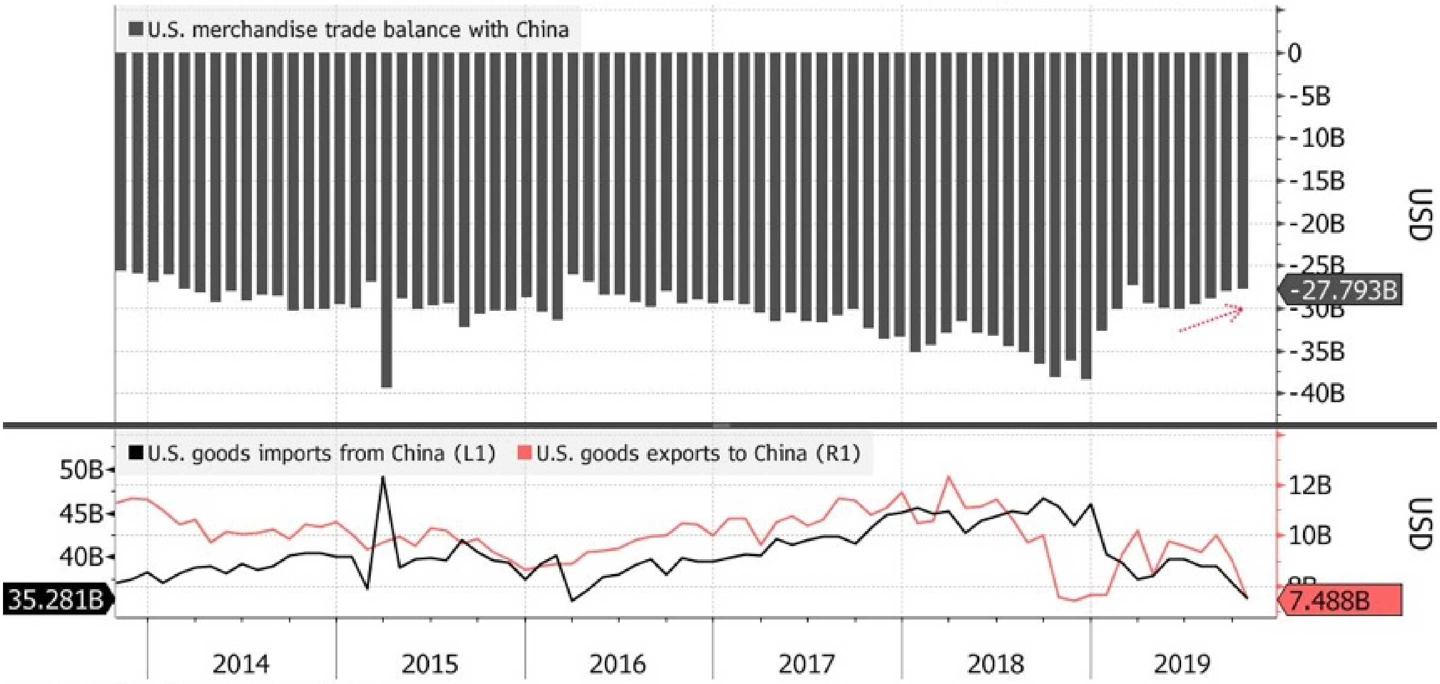
- Commerce Secretary Wilbur Ross put the onus for a completion of a U.S.-China phase 1 deal on China last week, saying that a completion of the deal "depends on their behavior" and adding "It's great that he [President Trump] has the hammer of December 15th," the date when the next round of U.S. tariffs on Chinese products will be implemented if a trade deal is not struck before then.

- Only 6 days remain for Amb. Lighthizer and his Chinese counterpart, Vice Premier Liu He, to lock in the details of a phase-one deal to avoid another escalation in a trade war with the 4th tranche of U.S. tariffs (List 4b) scheduled to take effect on Dec. 15th, covering consumer products such as smartphones, laptops, and toys. Last week President Trump indicated a deal was close: "We're in the final throes of a very important deal, I guess you could say one of the most important deals in trade ever." "It's going very well but at the same time we want to see it go well in Hong Kong and I think it will. I think that [Chinese] President Xi [Jinping] can make that happen, and I know him, and I know he'd like to make it happen."

- Recent monthly U.S. trade statistics suggest the U.S. – China trade tensions are curtailing bilateral trade.

Less Trade

U.S. merchandise gap with China narrows as trade war depresses shipments



Source: U.S. Department of Commerce

U.S. - Japan Trade Agreement

- The upper house of the Japanese parliamentary body, the Diet, approved the U.S.-Japan stage 1 deal

- The upper house of the Japanese parliamentary body, the Diet, approved the U.S.-Japan stage 1 deal on December 4th, 2019, following on the heels of the lower house's passing of the deal on November 19th and clearing the way to meet the goal of implementation of the deal on January 1st, 2020. The deal was approved by the Diet in record time. "I commend Japan's quick action to approve these important trade agreements between our two nations…Now, U.S. farmers and ranchers will have significantly improved access to Japan's market, and America's leadership in the growing digital economy will continue to flourish to the benefit of all our workers" Amb. Lighthizer said in a statement released by USTR.

