POLICY PERSPECTIVES

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ASSESSING THE NEW US ADMINISTRATIONS'S IMPACT ON BC'S NATURAL RESOURCE INDUSTRIES

When trying to answer a big question without much information, it is tempting to assign great significance to the few facts that can be found. So it is with Donald Trump and the Republican Congress that will be sworn in next year.

The Economist, November 19, 2016

HIGHLIGHTS

- While the flurry of tweets and new Executive Orders are beginning to outline the preferences and direction of the Trump Administration in some areas, the remaining gaps make it risky to predict how the Administration will handle any number of files affecting BC's natural resource sectors.
- Since there are few reliable signals about how the Trump Administration will address continental trade in resources/commodities, BC resource firms can prepare by developing two (or more) scenarios to guide actions and responses based on whatever may affect them: "Trump Lite" and "Trump Heavy" scenarios are presented and applied briefly to key BC resource sectors.
- *Caution: The Present is No Guide to the Future*. Of the four trade disputes or irritants presently between Canada and the US, recent moves should not be relied on to predict how the Department of Commerce or Office of the US Trade Representative will act in coming months and years.
- The new protectionism in the US will likely bring on NAFTA 2.0 and Buy American 2.0. Despite this, it doesn't have to be all bad for BC or Canada. However, BC's continuing reliance on the US as our principal goods export market leaves our resource sectors at some risk in the event that a "Trump Heavy" Administration pursues a strongly protectionist agenda over the next four years.

HOW/WHETHER TO CRYSTAL BALL?

The period from US Election Day to Inauguration Day – and beyond – was unusually dramatic: by turns entertaining, encouraging and alarming, depending on where you stand. The election campaign itself offered virtually no policy insight, and more recent statements – the new President's inaugural speech, ongoing tweets, and the flurry of Executive Orders – are only beginning to outline the preferences and direction of the Trump Administration. While clarity of direction – if not coherence of policy – is now evident in some areas, the remaining gaps make it risky to predict how the Administration will handle any number of files affecting BC's natural resource sectors. We just don't and won't know what the Trump Administration will do on several important trade and resource policy matters until cabinet confirmations are complete and the offices critical to the US-Canada relationship are staffed. It will take time to evolve from often vague campaign promises to actual policies and then to actions.[1] In short, the crystal ball remains cloudy.

What the US Administration does on trade, energy and environmental

[1] While outside the scope of this discussion, the incoming Administration's corporate tax policy could have a substantial impact on Canadian business, which in turn could affect BC's resource sectors.

policy matters to BC's natural resource sectors, and to the overall health of our economy. BC shipped nearly $1.8 billion worth of goods exports to the US in the single month of November 2016, a 20% increase over November 2015. Year to date exports (January - November 2016) were $19.3 billion, up 11% over the same period in 2015. As a share of BC's merchandise exports to all destinations, the US was tracking higher in 2016 (54.5%) than for all of 2015 (52.2%). In this unusual commodity cycle, certain segments are up, while others are flat or down.

TABLE 1: **SELECT BC COMMODITY EXPORTS TO US, YEAR TO DATE (JAN-NOV) 2015-2016**

Product	2015 (C$ millions)	2016 (C$ millions)	% Change
Solid Wood Products	4,517	5,914	+30.9
Pulp and Paper	1,110	926	-16.6
Energy	2,559	2,888	+12.8
Metallic Minerals	1,005	1,319	+31.3
Agricultural (other than fish)	1,740	1,813	+4.2
Fish/Fish Products	631	718	+13.8
Machinery & Equipment*	2,967	2,857	-3.7

* Machinery & Equipment is not considered a natural resource product, but the category is included here to inform the protectionism discussion below.

Source: BC Stats.

Unpacking a few of the broad categories: in solid wood, exports of lumber and finished wood products are up, but logs are down; in pulp and paper, all products are down; in energy, natural gas is up and coal doubled (from a very low base), while electricity is down; in metallic minerals, unwrought aluminum and unwrought lead are up, all others are down; and in agricultural goods, vegetable oils are down, meats, breads and vegetables are up, as are fish products.

Caution: The Present is No Guide to the Future. There are at least four trade irritants or disputes presently being negotiated or adjudicated between Canada and the US, all of which relate to natural resources. These include: super-calendared paper (pulp & paper), softwood lumber, drywall/gypsum, and wine. The US has brought three of the four actions: paper, lumber and most recently wine, in the final days of the Obama Administration. Meanwhile, in September 2016, Canada imposed anti-dumping duties on US drywall imports into the western provinces.

