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Canada-EU Free Trade: A Building Block for Renewed Multilateralism

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Summary

Canada has long been interested in enhancing trade and investment links with the European Union, but the EU has resisted the idea of free trade with Canada, preferring to support the multilateral system. Now, with the suspension of the Doha Round of WTO trade talks, Brussels is reconsidering its stance, and preparations for EU-Canada trade negotiations are expected to follow French president Nicolas Sarkozy's upcoming Canadian visit. Such negotiations would present considerable challenges, including the need to remove nontariff barriers to trade, especially in services and agriculture. However, an EU-Canada agreement, in addition to obvious bilateral benefits, would also demonstrate the North Atlantic community's united front in future multilateral negotiations.

There is nothing new about Canadian efforts to strengthen transatlantic economic ties. Following Confederation, trade policy concentrated upon the reduction or even elimination of tariffs with European nations (France and Spain, in particular). With free- trade Britain, the route was paradoxically more difficult. Imperial enthusiasts repeatedly sought greater unity of the Empire and common economic benefit in an imperial tariff preference. But that was only possible if Britain placed highly unpopular duties on imported goods so as to be able to create, in turn, a tariff preference for food from the Empire. And the Dominions for their part were opposed to a tariff preference for manufactured imports from Britain that competed with domestic products. Incredibly, as late as the 1960s, a British offer of bilateral free trade was declined by Ottawa, largely at the prompting of the timid Canadian Manufacturers Association, which remained ever fearful of the competition of British manufacturers.

Following the lack of interest in a protectionist-minded Washington in a broad trade negotiation, the near debacle of the 1932 Imperial Economic Conference in Ottawa, seen by some as providing economic underpinning for the Statute of Westminster, did, largely at Britain's expense, achieve imperial tariff preference of sorts, toward which the United States was immediately hostile. In the case of Canada, nonetheless, Washington did win improved access as a result of a 1938 agreement. During the Second World War, having failed in the immediate pre-war years — in the words of the then US secretary of state — in "the chipping off of the structure of imperial preference," the United States made it a condition of its wartime supplies to a beleaguered Britain that imperial tariffs be abolished. That, too, did not work, so in 1948 Washington sounded out Ottawa on bilateral free trade as another means of breaking the imperial preference. Prime Minister Mackenzie King was wary, specifying, inter alia, that "the United Kingdom [should be added] to such discussions." Washington did not respond.

Ottawa was convinced that transatlantic trade liberalization was the most immediate way — when matched by the Marshall Plan — out of the economic and social mess left by the Second World War. In early 1948, as an alternative to what Mackenzie King feared was a dangerous political move into continentalism, Ottawa proposed that transatlantic economic ties be embedded in the draft North Atlantic Treaty, thereby making more than merely a military response to the mounting threat of the Soviet Union. Mackenzie King declared that "trade proposals might be made to fit…into the larger Atlantic Security Pact….[W]e might immediately follow thereafter with…the removal of restrictions to trade within the area." This bold Canadian proposal, although finally accepted by the signatories, was never implemented. In light of the eagerness in Washington and in European capitals to get on with military collaboration, the complicating "Canadian article" was much diluted and incorporated in the draft treaty only when it had been reduced to "[member states] will encourage economic co-operation between any and all of them."

Article 2 — the economic article — of the North Atlantic Treaty was a dead letter from the beginning and has remained so for 60 years. Yet NATO would have been a more coherent, although necessarily more complex, organization if transatlantic economic as well as military cooperation had been sought from the beginning. Intra-European economic cooperation, including the dismantling of trade barriers, as distinct from transatlantic cooperation, then received priority, fostered by the Marshall Plan. Eventually, the result was the near miracle of the European Union (having had its beginnings in the several agreements of the 1950s), but also a failure to strengthen transatlantic ties, except for the largely inconsequential creation of the Organisation for European Economic Co-operation (later the Organisation for Economic Co-operation and Development, OECD) and the more promising multilateral General Agreement on Tariffs and Trade (GATT).