U.S. - EU Trade

- The incoming European Commission plans to focus its agricultural trade policy on Africa rather than on markets such as the U.S. or China, an EU official said last week. The official cited the growing middle-class in Africa as a reason for making the continent a central feature of its agricultural trade policy. The official also indicated that the EU commission plans to stop negotiating free trade agreements (FTAs) within the next ten years, and that an FTA with the U.S. is not a priority within this timeframe. "I don't think we're going to be seeing FTAs with India, with Russia, with China or the U.S. so by the next Commission our FTA agenda, I think, will be effectively finished" the official explained.

- During the NATO meetings in London, President Trump indicated that he is optimistic about the possibility of a U.S.-EU trade deal, saying "Meetings have been set up, and we'll talk. And I believe that it will work out well for everybody." German Chancellor Angela Merkel also expressed a degree of optimism before heading into a closed-door meeting with President Trump, saying "The fact that there is a new commission in place and also…a new president of the European Commission…now we have a very good basis to resume our trade talks as well."

(Chancellor Merkel and President Trump)

- EU tariffs are in the spotlight again as USTR announced possible tariffs of up to 100% on a range of European goods including aircraft parts, agricultural goods and a variety of other products connected with its review of the affirmative WTO case on illegal launch aid by Airbus. Last Friday, USTR issued a list of European products under consideration for up 100% tariffs. USTR is seeking comments by Jan. 13, 2020 on removal or increase in the contemplated duties on the list.

- The EU is expected to punch back with its own tariffs in early 2020 when a WTO arbitrator is expected to approve retaliatory tariffs in the countersuit on Boeing for illegals subsidies.

- In October, USTR announced 10% or 25% tariffs on $7.5 billion of EU goods, resulting from the WTO's ruling on the airbus dispute. Products subject to additional 25% duties include a wide range of agriculture and manufactured goods, notably cheeses, yogurt, butter, fruits, whiskey, and certain textile and apparel items, according to the final list released by the White House. The 10% duties are comprised solely of non-military aircraft and parts.

U.S.-U.K Trade Agreement

- Brits will head back to the polls on December 12th for a general election that was called for by Prime Minister (PM) Boris Johnson on October 29th. PM Johnson hopes that the elections will give him a majority in Parliament, thus paving a smoother path for the passage of a Brexit deal ahead of the extended deadline of January 31st.

- Proposed changes to the EU and U.K. tariff schedules after the completion of Brexit remain a major concern for the U.S. and other WTO members. The U.S. was recently joined by Australia, New Zealand, Canada, China, Mexico, South Korea and others in speaking out against the proposals, arguing that they would lead to diminished market access.

- The U.S. stated during the Geneva meeting that the UK and EU plan will not equitably divide access to the two members' markets but will rather decrease it. Citing two examples, the U.S. noted that TRQs (tariff rate quotas) would be effectively eliminated, pointing to grape juice exports to the bloc and pizza cheese exports to the UK as illustrative examples. "Furthermore, the proposed approach fails to address how bilateral EU-UK will be treated once the UK is no longer part of the European Union. Currently that trade is not subject to the TRQs. But what happens once Brexit concludes?" The U.S. further stated, "This is unjustifiable, and clearly an unacceptable outcome for other WTO members," and invited both trade partners to engage with the U.S. in "productive negotiations" on the issue.

- President Trump and Prime Minister Johnson previously expressed a common goal to have a U.S.-UK free trade agreement concluded quickly after the exit of Britain from the European Union. According to Bloomberg Economics, about 0.9% of global GDP is exposed to Brexit trade risk. For some context, EU-UK trade is about 3.1% of world trade.

Suspension Agreements

Sugar Suspension Agreement

- The stay granted by the Court of International Trade (CIT) for "vacating" the Sugar Suspension Agreement with Mexico expired last Friday, December 6th, reverting the trade terms back to the 2014 agreement.

- As noted earlier, the Court of International Trade (CIT) extended the enforcement date to December 6th, 2019 for "vacating" the existing Sugar Suspension Agreement with Mexico. The Justice Department had requested a 90-day stay of a CIT's ruling ordering the U.S. to vacate the 2017 amendments to sugar suspension agreements with Mexico. The request was supported by domestic producers, the Mexican industry, and Mexican government as being necessary to ensure that all parties have ample time to file comments with the Department of Commerce on the suspension agreements, and to give the Department of Commerce time to follow proper procedure during the process, according to an American Sugar Alliance spokesperson.

