Trade Update

December 18, 2019

By Michael Anderson

Highlights

- **USMCA:** USMCA arrives! USTR submitted the USMCA implementing language last Friday to Congress. Earlier in the week, U.S. and Mexico signed the new version of USMCA, incorporating changes negotiated by House Democrats and USTR, and the Mexican Senate subsequently approved the changes. The House plans to vote on the new deal this week, while a Senate vote is expected in January 2020.
- **China Tariffs:** The U.S. and China announced a phase one deal last week averting new tariffs and rolling back some U.S. tariffs, while addressing areas of intellectual property, technology transfer, agriculture purchases, financial services, currency, trade expansion, and dispute resolution.
- **WTO:** Last week, the WTO Appellate Body ceased functioning. WTO members continue to discuss how best to move forward in the absence of a functioning Appellate Body. The U.S. continues to have concerns with the practice of the self-designation of "developing" and associated special and differentiated treatment for those countries.

USMCA

- Culminating a flurry of USMCA activity last week, USTR delivered to Congress the USMCA implementing bill on Friday, which was introduced as H.R. 5430 ("to implement the Agreement between the United States of America, the United Mexican States, and Canada attached as an Annex to the Protocol Replacing the North American Free Trade Agreement"). USTR also released the final text of the USMCA, setting the stage for an expected vote in the House this week.
- Senate Finance Committee Chairman Grassley confirmed Congress' receipt of the USMCA implementing bill, paving the way for the House Ways & Means Committee consideration of the bill Tuesday the 17th. Grassley called the move an "important milestone," and added that "Americans have been waiting for more than a year for House Democrats to act, and now Congress can finally consider this trade agreement." The House Ways & Means Committee will hold a markup on Dec. 17, according to a statement issued last Friday.

(Senator Chuck Grassley)

- USTR released the USMCA changes, "protocol of amendment" last Tuesday, which includes changes to USMCA's labor, environmental, pharmaceutical and dispute settlement provisions. U.S. Trade Representative Robert Lighthizer first negotiated the addendum with a group of House Democrats. It was then signed on Tuesday by Amb. Lighthizer, Mexican Under Secretary for North America Jesús Seade, and Canadian Deputy Prime Minister Chrystia Freeland.

- Within days of the announced deal on changes to USMCA, the Mexican Senate ratified the revised USMCA text (e.g. protocol of amendment) by a 107 – 1 vote.

- However, a potential wrinkle in the significant progress of USMCA was raised in Mexico over the weekend. The new USMCA implementing legislation outlines the designation of up to five U.S. experts who would monitor compliance with local labor reform in Mexico, which generated swift criticism from Mexico's chief USMCA negotiator, Jesús Seade, who sent a letter to Amb. Lighthizer expressing surprise and concern over the provision. Seade said he would travel to Washington for talks. Seade indicated concerns that the legislative language "go[es] beyond what is necessary to take care of the good compliance of the negotiators." "While Mexico respects the U.S. legislative process and the initiative of law that is part of the approval process of the T-MEC -- in Mexico, Mexico does not intervene -- its content was expected to reflect the scope of the agreed commitments, without establishing" additional "considerations or mechanisms," the letter states.

- **[Update] Reports late Monday indicate Amb. Lighthizer sent a letter to Undersecretary Jesús Seade** to reassure Mexico's government that U.S. labor attachés promised in the USMCA implementing legislation will not be akin to labor inspectors. Seade indicated Lighthizer "apologized" for not consulting with Mexico before deciding to include the attachés in the implementing legislation, and that he is satisfied with the letter Amb. Lighthizer sent him on Wednesday shortly after the two officials met in Washington, DC.

- Some Republican Members of Congress have signaled concern regarding the new version of USMCA. The AFL-CIO endorsement of USMCA has led to concern among some Republican senators that too many concessions to labor were made during negotiations and that the deal is too liberal. Senate Majority Leader Mitch McConnell said on Tuesday that "it's not as good as I had hoped," while Sen. Pat Toomey referred to it as "a terrible new standard" for trade agreements. Sen. John Cornyn cited his concern over "some of the things that he [Lighthizer] had to do to get the endorsement of Mr. Trumka."