Although fully playing its part in NATO with forces in western Europe, Canada continued to yearn for more in the way of transatlantic ties. In 1958, Canada was the first country outside Europe to appoint an envoy to the then fledgling European Economic Community. In 1967, Lester Pearson, reflecting a growing concern about Canada's increasing dependency on a single market — the United States — called for more intensive efforts to develop transatlantic trade and investment. "It is not a very comforting thought…when you have sixty percent or so of your trade with one country; you are in a position of considerable economic dependency." The GATT had succeeded in reducing trade barriers across the non-communist world, but Canada's dependence on a single market had only increased. Four years later, in a quest for trade diversification, Pierre Trudeau identified a "third option" in Canada's international economic relations: while continuing to pursue trade interests multilaterally in the GATT and lessening its dependence on bilateral trade with the United States, it should pursue policies that would enhance Canadian self-reliance. In 1976 Canada became the first non-European nation to conclude a "contractual link" with the European Economic Community, but little resulted. Exhortatory declarations followed in 1990 and 1996.

All such initiatives — and they were Canadian, not European — were fuelled in part by a recognition that western Europe was integrating, having learned that an economic architecture can provide the girders for a larger political purpose and wider global influence. Much later than western Europe, North American economic collaboration — beyond the GATT — eventually took a different form, limited to free trade among three member states that certainly did not seek in the North American Free Trade Agreement (NAFTA) the political integration that has been a European goal.

Paradoxically, the risk of regionalism on both sides of the Atlantic, however different, has at one and the same time both simplified and complicated transatlantic thinking. On the one hand, Europe and North America were pioneers in pursuing deeper global economic cooperation. In principle, their regional structures, although differing widely, could have provided logical building blocks for an ambitious economic bridge across the Atlantic. On the other hand, the creation of the European Union and NAFTA tended to make both regions more inwardly focused, exaggerating rather than reducing, transatlantic differences.

As transatlantic trade and investment flows increased, underlying structural or "systemic" differences between Europe and North America emerged. Disputes that were once confined largely to agricultural and industrial trade have more recently encompassed issues as diverse as competition law, taxation, technology policy, government procurement, environmental protection, labelling requirements, investment restrictions, health and safety standards, intellectual property, and personal privacy. Unlike the sources of traditional trade disputes, these issues are neither primarily economic nor international in nature. Instead, they involve domestic policies and priorities, reflecting the way that separate legal, regulatory, and even cultural systems have evolved on both sides of the Atlantic. Policymakers in these specific areas operate under mandates very different from those governing trade negotiators: the former respond to different problems, the latter respond to different constituencies — their priorities do not involve trade or investment liberalization; indeed, their constituencies may resist all such initiatives.

Against the background of transatlantic differences, the EU Commission in Brussels carved out access to various markets through regional free trade agreements (all duly endorsed by the GATT). Indeed, the proliferation of such EU free trade agreements has become so global that the term regional is almost superfluous. They have been driven in part by a perceived need to counterbalance US bilateral trade forays.

For its part, for more than three decades Washington viewed open world trade as both in its national interest and as a cornerstone of the post-war international order, initially to rebuild prosperity and stability in Europe and Asia, and subsequently to secure democracy against communist expansion. With the first of Nixon's protectionist measures of 1971 and the later fall of the Berlin Wall, however, this rationale for multilateralism weakened. The free trade coalition in the United States eroded in the face of concerns that Japan and Europe and, more recently, China and India were free-riding on the openness of US markets. Meanwhile, a parallel concern about declining US competitiveness put a new emphasis on full reciprocity in trade negotiations. Both trends have led to a less pronounced US commitment to multilateralism exclusively. Although Washington supported the successful completion of the Uruguay Round of the GATT in 1994, US trade policy since then has focused increasingly on bilateral and regional initiatives. Many of these initiatives were influenced by a desire to respond to commercial competition from Europe and to counter the EU's growing power as a regional trade bloc. Indeed, the Canada-US free trade agreement and the subsequent NAFTA were driven at least in part by concerns about trade diversion arising from EU expansion, as well as by its foot-dragging in the GATT.