U.S. - India Trade Developments

- As U.S. and Indian officials have conducted negotiations, they have specifically focused on goods on which reduced tariffs will benefit the U.S. over China, according to some sources. Because a partial trade deal would create tariff reductions on a most-favored nation (MFN) basis, other third-party countries such as China would have access to the same tariff rates as the U.S., pushing negotiators to be mindful of not introducing tariff reductions on products that would benefit Chinese exporters and result in a flood of Chinese imports to India.

- As previous reports indicated, Amb. Lighthizer is interested in aligning GSP benefits to reciprocal Indian market-access concessions. For example, the amount of GSP benefits reestablished would equal the amount of new market access India provided the U.S. on a dollar-by-dollar basis. U.S. industry sources indicated cautious optimism about the trajectory of the negotiations, but also indicated that they remain uncertain whether the discussions can be completed before the start of 2020.

U.S. - Brazil Trade Developments

- No significant updates since initial reports last month of a potential for U.S. – Brazil trade talks. As noted earlier, according to a joint statement released at the end of the annual U.S.-Brazil CEO Forum additional "higher-level" meetings under a bilateral forum led by USTR and the Brazilian foreign affairs and trade ministries could occur. According to reports, initial discussions between the two sides also discussed several aerospace, infrastructure and transportation initiatives.

General Trade Cooperation/WTO Reform

- Americans for Prosperity coordinated an industry letter to President Trump, laying out specific reforms for the WTO Appellate Body and urging the Administration to resolve the current impasse. The letter was signed by 26 organizations ranging from manufacturers to consumer advocates to agriculture groups. The letter encourages the administration to support consensus reform proposals (the "Walker principles"); the establishment of an oversight and audit committee; and eight-year term limits for members of the AB secretariat. In its press release, American for Prosperity stated, "America's economic interests will be harmed if there is no internationally agreed upon mechanism for combatting unfair trade practices of other nations. Now is the time to put forward a specific, detailed U.S. proposal aimed at reforming the dispute settlement system so that global trade rules can be predictably enforced. The WTO dispute settlement system is worth saving."

- U.S. WTO Ambassador Shea indicated that any resolution to the AB crisis was unlikely at the General Council meeting next week, reaffirming the Trump administration's stance that members must first identify the "underlying problems." "We have asked repeatedly, if the words of the [Dispute Settlement Understanding] are already clear, then why have the practices of the Appellate Body strayed so far?," Shea said at a Trade Negotiation Committee. "This is not an academic question; we will not be able to move forward until we are confident, we have addressed the underlying problems and have found real solutions to prevent their recurrence."

WTO Ambassador, Dennis Shea (U.S.)

- As dissolution of the AB has arrived, the AB's future has focused increasingly on its permanent Director, Werner Zdouc (Austria). Viewed by many as dedicated public servant anchoring and ensuring the institution adheres to consistency, others are critical of his undue influence over appellate rulings and what they perceive as Zdouc steering the body away from its original mandate. He has served as secretariat director since 2006.

- The present debate by critics and supporters surrounds the issues of whether Zdouc exerts undue influence in the AB system, including by writing or revising draft appellate reports. Supporters argue that Zdouc is accountable to AB members and, accordingly, his power in the AB can be checked by members. Zdouc's supporters further contend his aims are to ensure consistency in Appellate Body rulings and the protection of the institution's integrity. Alternatively, Zdouc's critics counter that his obsession with consistency has produced "ossification" – according to former AB member Jennifer Hillman – creating an environment where Zdouc and AB members are unable or unwilling to admit, much less correct, past mistakes. The U.S. has cited trade remedies as an example of errant AB interpretations.

