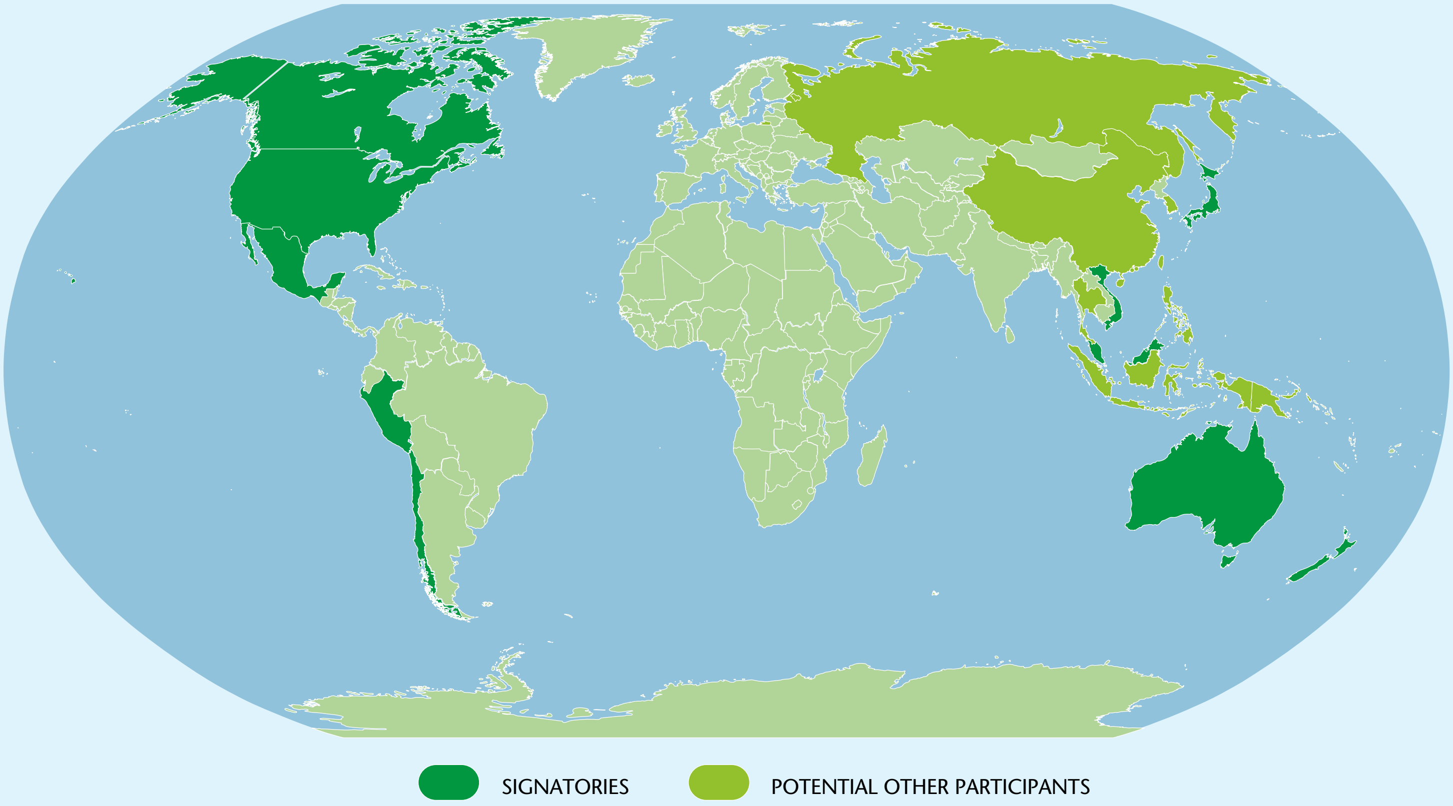

The TPP map—12 signatories including Canada, the US and Mexico. Wikipedia image

Canada's Trade Agenda: Facing Headwinds

Dan Ciuriak

Canada is at a historic juncture in trade policy, with major trans-Atlantic and trans-Pacific agreements pending at a time when trade agreements are meeting severe headwinds. Trade policy analyst Dan Ciuriak assesses the potential impact of the major trade agreements currently in the pipeline and suggests a list of priorities for Canadian trade policy going forward.

As with most government transitions, the policy hand-off from the former Harper government to the new Trudeau era includes a number of unfinished trade files. While the incoming executive has not been as unconditionally supportive of the biggest trade deal since the North American Free Trade Agreement (NAFTA)—the Trans-Pacific Partnership (TPP)—which was negotiated under the Harper government, the fact that both the Liberals and their Conservative predecessors are generally pro-trade liberalization has facilitated the political and policy transition.