Each of these trade disputes is at different stages. But recent moves (and some findings favourable to BC - Catalyst Paper in the case of supercalendared paper) should not be relied on to predict how the Department of Commerce or Office of the US Trade Representative will act in coming months and years. President Trump's Cabinet nominations have been made, offering some (possibly contradictory) clues as to the stance of the Administration on trade issues. Specifically, Wilbur Ross, the nominee for Secretary of Commerce, is said to hold pro-trade views, but he has also criticized NAFTA and the WTO as offering too few trade protections for American companies and workers. Robert Lighthizer, the nominee for US Trade Representative, is believed to hold similar views.

SCENARIOS

Since there are so few reliable signals about how the Trump Administration will address trade, or US domestic policy that will affect trade in resources/commodities, BC resource firms with exposure to the huge American market can prepare for the possible impacts by developing two (or more) scenarios to guide actions and responses – and recalibrations – based on whatever may directly or indirectly affect them. Scenarios may be developed that have the following general contours:

"Trump Lite" – this assumes the Trump Administration moderates its positions from those expressed on the campaign trail, and/or that the influence of Cabinet and the legislative branch of the US government are brought to bear. This means the executive branch does less to upset the architecture

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of international relations and trade agreements and behaves in a less protectionist manner than many fear.

"Trump Heavy" – the new Administration remains unshackled from America's traditional commitments and approaches to the existing international order (geopolitically), is happy to destabilize trade relationships and undermine existing global trade norms and rules, and acts aggressively in line with the sharp protectionist rhetoric expressed during and since the campaign.

KEY BC RESOURCE SECTORS

Forestry

Softwood lumber of course cannot be ignored, but is in some ways a special case. The launch of trade action against the Canadian softwood lumber industry will likely result in similar response strategies as have played out in prior disputes ("Lumber I" through "Lumber IV") – a combination of litigation and negotiation. Countervailing duties (CVDs)[2] of around 30% or higher are thought by forest industry analysts to underpin the US industry's petition to the Department of Commerce. If USTR proceeds with a high CVD, it may signal the Administration's desire for a quick win under a Trump Heavy scenario. However, the history of lengthy litigation, and the survival of the Canadian industry in the face of countervailing and anti-dumping duties in previous disputes, suggests a quick win is not likely – even with a heavy approach to softwood lumber. In other words, the special case of softwood may be an example of history being a guide to the future.

Traditional Energy

The new Administration's expected policies on energy raise a number of questions for BC's energy sector: exports of fossil fuels to the US from BC/western Canada could face a rough ride under a Trump Heavy scenario if the US strongly encourages the expansion of domestic hydrocarbon supply, particularly shale oil and gas which suffered during the global price depression of the past two years. Still, under a Trump Heavy scenario, BC/western Canadian oil and gas producers could do well if US oil imports from overseas are constrained, and if Canada is viewed neutrally or favourably by the Administration as a reliable and "friendly" supplier. The makeup of the Trump Cabinet is likely to be influential here, as the nominees for Secretary of State (Rex Tillerson) and Secretary of Energy (Rick Perry) have more than a passing knowledge of the North American oil industry.

A Trump Lite scenario would be more likely to pay close attention to continental energy flows, taking account of the efficiencies offered by continuing integration of North America's oil and gas sectors. In either scenario, recent Executive Orders suggest the new Administration, in sharp contrast to its predecessor, is keen to see the construction of energy infrastructure between Canada and the United States. This is welcome news for western Canada's energy industry. However, even with a resurgent US economy it is hard to see Canadian gas regaining its previous state-side market share in light of growing US shale production and ever expanding reserves. Bitumen exports, on the other hand, seem set to increase from western Canada to feed the eight million barrels per day of heavy crude capacity in the Gulf Coast refinery complex.

Renewable Energy

The new Administration's statements on climate change signal that its stance will complicate Canadian climate policies: the blueprint

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[2] There is some chance that anti-dumping duties may also be part of the overall penalty imposed on lumber imports from Canada.

announced at the "Three Amigos" Summit in mid-2016 for cooperation on advancing renewables and improving efficiency will likely be one casualty. In terms of the business prospects for renewable energy (including the hydroelectricity presently traded around the Western Electricity Coordinating Council (WECC) region), it is difficult to see, under either a Trump Heavy or Trump Lite scenario, a substantial change in renewable energy trade with the western states from a BC perspective. Renewable Portfolio Standards are state-governed, and any federal change – even overturning Obama's signature Clean Power Plan and/or the elimination of federal Production Tax Credits for wind power – would not affect the authority of states to implement their own standards. The magnitude of BC electricity exports in the coming 3-5 years is likely to reflect economic activity and demand/supply fluctuations in the Western US rather than measures taken by the Trump Administration.