- Sen. Cornyn also expressed his lamentations over the expected timeline for the Congressional vote on the agreement, which will skip over some steps that have become customary with recent trade agreements but are not required under the Trade Promotion Authority Act. For instance, the timeline will "essentially pre-empt the Senate Finance Committee from doing a mock markup, which has been done on every trade agreement since 1974 on…implementation language" he said, which will limit Senate input on the agreement. "Essentially, because the administration has cut their deal with Speaker Pelosi, the Senate is being precluded from participating in it. That's concerning." Sen. Cornyn added. According to Michael Zona, a spokesman for Senate Finance Chairman Chuck Grassley, a Senate markup will occur, but "No amendments will be allowed in accordance with the law under the Trade Promotion Authority." Sen. Cornyn has said he will vote in favor of USMCA, despite his dissatisfaction with the process.

- With expectations that the House will hold a vote on USMCA this week, Senate Finance Chairman Chuck Grassley said last Wednesday that the Senate will plan its vote on USMCA after the conclusion of the impeachment process, pushing its expected approval timeline into 2020, as the Senate is too busy with funding bills to hold a vote before the end of the year. "Just as soon as we get done with impeachment, it will pass the Senate a lot easier than it passes the House of Representatives" he said.

- Senate Majority Leader Mitch McConnell reaffirmed the Senate's USMCA timeline last week. "We will not be doing USMCA in the Senate between now and the end of next week.". "That will have to come up, in all likelihood, right after the trial is finished in the Senate." McConnell said. McConnell continued stating, the deal was "not as good as I'd hoped" but added that "we'll have to take a look at the whole package." Sen. John Thune weighed in on timing citing a vote on the deal this year impossible due to Democrats demands changes to the existing USMCA text. Thune continued, "It's going to be entirely up to our members and the amount of time they think they need to review it," Under Trade Promotion Authority law, the Finance Committee must vote on a trade implementing bill no later than 15 days after the House approves it or the bill is automatically discharged. The Senate must vote on the bill within 15 days of the Senate Finance Committee vote.

(Senate Majority Leader, Mitch McConnell)

- Mexican officials agreed to a "melted and poured" standard for steel in USMCA that will not take effect until seven years after the agreement goes into force. Previous to last week's signing of the agreement, a Mexican official said that Mexico would only consider agreeing to the U.S.'s demand concerning the "melted and poured" standard for steel if it was not implemented for a minimum of 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, which was part of the U.S.' original demand, 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.

- Consistent with Mexico's opposition to a provision negotiated by House Democrats that would allow U.S. inspections of Mexican factories, the final version of USMCA includes a special dispute settlement mechanism for labor disputes, according to Mexican Undersecretary for North America Jesús Seade. More details on the new plan emerged last Thursday. The mechanism will be directly related to union rights, an issue that was a large focus of Mexico's labor reforms passed last year. It allows the U.S. to file a complaint about any suspected union rights violations at a factory; if Mexico agrees with the complaint, it has 45 days to fix the issue. If it fails to do so, the U.S. can ask for the creation of a three-member panel, made up of one American member, one Mexican member, and one member from a third country, that will have the right to visit the factory where the union issue is occurring, as well as request documents or other evidence pertinent to the issue. Likewise, the Mexican government will have the ability to trigger the same mechanism for suspected issues in American factories.

- However, U.S. officials seemed to dispute this in a fact sheet released by the House Ways & Means Committee that notes that "State-to-state dispute settlement by itself has not been effective to ensure that U.S. trading partners live up to their labor commitments" and specifies that the enforcement mechanism "requires verification of compliance by independent labor experts."

Section 232 Tariff Actions

- No significant updates on President Trump's 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.

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," Amb. 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.
- USTR is accepting public comments until January 6, 2020 and holding a public hearing on January 7th on the proposed Section 301 actions on French products because of France's digital services tax.

Tech and IP Policies - China

- The U.S. and China announced a "phase one" deal to deescalate trade tensions. USTR released a fact sheet, providing some details of the "historic and enforceable agreement on a phase one trade deal" with China. The agreement includes reforms in China's IP protections, technology transfer, expanded agriculture purchases, reduced barriers to financial services, expanded U.S. import purchases (i.e. $200 billion), currency manipulation, and improved dispute resolutions procedures.
- According to White House reports, the U.S. will roll back existing tariffs on $360 billion of Chinese goods by as much as 50% as well as suspend the new 15% tariffs scheduled to go into effect last Sunday the 15th, as announced last October. The Trump Administration placed 25% tariffs on $250 billion worth of goods and 15 percent tariffs on about $112 billion worth of goods. The phase one deal would cut those tariffs to 12.5 percent and 7.5 percent, respectively. In return, China is expected to significantly increase annual agriculture purchases. China also agreed to expand access to its financial services market and include language on currency and intellectual property.
- Amb. Lighthizer confirmed China's commitment to expand agriculture purchases under a phase one deal, though less than the $40 - $50 billion previously sought. "There's a commitment to increase by $32 billion over the course of two years," said Amb. Lighthizer last Friday. "Their objective is to go to $50 [billion]. The commitment is to go to $40 [billion]." The baseline for increased agricultures purchases compares to the 2017 level of U.S. agriculture exports to China ($24 billion). Amb. Lighthizer stressed the expectation that China would continue a high level of U.S. agriculture imports beyond the two-year commitment. He further noted that China agreed to ramp up its overall purchases of U.S. goods and services by $200 billion. Formal signing of the deal is expected the first week of January after legal review and translation of the 86-page deal. The signing will be in Washington at the ministerial level.