Among the trade agreements yet to reach ratification in the negotiation-agreement-legal scrubbing-ratification trajectory, Parliament is currently examining and considering ratification of the second largest bilateral agreement that Canada has ever signed, the Comprehensive Economic and Trade Agreement (CETA) with the European Union, and the largest regional trade agreement it has ever signed, the TPP agreement with 11 other countries circling the Pacific Rim, including the United States. At the same time, the Transatlantic Trade and Investment Partnership (TTIP) talks between the United States and the European Union continue, in a process that could have significant ripple effects throughout the trading system and expose Canada to tougher competition in both the US and EU markets, raising for Canada an imperative to trilateralize the agreement. Flying low under the radar are the negotiations towards a Trade in Services Agreement (TiSA), which involve some 23 parties. And waiting in the wings are possible negotiations towards a Canada-China trade agreement, overtures for which have already been made.

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However, volume should not be mistaken for momentum. Since the great recession of 2008-2009, global trade has grown only in line with global GDP. Prior to the recession, global trade had grown much faster than global GDP, driven by the formation and expansion of global value chains, as evidenced in a massive expansion of trade in intermediate goods and services. Today, global value chains are as likely to be consolidating as expanding. This means that trade costs have risen – whether due to border thickening because of tightened security or because of recognition of risks of extended supply chains.

The WTO Ministerial Conference in Nairobi in December 2015 sounded the death knell of the Doha Development Agenda. Every previous multilateral trade round since the inception of the General Agreement on Trade and Tariffs in 1947 had reached a successful conclusion; the first launched under the auspices of the World Trade Organization (WTO) failed. The WTO continues to provide the overall framework for global trade (including particularly through its Dispute Settlement Mechanism), and has had some significant recent successes in the upgraded Government Procurement Agreement (GPA), which entered into force in 2014, and the conclusion of Trade Facilitation Agreement (TFA), which has yet to be ratified by a critical mass of WTO members (Canada has yet to ratify). But the path for a return to multilateral liberalization is simply unclear.

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The TTIP, easily the most ambitious trade negotiation ever launched, is now widely regarded as likely to be “dead on arrival”. The main objective of the agreement is to achieve regulatory harmonization. A trade sustainability impact assessment on the TTIP published by the European Commission in May 2016 reports GDP gains of 0.5 per cent for the EU and 0.4 per cent for the United States; three-quarters of the impact for the EU comes from regulatory cooperation and almost 90 per cent for the US. However, the US and Europe are socially out of sync on regulatory precaution and privacy. Differences on the former will likely eviscerate the TTIP’s potential economic impact, while differences on the latter could scupper the agreement altogether, as they did the Anti-Counterfeiting Trade Agreement (ACTA) before it.

The TPP, meanwhile, is in danger of not being ratified in the US, the jurisdiction that championed it. The rhetoric in the 2016 election year is tailored to populist anti-trade sentiments. This is hardly unusual for US election campaigns. However, the distemper in the United States is elevated, and a return to business as usual post-election cannot be taken for granted. Going into their party conventions, both presumptive nominees, Republican Donald Trump and Democrat Hillary Clinton, opposed TPP. Moreover, compromises in the TPP text on intellectual property for biologic drugs may not be acceptable to a Republican Congress, and could be a death blow to the agreement. In Japan, the other major party to the deal, where the TPP is an integral part of Prime Minister Shinzo Abe’s “Abenomics”, the administration’s plan to counter deflation and reinvigorate growth, the ratification debate has been postponed twice in the first half of 2016 because of its unpopularity with the electorate.

The Canada-EU Comprehensive Economic and Trade Agreement (CETA) also faces ratification risks due to some EU member states' opposition to inclusion of investor-state dispute settlement (ISDS) and, in the case of Romania and Bulgaria, due to a possible refusal to ratify unless Canada lifts visa requirements on their citizens. The substantially improved ISDS mechanism developed by Canada and the EU may overcome EU member state objections on that score, but may complicate matters for the TTIP negotiations, not to mention TPP ratification in Canada, since the TPP ISDS mechanism is now a decidedly inferior option.

The quantifiable impacts of trade agreements are an important factor for policymakers. But there are other factors that cannot be easily reduced to dollars and cents that also need to be taken into consideration.

On the numbers alone, the impacts on the Canadian economy of CETA, TPP, and a Canada-China FTA taken together would amount to little more than one quarter of annual GDP growth in a relatively modest growth year. The opportunity costs for Canada of not ratifying the TPP while the other parties go ahead would be greater by a factor of about 50 per cent. The opportunity costs of a failure to implement CETA would likely be greater still in the event of the TTIP going forward, as there would be no offset to the preference erosion Canadian exporters would face in the US and EU markets.

