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by Hugh Stephens
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POLICY PAPER

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Executive Summary

The Trump administration's arrival has scrambled the cards in the trade policy world. Not only will the North American Free Trade Agreement (NAFTA) be reopened with uncertain results, but President Donald Trump has scuttled the Trans-Pacific Partnership (TPP) by announcing the United States' withdrawal from the agreement. Canada, originally cool toward the TPP, pushed hard to be included in it. The TPP became the centrepiece of Canada's Asia trade strategy, notwithstanding some public ambivalence on the part of the Trudeau government. With the TPP in its present form now in limbo, Canada still has options in Asia. First, it can keep an open mind with regard to the possible reconstitution of the TPP in another form, such as "TPP Minus One" (i.e., minus the U.S.). It should also push to reopen the bilateral negotiations with Japan that were suspended when that country joined the TPP negotiations. Canada is already exploring the possibility of an economic partnership agreement with China, perhaps on a sectoral basis, and simultaneously, it should actively pursue negotiation of a free trade agreement with the Association of Southeast Asian Nations (ASEAN) community. This could in time provide Canada access to the Regional Comprehensive Economic Partnership Agreement (RCEP) currently being negotiated among 16 countries in the Asia-Pacific region and would position Canada well in the eventuality that a Free Trade Area of Asia-Pacific (FTAAP) emerges. In the meantime, uncertainty regarding NAFTA's future needs to be addressed. This uncertainty makes it more difficult for Canada to attract Asian investment but it also provides further impetus for Canada to diversify its trading relationships and to explore stronger relationships with Asian economies.

What happens when you put most of your eggs into one basket, and then someone steals the basket? This is what happened to Canada when the Trump administration trashed the Trans-Pacific Partnership (TPP), the lead vehicle to reassert our interests in the Asia-Pacific. But while the TPP's apparent collapse represents a setback for Canada, all is not lost. There are still several good options for moving forward. To understand better what these are and how they could affect Canadian interests, let's recall how we arrived at the current impasse.

Back in the period 2008-2011 when the TPP was a grouping of just nine countries (the U.S., Australia, New Zealand, Singapore, Vietnam, Brunei, Malaysia, Chile and Peru), Canada was very much on the outside looking in[1] when it came to the evolving structure of Asia-Pacific trade. This was partially by circumstance, since the minority Harper government was preoccupied with other issues, and partially by design since the prevailing wisdom at the time was that the makeup of the TPP offered little to Canada by way of new market access — and Canada did not seem to be interested in the TPP's strategic dimension. After all, we already had an agreement with the U.S. through the North American Free Trade Agreement (NAFTA), and bilateral agreements with both Chile[2] and Peru.[3] Participation would have exposed us to pressures to make changes to our supply management and intellectual property regimes, among other areas. The use of the TPP to gain an additional foothold in the Asia-Pacific region did not get much traction in Ottawa. The Harper government preferred bilateral arrangements.

All that changed when Mexico expressed an interest in joining the TPP. Suddenly, Canada's preferential access under NAFTA to the U.S. market risked dilution, and joining the TPP negotiations became imperative if only as a defensive measure. Just as quickly then-International Trade minister Ed Fast was on a plane to TPP capitals to promote Canadian participation. The previous arguments against joining late, such as the requirement that as a condition of entry latecomers accept all elements of the agreement already negotiated and agreed to by the original partners, went by the boards. The U.S. was not helpful, dragging its feet and not endorsing Canada's participation until the 2011 APEC Summit in Honolulu[4] when then-prime minister Stephen Harper met with former U.S. president Barack Obama. But then we were in. And shortly after Canada and Mexico formally joined the negotiations, Japan became the 12th partner. Now there was a concrete economic objective for Canada — obtaining access to the Japanese market on equal terms with a prime competitor, the U.S., as well as Australia.