More recently, as China and India have merged as major trading partners, Brussels and Washington have each sought additional free trade agreements with other countries, mainly developing. It is generally acknowledged that this expanding web of bilateral and regional free trade agreements can benefit the partners involved (why else would they join?). But, from a wider perspective, the proliferation of free trade agreements also reflects a worrying fragmentation of the global trading system and a concern that preferential blocs can beget greater geopolitical rivalry and instability. The transatlantic powers created the multilateral trading system in the immediate post-war era precisely to avoid a return to a world of divisive trading blocs. In something of the same way, the recent weakening of support for multilateralism is at least partly a reflection of the breakdown of transatlantic consensus. It illustrates why transatlantic economic discord matters, not just because of the economic costs, but because it can have repercussions that extend well beyond its effects on bilateral trade, spilling over into other aspects of the relationship and generating wider geopolitical instability.

Multilateral trade liberalization did, however, achieve a victory in the successful conclusion in 1994 of the long-standing and hard-fought Uruguay Round of the GATT. Its most remarkable achievement was the creation of a true World Trade Organization (WTO), which the United States had opposed as early as 1948. Residual industrial tariffs were reduced or even eliminated, progress, however modest, was made in agricultural trade, and a start was made on dealing with new trade issues of a decidedly domestic character. But that victory was short lived. Instead of allowing members states to digest the heartening results of the Uruguay Round — a major adaptation for many to make — another round was launched too soon, despite the immediate misgivings of many developing countries.

That the Doha Round was launched prematurely is now incontrovertible. The new WTO had no time to consolidate or to adapt to the membership of China. There were no pressing trade and investment issues calling for immediate resolution. In fact, the round was hurriedly launched by the United States in an ill-considered effort to display global unity in the wake of the divisive terrorist attacks of 9/11.

Further, the initiative was marred by being named the "Doha Development Round," as distinct from a traditional trade negotiation round based upon the fundamental principles of "most favoured nation." Without waiting for the negotiation of the new round — if such there were ever to be — many developing countries expressed skepticism about the timing of the initiative by redoubling their efforts to conclude amongst themselves a range of bilateral and multilateral agreements and policy collaboration.

They were not alone in their wariness to put all their trade liberalization eggs in the now uncertain multilateral basket. The United States, the European Union, Australia, Canada, and Japan — staunch multilateralists of the past — all sought or concluded bilateral agreements with a range of developing countries, although noticeably not Europe and North America with each other.

Skepticism about the multilateral Doha Development Round had spread widely long before it ground to a halt in July 2008. Theoretically, the round could be revived sometime in 2010 or beyond, but the immediate prospect is that the move toward bilateral and regional agreements will accelerate, and the multilateral forum will need to be content to be their monitor and the resort for the settlement of trade disputes (a lesser but certainly not necessarily ignominious role for the beleaguered WTO, if carried out rigorously).

The Doha Development Round came to a halt ostensibly over the opposition of India and China to any agreement that did not permit them to introduce special measures to protect their farmers in the event of a "surge" in imported foodstuffs. But that specific issue masked a complex host of other unresolved and never lapidary issues. More important, it confirmed the arrival on the world stage (for which the WTO was woefully unprepared) of China and India as decisive players in the new world order.

For at least three decades following the Second World War, the GATT was basically a transatlantic negotiating forum. Its membership was much smaller than that of the WTO today — just 23 countries in 1948 — and US-European leadership was unquestioned. GATT rounds typically took the form of US-European negotiations, the outcome of which was then "multilateralized" for the benefit of other contracting parties.

No more. With the creation of the WTO — the first new international institution of the Cold War era — the multilateral trading system was transformed from a club of the industrialized West to a truly global institution. With the implosion of the Soviet bloc and the policy shift, however uneven, in the developing world toward open markets and trade, the active membership of the multilateral trading system has rapidly mounted. The new WTO has 150 members, three-quarters of which are developing countries or economies in transition. The range of its policy interests has expanded in tandem with the expansion of its membership. That spectrum ranges from least-developed countries experiencing great difficulties just living up to their Uruguay Round commitments, to advanced economies pushing for "WTO-plus" — for new rules-making in complex policy areas such as trade in services, investment rules, global mergers and acquisitions, intellectual property protection, and the growing interface between international business and environmental law — an approach seen as an answer to those who contend that no ship must move faster than the convoy. Additionally, China's accession to the WTO marked a profound shift, fundamentally altering the developing/industrialized country balance and adding a new dimension of complexity to the management of an already delicate, technology-driven multilateral system. Some now wonder whether a system as universal and as intricate as the WTO can move forward in anything but incremental steps. Grand negotiating rounds may have become a thing of the past.