Werner Zdouc, Director WTO Appellate Body Secretariat

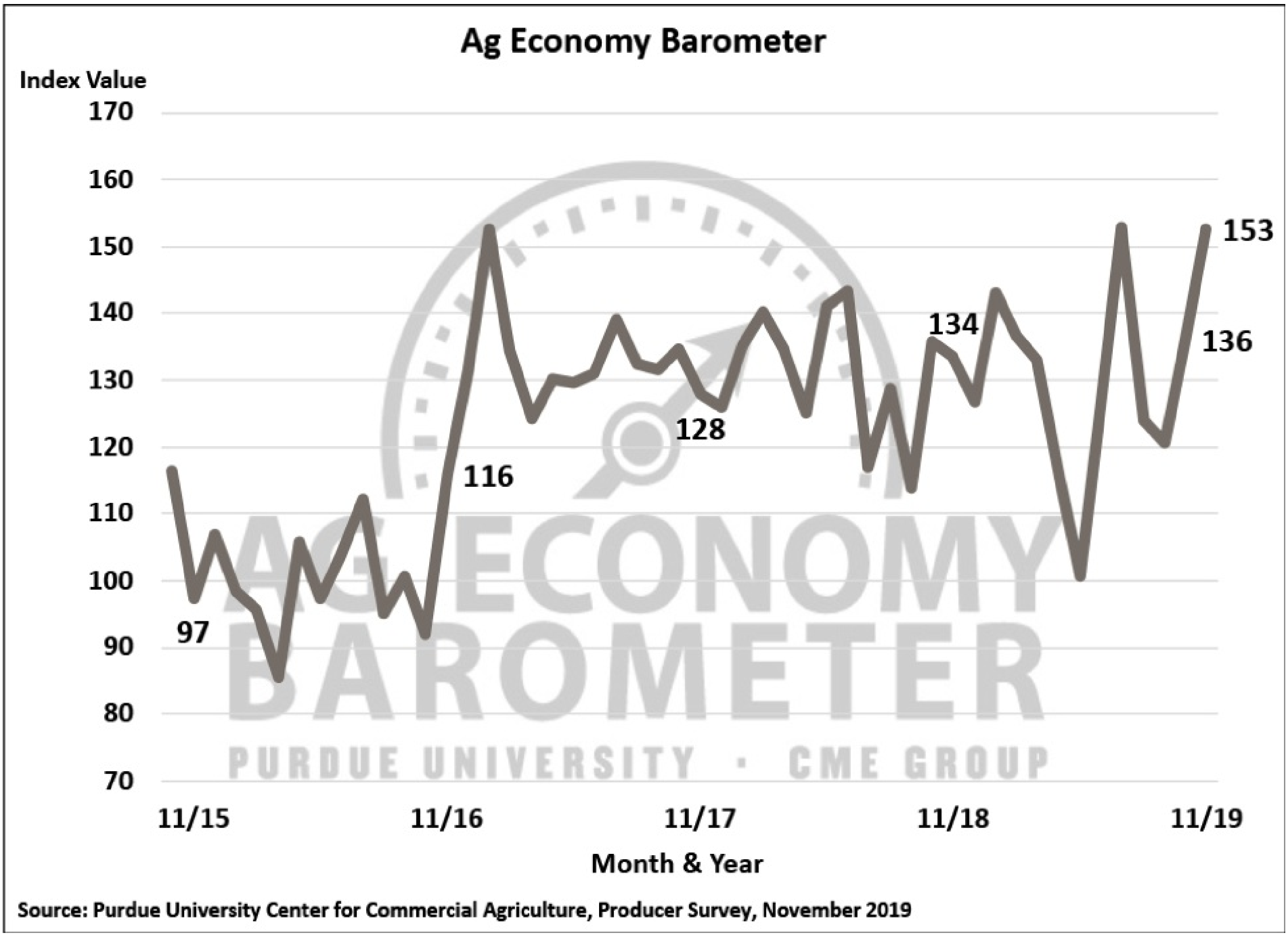
- Despite speculation that AB Chairman Thomas Graham might extend his AB tenure past December 10th in order to hear pending disputes, which is permissible under Rule 15 of the WTO Working Procedures for Appellate Review, Graham has stated that he will not do so, effectively cementing the shutdown of the AB as it loses quorum. Graham has based this decision on the continued tenure of Appellate Body Secretariat Director Werner Zdouc, whom Graham considers embodying the lack of willingness to make WTO reforms as desired by the U.S.

- The WTO has avoided a January 1st shutdown by passing a preliminary 2020 budget that acquiesces to U.S. demands to reduce funding for the Appellate Body. Members will delay discussions over the 2021 budget until a later date. The WTO revised budget calls for $199.23 million for 2020 and 2021, after an understanding was reached between the U.S. and the WTO officials cap allocated funds at $7 million for the Appellate Body.

- As AB shutdown approaches, the EU filed an appeal against the WTO ruling granting the U.S. the ability to impose retaliatory tariffs on European products as a result of EU subsidies for Airbus. The EU argues that it has cancelled one of the major programs receiving the subsidies and thus has dealt with the U.S.' complaint, and thus the retaliatory tariffs should be reduced. The EU's appeal almost certainly will not be resolved anytime soon due to the AB shutdown.

AG Economy Barometer

- The Ag Economy Barometer for the second consecutive month, climbing to 153 in November, 17 points higher than in October when the index stood at 136. The jump in sentiment, matches the previous 2019 high point in July. Contributing to the positive upward move were fall harvest activities and optimism for progress on current trade tensions with China and expectations a Congressional vote on USMCA.


Ag Economy Barometer
Index Value
170
160
150
140
130
120
110
100
90
80
70
97
116
128
134
153
136
11/15
11/16
11/17
11/18
11/19
Month & Year
AG ECONOMY BAROMETER
PURDUE UNIVERSITY · CME GROUP
Source: Purdue University Center for Commercial Agriculture, Producer Survey, November 2019