

## Cross-Border Logistics: NAFTA tune-up time

We take a deep dive into the 23-year-old NAFTA agreement, look at the impact it has made on logistics operations in the United States, Mexico and Canada, and then hear what the experts suggest Washington should—and should not—do.

By John D. Schulz · June 2, 2017

Trucking executives, transportation officials and shippers have enjoyed 400% growth in cross-border trade since the North American Free Trade Agreement (NAFTA) (/topic/tag/NAFTA) was implemented 23 years ago. However, all three contingencies are now openly concerned about Washington making impulsive moves that could threaten the open borders that connect the United States, Canada and Mexico.

"We are going to make very big changes, or we are going to get rid of NAFTA once and for all," President Donald Trump (/topic/tag/Trump) said recently. "We cannot continue like this."

All cross-border freight transportation stakeholders are essentially begging the first-year president to find his fights elsewhere. Privately and publicly, those on the front lines of border trade are telling the administration: "Please, no major changes to NAFTA."

"I'm concerned about it because I believe in free trade," says David Congdon (<https://www.linkedin.com/in/david-congdon-b296aa27/>), vice chairman and CEO of Old Dominion Freight Line (<http://www.odfl.com/>), the nation's third-largest LTL (/topic/tag/LTL) carrier. "Global trade is a reality of life these days. The United States is a consuming nation; and yes, a lot of our manufacturing has moved offshore and we import a lot. However, if you start putting a tax on products that U.S. consumers are buying, that's not good."

According to Congdon, what could hurt logistics and transportation companies would be a general decline in the U.S. economy. For instance, Trump's proposed "border adjustment tax" could raise costs for consumers and put a damper on spending—and thus slowing the economy. Yet, that's exactly what the fledgling Trump administration is considering.

Whether it's called a "border tax" or an "import tax," logisticians say it's a bad idea, and one that could harm long-standing relationships between two of our largest trading partners: Canada and Mexico. To top it off, President Trump's harsh rhetoric toward Mexico during his campaign and presidency has not helped relationships with our southern neighbor.

In the meantime, trade and tax experts say that Trump doesn't, or can't, distinguish between a "border adjustment tax" that affects all industry and "individual trade sanctions" that he would like to apply on a company-by-company basis. At this point, it appears that Trump believes that his tax proposal would essentially utilize a border tax as if it were a trade sanction—which it's not.

"Any way you consider it, NAFTA has been a phenomenal advantage to both the United States and Canada," says John Costanzo (<https://www.purolator.com/en/resources-and-support/about-us/governance/executive-team/john-t-costanzo.page>), president of Purolator International, a subsidiary of Purolator Inc. (<https://www.purolator.com/purolator/home.page?>) in Canada and the largest parcel delivery service in the country. While noting some manufacturing jobs have left the United States, they did not go to Canada—most went overseas because of lower wages.

"NAFTA's elimination of tariffs has enabled the United States to become more efficient in its exports," says Costanzo. "And if we didn't have NAFTA, we'd have to create something like it, otherwise we're giving up manufacturing to other countries. It's been a tremendous asset to both the United States and Canada, and I don't see it going away."

Whether Trump knows it or not, the 23-year-old NAFTA is an extremely complex document that affects mightily the economies of three nations, is politically and legally complicated, and fraught with minutiae and fine print legalities that the president probably knows little or nothing about.

Julie Gibbs (<https://www.linkedin.com/in/julie-gibbs-11a8a86/>), director of BPE Global, a global trade compliance consulting firm, called NAFTA "the largest free-trade agreement in the world" that has quadrupled the trade among the three countries.

"The agreement is not trivial in its impact and would be extremely difficult to detangle or revoke," says Gibbs, adding that whether it could be revised in one easy-to-do swoop is probably unlikely. As with Trump's non-existent repeal of the Affordable Care Act, it's highly possible that the president would just give up first before any hard revisions—which is actually what most



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logisticians are fearing most.

The North American free trade market is working extraordinarily well, they say, and even a whisper of major change hurts the marketplace. “As a rookie president, Trump has shown intolerance of delays and compromise,” says Gibbs. “And it’s highly likely that Trump will tire of renegotiation of NAFTA.”

Now, let’s take a deep dive into the 23-year-old NAFTA agreement, look at the impact on logistics operations on all sides of the border, and then we’ll hear what the experts are saying Washington should—and should not—do.

## NAFTA: Size and scope

First, let’s look at the North American market, NAFTA’s impact on the U.S. economy and its enormous scope. Total value of cross-border freight among the three NAFTA countries and carried on all modes—truck, pipeline, vessel and air—fell 3.4% from 2015 to \$1.069 trillion in 2016. Trucks carried 65.5% of U.S./NAFTA freight, the most heavily utilized mode for moving goods.

Mexico exports about \$1 billion worth of goods per day to the United States, making it the single largest source of imports and its third-largest trading partner. According to the Wilson Center, a Washington research center and think tank, 25 cents out of every dollar of goods that are imported from Canada to the United States is actually “Made in USA” content, as are 40 cents out of every dollar for goods imported into the United States from Mexico.

Even though trucking hauled slightly less U.S. freight to Canada and Mexico in 2016 than 2015, the Department of Transportation’s Bureau of Transportation Statistics (<https://www.bts.gov/>) own numbers show that still results in an enormous amount of freight between the three NAFTA countries.