The negotiations were difficult and almost collapsed at several points, but finally, on Oct. 5, 2015, after more than five years of negotiation, a conclusion was announced.[5] Two weeks later Canada went to the polls and the Conservatives, who had agreed to the negotiated outcome, were out of office. The Trudeau Liberals while professing themselves to be free-traders were nevertheless on the horns of a dilemma. It was politically difficult to simply endorse the TPP negotiated under Harper, especially given vocal anti-TPP protests from a variety of quarters. These included dairy farmers who had to give up just a little of their protected monopoly, "freedom of the Internet" advocates who objected to stronger intellectual property protection for copyrighted content, and general anti-globalization activists who were and are against any trade agreement.

What did the Trudeau government do? Rather than endorsing or condemning the agreement, it ragged the puck, setting up a series of consultative meetings across the country to review what had been negotiated. This, despite the fact there was no real chance of unilaterally changing the outcome as long as the others, and particularly the U.S., ratified the deal. The federal government even proceeded with signing the agreement in February 2016,[6] all the while continuing to invite Canadians to provide comments on its terms.

In reality, the Liberals were waiting to see what would happen in Washington, given that both presidential candidates had gone out of their way to attack the TPP, with Trump calling it "a potential disaster for our country" and "the death blow for American manufacturing." If the U.S. had ratified — an outcome that looked increasingly unlikely as the 2016 presidential campaign went on — Canada would have had no alternative but to be on board the next day. The agreement enjoyed strong support from business leaders[7] and it would have been unthinkable to have walked away from a deal where we had successfully protected our access to NAFTA and opened the Japanese market to Canadian products. But although there was a faint hope that Hilary Clinton might have found a way to ratify the TPP (possibly under another name) if elected, once the unexpected results of the U.S. election were in, the writing was on the wall. We know what happened: Trump signed an executive order just three days after his inauguration, withdrawing the U.S. from the agreement. For Canada, which had worked so hard to get into the TPP — and which had placed many of its eggs in the TPP basket — this was a setback to our Asia-Pacific ambitions. The question is, where does Canada go now?

Foreign Affairs Minister Chrystia Freeland in effect proclaimed the TPP to be dead, citing the agreement's provisions that required ratification by six of the 12 partners comprising 85 per cent or more of the collective GDP of the negotiating countries for it to enter into force. Assuming it is dead, an obvious move for Canada would be to revive the Canada-Japan talks. There had been seven rounds of such talks[8] but these had made little progress and were suspended when Japan joined the TPP negotiations in 2012. However, since Trump's announcement of the U.S.'s TPP withdrawal, Japan has been reluctant to come to the table with Canada, clinging to the notion that the TPP is not completely dead.[9] One reason may be that Canada does not offer Japan the kind of market access that the TPP would have locked in, especially since NAFTA's future is in question, weakening Canada's appeal as a North American gateway. For Japan, keeping and expanding its access to the U.S. market is the prize. Prime Minister Shinzo Abe even travelled to the U.S. to meet Trump to argue Japan's case. Abe still needs the TPP as the spur to enact his domestic economic reform agenda and Japan has refused to let the agreement die even as it explores informally the possibility of opening bilateral talks with the U.S.

Pursuing bilateral negotiations, with the U.S. as the hub and other countries as the spokes, is apparently the strategy Trump favours. If or when the U.S. and Japan commence formal bilateral negotiations, Canada may well be cast aside, left standing at the altar as happened after

Korea concluded deals with the U.S. and the European Union (EU). Canada and Korea began free trade negotiations in 2005 before either the EU or the U.S. opened talks with that country. However, once negotiations for the KORUS (Korea-U.S. Free Trade Agreement) began, the negotiations with Canada went slowly due in part to a trade dispute involving Canadian beef.[10] South Korea had banned imports owing to the discovery of mad-cow disease in the Canadian herd, and there was also Canadian foot-dragging because of opposition from this country's automotive sector.

The U.S. signed its agreement with Korea on June 30, 2007 and was able (eventually, through some tweaks to the final text) to get those same North American automakers onside. As a result, KORUS finally entered into force on March 15, 2012. At that point, after both the EU and U.S. agreements were in effect, Canada realized it was only punishing itself by not talking to Korea. By that time, however, the trail had gone cold and it was not easy to get Korea's attention and put things back on track. Canada employed various means of diplomatic pressure to get the Koreans back to the negotiating table with the result that the Canada-Korea FTA[11] was finally completed in late 2014, coming into effect on Jan. 1, 2015. While this helped level the playing field for Canadian exporters, the implementation timetable put liberalization of market access for Canadian products at least two years behind liberalization for competing U.S. products, such as pork and beef.

