

Nafta: Is a handshake imminent?

Nafta negotiations are set to resume today between the US and Canada, with the aim of striking a deal by the end of the week. Time is running out to secure an agreement as an end-of-month deadline looms to present the text of the deal to Congress. We think a fudge is more likely than not, but will it come this week?



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Although there's an element of déjà vu here, Canada's Foreign Affairs Minister, Chrystia Freeland, has agreed to meet Robert Lighthizer, the US Trade Representative, today, with the aim of keeping Canada in the agreement. US Congress, which is in favour of Nafta, is pushing for Canada to be kept in the trilateral agreement, and the pressure is on for a new deal to be signed before Mexican President Enrique Peña Nieto leaves office in December. However, these congressional pressures haven't been sitting too well with President Trump, who has (quite directly) addressed Congress through tweets by saying, "Congress should not interfere w/ these negotiations or I will simply terminate Nafta entirely". Thoughts differ on whether this should be taken at face value or is merely a negotiating tactic.

What is keeping them from securing a deal?

Progress on the talks has picked up pace over the past few weeks. Although the two sides are

closer than they've ever been, there are still major sticking points preventing a deal being reached. One of the key points is the dispute settlement, specifically [Nafta's Chapter 19](#), which focuses on countervailing and anti-dumping duties. In short, Washington wants to scrap this completely, whilst Canada remains adamant that this is a red line it won't cross. It will be interesting to see how both parties get around this. We think the final outcome will be somewhere between the current situation and the deal recently struck between the US and Mexico, where Mexico agreed to soften the dispute settlement in a bid to please the Trump administration and strike a bilateral agreement.

There are signs that Canada may not back down on the dispute settlement issue; Canadian President Justin Trudeau recently stated that "we are going to make sure we are doing what is necessary to get the right deal for Canadians", and keeping Chapter 19 appears to be one of the necessary things. One saving grace could be Canada's dairy market. Canada has said it will offer concessions here by allowing the US limited access to the market.

Another deadline looms

A Canadian government official said a possible 'handshake deal' could come on Thursday (20 September) but Nafta deadlines have been missed in the past and there are no guarantees that an agreement will be struck by this date. That said, the White House will struggle to present the full text of the trilateral agreement to Congress by the 30 September deadline, if a deal isn't reached this week.

We see three possible outcomes from the talks:

1 A happy ever after...

A deal is reached on Thursday and Nafta remains as a three-way agreement - albeit a reworked version

2 Deal or no deal

The Thursday deadline is another false dawn and uncertainty continues to linger that Nafta could be dissolved

3 Trump vs. Congress

No deal is reached. Trump fights with Congress to withdraw from the trade deal. However, it is unclear whether the president actually has the ability to do this. Our trade team says that Trump may have the power to withdraw from trade agreements, but this is likely to be challenged in court by Congress

A waiting game

Despite the lack of clarity on Nafta, the Canadian dollar has been closely tracking the Mexican peso since early September, suggesting that a degree of optimism is being priced in. This follows President Trump's announcement of progress on a bilateral deal with Mexico in late August. Were clear signs of progress to emerge on Canada's position by 20 September, we suspect USD/CAD could trade down to the 1.27/28 region - especially given the prospect of a Bank of Canada rate hike in late October.

We do think a compromise is more likely than not; the complexity that comes with long-lasting trade agreements leaves the economies involved heavily intertwined and it's not so easy to simply 'get rid' of Nafta. In addition, Canada's high dependence on the US as an export market (the US accounted for 76% of Canadian exports in 2017) means it's probable that Canada will acquiesce to most demands coming from the US, even if this does push their limits.

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