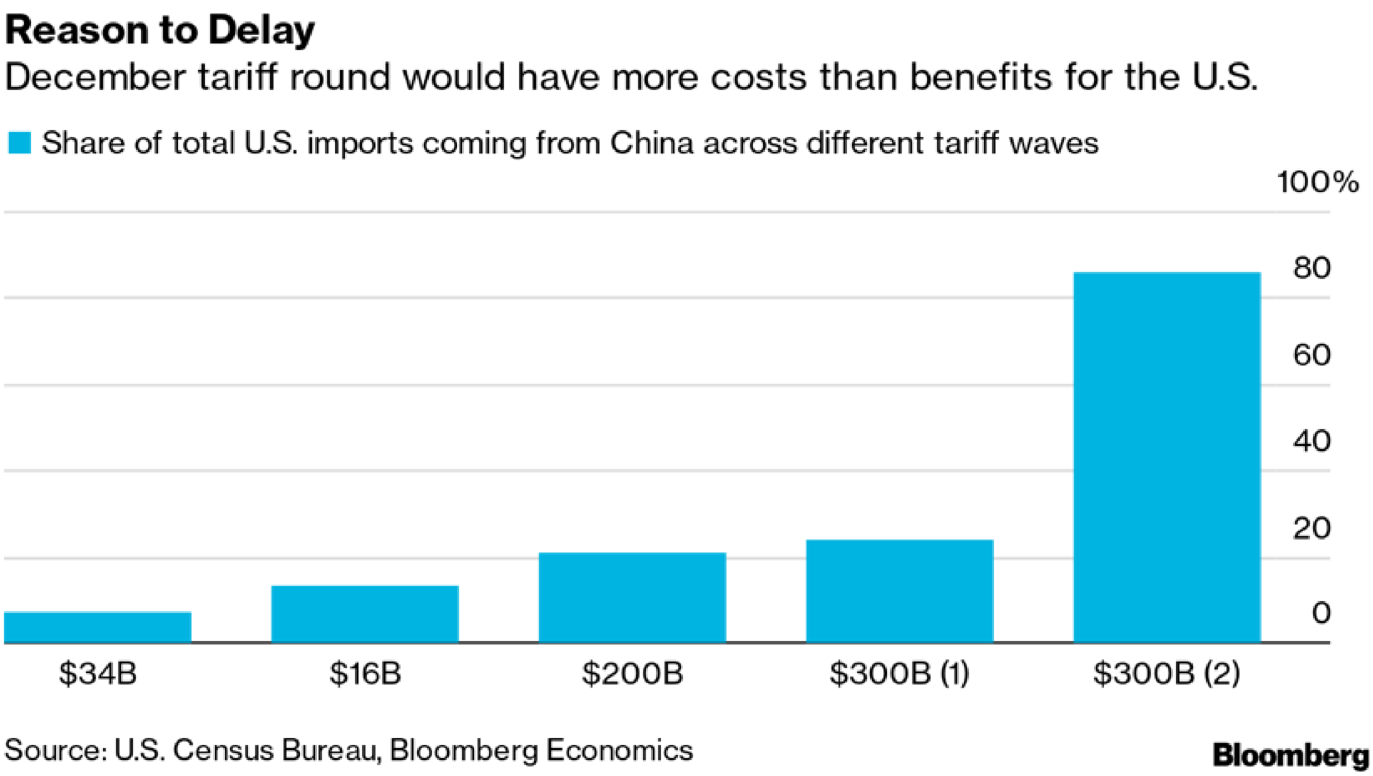
U.S. Trade Representative, Robert Lighthizer

- Chief White House economic adviser Larry Kudlow proclaimed that USMCA and China phase one deal combined should boost U.S. economic growth about a half a percentage point in 2020. "These trade deals are going to be very helpful," Kudlow said on Fox News. "They will reduce uncertainty and probably pick up some important business spending, …I would say we will do half a percent better GDP in 2020 than otherwise would have been case."