Value of U.S.-Canada freight flows fell 5.4% to \$544 billion in 2016. Trucks carried 60.1% of the value of the freight to and from Canada, followed by rail at 16.2%. The top commodity transported between the United States and Canada in 2016 was vehicles and parts at \$106.1 billion, with trucks moving 56.4% of the value.

In the meantime, the value of U.S./Mexico freight fell 1.1% to \$525.1 billion last year. Trucks carried 71% of the value of the freight to and from Mexico, followed by rail at 14.7%. The top commodity transported between the United States and Mexico in 2016 was electrical machinery at \$102.6 billion, with trucks hauling 91.6% of the value.

However, it’s not just raw materials and finished goods coming to and from this country. A sizeable chunk of the American economy depends on exports. And even if the nation runs a deficit in trade, no less an authority than the U.S. Chamber of Commerce says that’s not necessarily a bad thing.

“While trade deficits often don’t tell us much about the overall health of our economy, it is a good time to examine our various trading relationships to increase opportunities for American companies to compete on a level playing field,” says the U.S. Chamber of Commerce (<https://www.uschamber.com/>) president and CEO Thomas Donohue (<https://www.uschamber.com/thomas-j-donohue>). “It is worth remembering that some of our best years of economic growth have produced our largest trade deficits, while the Great Recession was accompanied by a sharp reduction in the trade deficit.”

According to Donohue, the Chamber is supporting strong enforcement of trade rules and agreements “as long as such enforcement is based on facts and the proper interpretation of those facts and not politics.”

According to the Department of Commerce, U.S. exports of goods and services to Canada supported an estimated 1.7 million jobs in 2014 (latest data available) with 1.3 million supported by goods exports and 394,000 supported by services exports.

U.S. goods and services trade with Canada totaled an estimated \$662.7 billion in 2015. Exports were \$337.3 billion; imports were \$325.4 billion; and the U.S. goods and services trade surplus with Canada was \$11.9 billion in 2015.

Whatever the precise numbers, U.S. transport executives say that the export market is a solid, growing, reliable part of their businesses. It’s a market that is to be cultivated—not curtailed by some arbitrarily written border tax.

“I believe whatever the taxing mechanisms are, they ought to be fair and balanced,” says Old Dominion’s Congdon. “I’m for that. I know how much freight we haul to the Mexico border and how much we haul back and forth to Canada, and it’s good business. The North American markets are good to us, and I don’t want to see our levels of business disturbed. We have to be fair and rational.”

## So what should be done?

Reminiscing on NAFTA’s early days, many may recall 1992 presidential candidate Ross Perot’s reference to NAFTA as a “giant sucking sound going South.” More than 20 years later, some still argue that NAFTA drove U.S. jobs south; but at the same time, others argue that jobs lost over this period would probably have gone to China or elsewhere anyway.

“What we can say is that NAFTA fundamentally reshaped North American economic relations, driving unprecedented integration between Canada, the United States and Mexico,” says BPE Global’s Gibbs.

But as in any healthy evolution, Gibbs says that there are always improvements to be made. Indeed, she believes that a 21st century overhaul to address data flow, a concept that wasn’t around in the 1990s, would be an important tweak to the agreement as would a look at the accounting for the online retail market to ensure that the complex rules of origin are fair across the three countries.



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The Trump administration shared their NAFTA draft proposal last month, and it's much less forceful than what candidate Trump was offering. Fortunately, there's no threat of withdrawal. Included are specific provisions for "snapback," market opportunities specific toward "domestic procurement," and a leveling of the tax playing field.

"All in all, these are elements that are in line with a much needed overhaul to the program," says Gibbs. "It will be interesting to watch these provisions manifest against the administration's protectionist stance."

Nevertheless, Gibbs adds that there will "undoubtedly" be changes. "The level of impact will depend on what Trump can push through. NAFTA is a big concern because of the immediate impact to U.S. jobs and the economy," she says.

President Trump has announced his intention to renegotiate at this point. Some changes being mulled include: Temporarily reinstating tariffs if a flood of imports causes serious injury to domestic industries; improving procedures to resolve disputes; and employing tougher intellectual property enforcement.

However, experts contend that the logistics and transportation markets shouldn't panic over Trump's rhetoric. Under the Constitution's Commerce Clause, only Congress may alter our tariff, tax and Customs laws.

According to Gibbs, U.S. companies should lobby Congress to protect themselves from losing this benefit by quantifying what the loss of NAFTA savings would mean to them in terms of tariff costs and global supply chain modifications. "Companies should also share this data with Congress to avoid a devastating impact to the U.S. manufacturing sector," she says.

Purolator's Costanzo adds that post-NAFTA trade harmonization rules have made exporting much simpler. "It's night and day," he says. "Pre-NAFTA, U.S. companies used to dread selling to Canadian customers. And while there's still complexity, if you do the setup correctly, it's seamless and relatively easy."

The state of the fast-growing B2B and retail e-commerce is another changing dynamic, adds Costanzo. E-commerce economics are very different than brick-and-mortar business, but he adds that only further strengthens the case to fine-tune—not trash—NAFTA.

"We've heard this rhetoric before," says Costanzo. We had 'Buy America' back in the 90s, and this too shall pass. The United States relies so heavily on exports and imports. In fact, we sell \$300 billion of goods to Canada, so we can't jeopardize those supply chain efficiencies. Eventually, I think that cooler heads will prevail."

## About the Author

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John D. Schulz has been a transportation journalist for more than 20 years, specializing in the trucking industry. John is on a first-name basis with scores of top-level trucking executives who are able to give shippers their latest insights on the industry on a regular basis.

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