Mining

The metals and minerals sector in BC could also see an impact from the new Administration's trade policies, most likely due to possible new "Buy American" policies. It is difficult to see policy-driven shifts resulting in substantial positive or negative implications for metal/mineral exports to the United States under a Trump Lite scenario. One possible exception is a lift in demand and prices if a mooted US$1 trillion infrastructure program proceeds – without too many Buy American strings attached. Under a more protectionist Trump Heavy scenario, BC-origin input goods (if made from Canadian-origin raw materials), could be subject to non-tariff barriers if new Buy American legislation is aimed at boosting US-origin products in federally funded public infrastructure projects.

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Agriculture

The agriculture sector is a bright light in BC's export picture, growing rapidly in recent years. About two-thirds of BC agriculture exports (including fish/fish products) are shipped to the US, aided in part by the competitive exchange rate. Most agricultural exports to the US are covered by the North American Free Trade Agreement (NAFTA), meaning tariff-free exports of most products. The exceptions include the Canadian supply-managed sectors, including poultry and dairy. Under a Trump Heavy scenario, we would expect USTR's (and possibly Congress's) sights to be set on the supply management regimes of Mexican and Canadian dairy industries. The past may be a guide to the future in one tactic: the recently averted trade dispute over the labelling of meat exports from Canada to the US (invoked then repealed in late 2015 by Congress under Country of Origin Labelling "COOL" legislation, a behind-the-wall tariff barrier). Under either a Trump Heavy or Trump Lite scenario, particularly given the make-up of the new Congress and the enduring power of the US Department of Agriculture, such legislative tactics may again be deployed in respect of British Columbia/Canadian exports of agricultural products.

WHAT FORMS WILL RENEWED US PROTECTIONISM TAKE?

NAFTA 2.0?

The most likely development impinging on the Canada-US trading relationship under the Trump Administration is the re-negotiation (or "tweaking," as Canadian Ambassador David McNaughton has put it) of NAFTA. This will of course directly affect all sectors of the BC economy covered by NAFTA. Is this necessarily a bad thing for Canada? Maybe... but maybe not, if the country is clear in its goals for a revised NAFTA, and skilful in its negotiations. It is unlikely, as some have proposed, that softwood lumber will be wrapped into NAFTA; similarly it is difficult to see other "managed" trade sectors included. But the addition of some 21st century trade deal elements (such as: improved dispute resolution mechanism, expanded procurement guidelines, strengthened harmonisation of performance/ production/ environmental standards to reduce "behind the wall" trade barriers, etc.) could benefit BC-origin resource products bound for the US. Also relevant, the Chapter 11 investorstate dispute settlement mechanism could be in line for significant change, given the negative comments that have been made about it by Mr. Trump and others in the Administration.

Buy American 2.0?

The US$1 trillion infrastructure spending program promised by the new Administration – Congress has yet to pronounce on the idea and ultimately it will control the purse strings -- could spell another round of "Buy American" policies that threaten Canadian firms' access to US procurement markets.[3] The previous "Buy American" provisions in the American Recovery and Reinvestment Act (2009) were not aimed at inputs or raw materials; rather, they required that finished goods be completed in the United States. This was still problematic in terms of the ability for Canadian firms to bid on sub-national procurement in the United States. The resulting 2010 Government Procurement Agreement affirmed the ability of Canadian suppliers to continue to bid on and win contracts on US state and municipal infrastructure projects.

Here again, the present may be no guide to the future. A Trump Heavy Buy American policy could well compromise the integrated supply chains that exist for many infrastructure projects. This hurts BC's energy and extractive industries to the extent that raw materials and input goods flow south, as they effectively are shut out of opportunities to provide materials and possibly related services linked to new American infrastructure projects. At this point we don't know how US procurement policy will play out in the era of Trump, but on the omens aren't particularly encouraging.

All in all, it is sobering times for BC's resource sectors, and the US election outcome is merely the most recent, albeit a large, potential stumbling block to the further expansion of our resource industries. This brief review has suggested that it doesn't have to be all bad for BC or Canada, but the reality is that BC's continuing reliance on the US as our principal goods export market leaves our resource sectors at some risk in the event that a Trump Heavy Administration ends up pursuing a strongly protectionist agenda over the next few years.

A previous version of this article appeared as a blog post for Resource Works in December 2016.

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[3] Thus potentially jeopardizing some of the $2.8 billion in machinery and equipment exports from BC to the US in the first 11 months of 2016.