- However, the phase one deal with China is not expected to tackle deeper U.S.-raised structural policy issues, such as state subsidies, that relate to China's state-led economy model. Those issues could be tackled in future rounds of negotiations, although the path forward for those negotiations remains unclear, particularly given [statements from senior Chinese officials]() that their state-led economy is not negotiable.

- Amb. Lighthizer said there is no date to begin negotiations on a "phase two" trade deal with China, now that the first phase has been completed. Negotiations on phase two hinge in part on how well phase one is implemented, Lighthizer said Sunday on CBS's Face the Nation. Whether the phase one agreement will work ultimately will depend on who is making the decisions in China – hardliners or reformers, Lighthizer said.

- What is and was at stake on Section 301 tariffs on China? The calculated share of U.S. imports from different Trump tariff tranches against China reveal that the products under List 4b are the most impactful for U.S. consumers and importers. For the first tranche a mere 7% of the total imports came from China, allowing imports to be sourced from elsewhere, with muted disruption to the U.S. economy. For the final tranche (List 4b covering in particular consumer electronics), the share of Chinese goods is a staggering 86%, illustrating the significant potential impacts on U.S. consumers and the U.S. economy.



- In a [letter to President Trump](), dated December 12th, Senators Schumer, Wyden, and Brown implored the President to secure a strong and enforceable phase one trade deal with China. The Senators noted that, "Year after year, the United States has failed to hold the Chinese government accountable for its abusive and unfair trade practices." "Your administration must stay strong again the Chinese government if fundamental concessions are not made. Anything short of a meaningful, enforceable, and lasting agreement would be a severe loss for the American people."

U.S. - Japan Trade Agreement

- As previously reported, 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. 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 EU is considering imposing tariffs on goods from countries like the United States that have failed to match their climate change policies. The European Commission last week said that as part of its Green Deal plan, it would prepare a proposal for a border levy in 2021 for "selected sectors" to combat carbon leakage. The threat of new carbon-linked tariffs coincides with the deadlock at the U.N. climate conference on formulation of rules to govern international carbon trading. Proponents linking national markets (e.g. Europe) with other national or regional systems will soften trade tensions by encouraging countries to align their climate policies. Presently the EU levies fee of 25 euros (nearly $28) per metric ton of carbon dioxide emitted by industries like oil refineries, steelmakers and paper producers.

- USTR continued to signal the possibility of tariffs on $7.5 billion of European Union goods to 100 percent in the long-running WTO dispute over Airbus launch aid. USTR imposed initial retaliatory duties of 10 percent on large civil aircraft and 25 percent on a wide variety of EU food and alcoholic products two months ago. Amidst the potential tariff escalation, Sabine Weyand, Director General of the European Commission, last week traveled to Washington, DC for meetings with Deputy USTR Jeffrey Gerrish and other U.S. officials. The higher tariffs are permissible following the recent WTO panel ruling that the EU was still not in compliance with the Airbus ruling of illegal subsidies. 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 recent ruling. USTR issued a list of European products under consideration for up 100% tariffs. USTR is seeking comments by Jan. 13, 2020 on removal or tariff increases for products on the list.

(Sabina Weyand, Director General, European Commission)

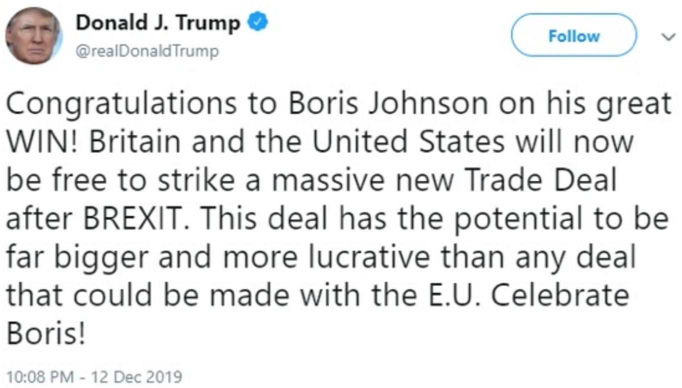
- The EU anticipates countering with its own tariffs in early 2020 when a WTO arbitrator is expected to approve retaliatory tariffs in the countersuit on Boeing for illegals subsidies.