During seven years of debate in the WTO about a Doha Development Round, the substantive policy differences between North and South, developed and developing, did not narrow; indeed, on some issues, positions actually widened. This is not the place to analyze those differences. It is, however, now evident that the WTO system, however central to European and North American thinking, can no longer provide the only policy and legal instruments for managing transatlantic economic relations. The diversity of the WTO is too broad, its rules too shallow, and the pace of its negotiations too slow, all problems that emerged as the Doha Development Round dragged on.

The debate now is not whether the WTO should be the most important instrument for managing international economic relations, including transatlantic, but whether it should be the only instrument. Not surprisingly, some have taken the troubles that have beset the Doha Development Round as a reason to pursue routes additional to the WTO to liberalize trade and investment. In their view, one size does not fit all. The WTO membership of 150 is now so diverse that it can no longer be squeezed into the same box of global trade rules, especially when the remaining major obstacles to liberalized trade are mainly domestic regulation, rather than old-style tariffs at borders.

What, in these circumstances, should Canada, in trade policy terms, do now? It should begin by phasing out its own pedestrian-sounding but fundamentally protectionist agricultural policy, as Australia and New Zealand have so successfully done. "Supply management" in the dairy and poultry industries - has prevented Canada from playing any leading or creative role in multilateral trade negotiations. Agriculture should not be — cannot be — exploited as a pretext for arresting progress in other major trade disciplines in a fast-globalizing world. Canada will make progress only if it is ready to subject its own policies and practices to closer scrutiny and adjust them where necessary in the interests of improved trade relations. That requires both an unusually self-critical approach and the courage to drive through often controversial changes in the face of resistant domestic constituencies.

More fundamentally still, Canada has redoubled its efforts to conclude bilateral and even regional free trade and investment agreements as the second-best way of achieving additional trade liberalization, partly in the conviction that they are stepping stones to an eventual multilateral agreement — which rightly remains the goal of all liberally minded trading countries.

Beyond Mexico and the United States, Canada has concluded free trade agreements with Chile, Costa Rica, and Israel, completed negotiations with Ireland, Norway, Switzerland, Colombia, and Peru, and engaged in talks with South Korea, Singapore, and several other receptive countries. But the biggest prize abides: the European Union, the world's largest market. However, for reasons best known to the EU Commission in Brussels and never fully explained to Ottawa, the European Union has for 15 years or more rejected Canadian overtures for a free trade agreement while welcoming those of developing countries, leaving Canada today as one of only 8 countries without some form of preferential agreement with the EU.

Ottawa has been left to speculate that the EU Commission (or France, in particular) regards Canada–EU negotiations as a potential threat to the sanctity of the Common Agricultural Policy of the EU. Or that the Commission may have convinced itself that it could not negotiate free trade with Canada without running the risk of giving something away that it might eventually want as a major negotiating chip in the far larger game with the United States — if any such negotiation were eventually to emerge (no such reservation existed in the case of Canada's NAFTA partner, Mexico, its being defined by Brussels as a developing country). The EU itself, in a July 18, 2008, letter from French president Nicolas Sarkozy and European Commission president José Barroso to Prime Minister Stephen Harper, stated that a free trade agreement between the EU and Canada would give rise to demands by other OECD members — notably Japan, but also Australia, New Zealand, and potentially the United States. Such demands would make it more and more necessary that the EU address the issue of agreements with the OECD countries. Negotiations with Canada would help to clarify the real questions. No longer is the EU putting forward the Doha Development Round as a reason a Canada-EU deal could not be discussed. That reason for delay no longer carries any conviction. With the indefinite suspension of the Doha Development Round, North America and Europe have a clear mutual interest in increasing their leverage vis-à-vis Asia, in light of fundamental power shifts in the global economy. The United States and Europe are losing their economic lead over their Asian rivals, notably China and India, and were accordingly unable to engineer an acceptable outcome of the Doha Round discussions, as they did at the conclusion of the Uruguay Round in 1994. They failed signally to find common cause with Asia. Worse, they now risk being left outside the grand free trade arrangements that are being designed among themselves by China, India, the ASEAN group, and other Asian and now African countries.