The relatively smaller impact on Canada of the TPP versus the CETA and CCFTA reflects the fact that there are no trade diversion gains within the regional grouping, only vis-à-vis third parties. Given the size of the TPP region, that shrinks trade diversion gains considerably compared to either the CETA or a CCFTA. A second key reason is that, within the TPP region, Canada experiences preference erosion in its key US market vis-à-vis Japan and other Asia Pacific economies that do not have FTAs with the United States. By the same token, an ambitious TTIP would erode Canada's competitive position quite significantly.

“Seal the deal on CETA. This is important both for the direct benefits of the deal but also in positioning Canada for a future TTIP of whatever level of ambition.”

The relatively large gains for Canada from unilateral liberalization reflect two things: (a) the ambitious nature of the liberalization assumptions, which go beyond what Canada has been prepared to offer in any of its agreements to date; and (b) the fact that unilateral liberealization removes some of the costs of trade that preferential trade agreements impose, even as they remove tariffs. These cost reductions affect Canada-US trade and thus leverage greater two-way trade than is possible under agreements that cover smaller trade flows. The positive impact on Canada's exports from a reduction on import costs under unilateral liberalization reflects the truism that a tax on imports is a tax on exports.

Estimates of Real GDP Gains for Canada Under Alternative Trade Agreements/Trade Policy Options.

	Real GDP % Change	Household Income (C$ billions)
CETA	0.30%	13.0
CCFTA	0.14%	6.6
TPP	0.07%	2.9
TPP excluding Canada	-0.03%	-1.7
TTIP	-0.04% to -0.07%	-2.8 to -5.0
Unilateral	1.67%	47.1

Source: Estimates by the author.

The quantitative impacts cited above reflect conservative views about what even deep and comprehensive trade agreements can achieve in terms of regulatory harmonization. The available evidence suggests that, outside the context of a single market governed by a commission with directive-issuing powers, regulatory convergence has been very slow. The TPP's regulatory convergence chapter invokes Good Regulatory Practices (GRP), which all TPP parties have already signed onto under OECD and APEC initiatives (not to mention similar programs in a NAFTA context). Why the institutions that would be put in place under the TPP would be more effective than other, long-standing processes—or indeed why they would be needed in addition to those processes—is simply not clear. Trade agreements are not the only game in town, after all.

Meanwhile, regulatory harmonization driven by trade agreements can be toxic politically, as the reaction to TTIP is showing. Simply put, it is impossible for a minister to explain why regulations for food safety, financial soundness, protection of the environment, or other policy objectives, adopted pursuant to regulatory impact assessments and full democratic processes with the full range of stakeholders involved, should be changed pursuant to a trade agreement negotiated in secret with a limited number of stakeholders that is handed to legislatures for a simple thumbs-up or thumbs-down vote.

These considerations underscore a critical failure of trade policy: as the focus of trade agreements shifted to so-called "behind the border" issues, the process for negotiating agreements that had worked for the GATT rounds which focussed on border measures was not appropriately reformed for the new circumstances.

> ***"If the TPP survives US ratification, Canada should, primarily for defensive reasons, also ratify, but simultaneously pursue a trade deal with China. If the TPP fails, Canada should add Japan to the priority list."***

For Canada, the soundest trade policy going forward is fairly straightforward, given the above considerations.

First, ratify the WTO Trade Facilitation Agreement. This will assist the many initiatives worldwide under the World Customs Organization, the World Bank and various Aid for Trade programs on reducing border costs. Canadian exporters will benefit. This is easily the lowest-hanging fruit.

Second, seal the deal on CETA. This is important both for the direct benefits of the deal but also in positioning Canada for a future TTIP of whatever level of ambition.

Third, put Canada's economic diplomacy firmly behind a broader Free Trade Area of the Asia Pacific (FTAAP) as a corrective to the divisive elements of the current mega-regional framework emerging in the Asia Pacific under the TPP and RCEP. If the TPP survives ratification, Canada should, primarily for defensive reasons will also have to ratify, but should then simultaneously pursue a trade deal with China. If the TPP fails, Canada should add Japan to the priority FTA list for its Asia Pacific engagement.

Fourth, Canada should be front and centre in using the "time to think", which the failure of the Doha Round occasions, to work out, as Jonathan Fried has suggested, the "what" and the "how" of the WTO's future role in advancing the trade policy agenda.

Fifth, study the consequences of the "spaghetti bowl" of Canada's preferential trade agreements, consider the benefits of going to a "tabula rasa" policy on a unilateral basis, and champion the sweeping away of preferential spaghetti on a global basis in the WTO for industrial goods.

Finally, the critical question which has not been answered—and cannot be answered by the available quantitative trade models—concerns the implications of the intellectual property provisions of modern trade agreements for innovation. This needs to be redressed, both from the perspective of negotiating trade agreements, and for implementing an innovation agenda in the age of FTAs. **P**

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