U.S.-U.K Trade Agreement

- Brits went back to the polls last Thursday, December 12th for a general election, called for by Prime Minister (PM) Boris Johnson on October 29th in hopes that the elections would 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. PM Johnson's risk paid off, as his Conservative Party received 42.6% of the vote and now holds 365 seats in the House of Commons. With 650 seats in the House of Commons total, the Conservatives now have well over the 326 seats they need to hold a majority. The Labour Party, which planned to renegotiate the Brexit deal and hold another public vote on the deal if it won the elections, received 32.2% of the votes and slipped from holding 262 seats to 203 seats.

- Following the surprisingly strong results, Prime Minister Johnson claimed a "mandate" to accomplish Brexit: "This one nation conservative government has been given a powerful new mandate to get Brexit done and not just to get Brexit done but to unite this country."

- President Trump congratulated PM Johnson on his party's win on Thursday night and stated his continuing support for a deal between the UK and the U.S. "Britain and the United States will now be free to strike a massive new Trade Deal after BREXIT." Trump wrote.



Suspension Agreements

Sugar Suspension Agreement

- The stay granted by the Court of International Trade (CIT) for "vacating" the Sugar Suspension Agreement with Mexico expired on 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 had 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

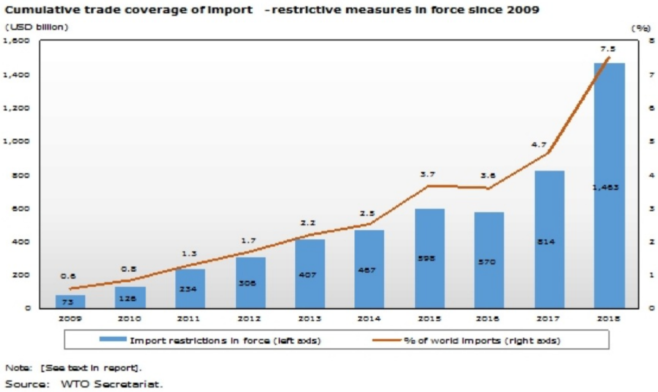
- WTO Director-General Roberto Azevêdo’s will consult with members to focus on finding the “missing pieces of the puzzle” left out of the so-called “Walker process” to address the dissolution of the Appellate Body last week, according to a recent report. Azevêdo said the Walker process addressed a “subset of issues” relating to U.S. concerns with the Appellate Body -- largely overreach and systemic problems -- noting that he would first decide whether “this understanding of mine that there are some things that are not on the table that need to be on the table” is accurate. The next phase would entail defining the concepts and framework for members to make decisions regarding a reformed or renewed AB. He expressed optimism that WTO members could make progress on resolving the crisis over the next six months, setting the stage for a decision at the June 2020 Ministerial in Kazakhstan. In the interim, Azevêdo implored members to withhold the unilateral application of trade-restrictive measures during this uncertain period. Azevêdo’s fears are not hypothetical--the EU, for example, is considering a regulation that would give the Commission the power to retaliate on trade issues without first securing WTO authorization.

(WTO Director General, Roberto Azevedo)

- The U.S. continued its objections to special and differential treatment provisions, stating that unless “certain members” forgo the use of those provisions it would not support any revisions to the present provisions. “[I]f a S&D provision is introduced in a WTO negotiation, the United States will indicate that it will not agree to that provision unless certain Members forego use of that provision,” U.S. Ambassador to the WTO Dennis Shea said at General Council meeting in Geneva last week. Shea also said that the U.S., during WTO trade policy reviews, would press countries “that we believe should not be claiming blanket S&D in future agreements.” According to the U.S., other members have asked when USTR intends to publish a list of WTO members that it does not believe should be able to access special and differential treatment. Shea said the U.S. was “consulting” on the issue but had no defined deadline.

- As reported earlier, the U.S. objects to the self-designated developing countries status provision, arguing that several large economies are avoiding the stronger commitments that would more properly reflect their economic status in the global economy. In particular, China, India, and several Latin American countries are frequently mentioned. Both Brazil and South Korea recently offered to relinquish their special and differential treatment provisions in future negotiations to appease the U.S. concerns.

- A recent WTO report revealed trade restrictions are at historic levels. Between mid-October 2018 and mid-October 2019, the amount of trade covered by import-restrictive measures imposed by WTO members was estimated at $747 billion — the highest level since 2012, and 27% higher than the prior period in 2018. The cumulative restrictive trade coverage vaulted to 7.5% of global trade or over $1.6 trillion in 2018.


Cumulative trade coverage of import -restrictive measures in force since 2009
(USD billion)
(%)
Import restrictions in force (left axis)
% of world imports (right axis)
Note: [See text in report].
Source: WTO Secretariat.