Asia would find it impossible to ignore a transatlantic free trade agreement, which would fundamentally transform the international economic dynamic. It would place, perhaps for the last time, ineluctable pressure on China, India, and others to negotiate seriously with a transatlantic bloc for fear of losing their competitive access to a newly integrated — and massive — North Atlantic economy. This same logic applied even when a Doha deal still looked possible. The logic is even more compelling in a world where the multilateral option is languishing. A transatlantic agreement could be the giant lever needed to move the world forward while North America and Europe still have influence. It might also just be the wake-up call that is needed to save the world trading system from drifting into irrelevance.

If both Washington and Brussels do not yet view a full transatlantic agreement as an early possibility, that is another reason for Brussels to welcome, rather than shun, the prospect of an EU-Canada agreement. Europe could use the agreement as a reason for arguing that the United States should follow its two NAFTA partners in engaging in broad transatlantic negotiations. Certainly, US companies would be prompt in recognizing the fact that their Canadian and Mexican competitors had gained preferential access to the world's largest market. Washington would face strong pressure from its business community to strike a similar transatlantic agreement, as happened in response to the Canada-Chile and Mexico-Chile free trade agreements of a decade ago.

The economic arguments alone for transatlantic liberalization of trade and investment should now be self-evident to both Canada and Europe. Problems there certainly are, as the recent abortive effort to conclude the negotiation of a Trade and Investment Enhancement Agreement demonstrated, but more evident are the benefits of an EU-Canada agreement. The European Union is Canada's second-largest commercial partner; Canada is among Europe's ten largest partners. Investment has grown rapidly — the European Union is the second-largest foreign investor in Canada; Canada is the fourth-largest investor in the European Union. Sales in each other's market by wholly owned affiliates are now four times the value of exports, with sales by Canadian affiliates within Europe growing especially rapidly.

More than seven years ago, the most recent occasion on which the Department of Foreign Affairs and International Trade undertook a detailed analysis, it was estimated that annual Canadian merchandise exports to the European Union would increase by 11 percent if tariffs were eliminated on all goods except agriculture. If tariffs were eliminated on foodstuffs as well, Canada's exports to the European Union would likely increase by 16 percent. EU exports to Canada were estimated to increase by 34 percent with or without tariff elimination for agri-food products. (The increase in trade in services, which has been growing rapidly despite formidable regulatory barriers, was not estimated.) A review in 2001 concluded simply that a major reduction in barriers would significantly increase the gross domestic product of both Europe and Canada. A joint study by the EU and Canada of the benefits resulting from a reduction or elimination of barriers, when published, no doubt will provide decidedly higher estimates for trade in both goods and services, in light of the economic expansion of both Canada and the EU and the further growth in EU membership.

A declaration in support of an EU-Canada trade and investment agreement, signed shortly before the June 2007 Berlin meeting of the prime minister of Canada and the chancellor of Germany (then also the president of the EU) called for "balanced and closer future EU-Canada economic integration." The joint EU-Canada study no doubt will identify not only the benefits, but also a range of challenges, many of which are of a regulatory character (chiefly in trade in services) and the complexities that arise from the EU's varied membership and Canada's federal structure. The Berlin declaration was matched by a statement of transatlantic businesses urging that "[i]t is more important now than ever to push forward achieving a barrier-free Canada-EU market. This is a first step towards realizing the goal of a transatlantic marketplace and will strengthen transatlantic leadership in global trade negotiations." Indeed, the EU commissioner for trade has already announced that his staff will "scope" the terms of the negotiations with Canada. This scoping presumably will provide the basis for the launch of negotiations sometime in 2009, to be announced by the president of France during his visit to Montreal for the annual Canada-EU "summit." The EU, however, has already specified that this "scoping" should enable the launch of negotiations only at the 2009 summit.

What the anticipated negotiations will include remains difficult to forecast. Even questions of nomenclature appear to create differences. Canada favours the simple designation of a "free trade agreement," a designation that has wide public recognition in Canada, resonating as it does with the century-old links with Canada's two founding nations. The European Union, on the other hand, appears wary of the phrase, preferring for reasons known to itself a designation such as an "economic enhancement agreement."

In any event, whatever the agreement is eventually called, Ottawa and Brussels have briefly listed the areas to be covered. “A declaration in support of an EU-Canada Trade and Investment agreement” by the Canada-Europe Roundtable for Business (founded in 1999) has been more comprehensive. This declaration by Canadian and European businesses identifies key areas as: the elimination of barriers to investment and services, including tax; the opening of capital and procurement markets; comity in competition and environmental regulation, including avoidance of discriminatory nontariff barriers to trade; trade facilitation, with a focus on improved and efficiency for goods and services crossing borders; and strengthened cooperation on science and technology. Any agreement should facilitate professional labour mobility in efforts to establish a common skilled labour market between the two territories. This latter would include removing onerous restrictions of length of stay for nonresident executives and residency requirements for boards of directors. Further, a provision should allow future markets, such as those for carbon and emissions trading schemes, to be incorporated into the eventual agreement.

In the complex area of regulatory cooperation, greater convergence of standards and regulations in both goods and services should be a priority. At a minimum, an agreement on regulations should discourage future divergences and reduce existing regulatory barriers, both federal and provincial. In the rapidly growing area of trade in services, regulatory barriers should be reduced at least to a level corresponding with intra-EU barriers. Regulatory collaboration on certification, packaging and labelling, and health and sanitary and phytosanitary standards should be binding, supported by a dispute settlement mechanism. In this broad area of regulation, Canada will need to keep in mind “harmonization” in NAFTA to meet US requirements.

Opening services markets will require commitment at both the national and subnational levels. Similarly, greater transparency and open competition in public procurement will need to carry the support of both the federal and provincial governments. The mutual recognition of professional qualifications will also require federal-provincial cooperation, as will the free movement of skilled workers.

For trade in manufactured goods, remaining tariff and nontariff barriers should simply be eliminated. For trade in agriculture, however, major nontariff barriers are well entrenched on both sides of the Atlantic. Whether they are tackled or simply left aside in whole or in part for WTO negotiations remains to be seen. Trade in goods, in any event, would benefit from customs cooperation and other trade-facilitation measures, including agreement on supply chain security.

Competition policy and regulation would probably take much of the negotiators’ time and ingenuity — the former requiring, for example, agreement on the protection of confidential information and, more indirectly, on the mutual recognition of standards.

With the suspension or demise of the Doha Round of the WTO in July 2008, the time has never been more propitious for a transatlantic agreement. Canadians, for their part, increasingly perceive, if only intuitively, that enhanced transatlantic economic relations are the best way to help transform Canada into the most competitive economic space in North America — as the key to attracting additional investment, technology, leading-edge production practices, and skilled workers who can respond to enhanced labour mobility. A bilateral deal with Europe would give Canadian companies a competitive advantage over US and Asian rivals in the burgeoning European market. It would also sharpen Canada’s competitive edge vis-à-vis the United States. And it would strengthen Canada’s hand in negotiating bilaterally with the United States, as US companies would be concerned about the dilution of their access to the Canadian market, especially if an EU-Canada agreement went deeper than the WTO in areas such as trade, facilitating services, investment, competition policy, intellectual property, the free movement of people, and so on. This would be especially so if the agreement were accessible by other countries that meet its disciplines.

Broader and deeper transatlantic relations should be seen as a cornerstone — and a foreshadowing — of relations in the wider global order. The Atlantic community is a set of countries that ultimately must stand together, work together, and continuously reinforce shared global interests, as Canada continues to do within NATO. To the extent that technological change is altering the foundation of international relations and creating friction, Canada and Europe need to discover together the ties that bind. It is not that deeper transatlantic cooperation is an alternative to broader global cooperation; rather, it is that a strong North Atlantic architecture is central to our mutual ability to manage and advance a larger global agenda.

Bio

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