As a former Canadian ambassador to Japan has argued,[12] one way for Canada to maintain its dialogue with Japan is to use the vehicle of the TPP, or what is left of it without the U.S., to lock in what was achieved. Some of the original TPP signatories have floated the idea of keeping the TPP alive. A meeting of ministers and officials was held in mid-March in Viña del Mar, Chile,[13] in what was officially billed as the High-Level Dialogue on Integration Initiatives in the Asia-Pacific Region. In addition to the original 12 TPP participants (the U.S. was represented by its ambassador to Chile), the Chileans also invited China, South Korea and Colombia. China's prime interest is to observe what is happening, given its own stakes in the Regional Comprehensive Economic Partnership (RCEP), another regional agreement discussed below. The purpose of the meeting in Chile was exploratory and open-ended — to see if there is a will to maintain the gains achieved through the TPP negotiations, a position strongly espoused by Australian Trade Minister Steven Ciobo.[14]

As expected, the only agreement was to keep talking and keep channels open. In a joint statement by the TPP partners,[15] the participants declared that they "exchanged views on their respective domestic processes regarding TPP and canvassed views on a way forward that would advance economic integration in the Asia-Pacific." The next opportunity to meet will be at the APEC trade ministers meeting in Hanoi in May. Notably, the way forward could also include the Pacific Alliance,[16] the trade and economic integration agreement formed in 2011 among Chile, Peru, Mexico and Colombia. Canada, along with many other countries, is an observer and one idea being floated is that if the TPP is too toxic a concept (or name) for some, then perhaps the Pacific Alliance could form the nucleus of a trans-pacific trade framework. Certainly, in its announcement of the participation of International Trade Minister François-Philippe

Champagne at the meeting in Chile, Global Affairs Canada studiously managed to avoid a single reference to the TPP, focusing instead on Canada's "progressive" trade agenda.[17]

Renegotiating the TPP will not be easy since many of the concessions the partners made were premised on gaining greater access to the U.S. market. All those tariff concessions they made will now have to be reviewed to ensure that a politically acceptable balance can still be achieved without the carrot of the U.S. market. While that will be difficult, it is not impossible. Other parts of the TPP, such as the "horizontal chapters" dealing with issues such as new rules for trade in e-commerce, small and medium-sized enterprises, trade facilitation, capacity building, competition policy, development, labour, the environment and so on could likely be adopted with less difficulty. While hanging on to a revised version of the TPP would, at first blush, seem to have little to offer to Canada, the TPP Minus One formula, as it is sometimes called, might offer the best way to pursue market opening with Japan. The fact that Canada attended the meeting in Chile is a good first step in terms of keeping options open and exploring alternatives to maintaining a foothold in trans-Pacific trade.[18]

Japan is just one of Canada's major trading partners in Asia. We have an agreement with Korea, as noted above, leaving China as a major challenge. Beyond China, there are the 580 million people of the 10-country Association of Southeast Asian Nations (ASEAN) bloc. ASEAN is the key player in another regional agreement currently under negotiation, the RCEP,[19] which if completed will be a trade agreement between the ASEAN countries and the countries with which ASEAN already has separate agreements, namely China, Japan, Korea, India, Australia and New Zealand. RCEP would harmonize these six separate agreements, as well as the agreement linking the 10 ASEAN countries (the ASEAN Free Trade Area or AFTA), into a cohesive whole.

Canada doesn't have a seat at this table although it has had a long relationship with ASEAN, having been a dialogue partner since 1977.[20] At one time, Canada maintained a Canada-ASEAN Centre in Singapore, funded largely by the Canadian International Development Agency (CIDA). The centre undertook a number of projects in the region including important work in the 1990s on the issue of conflicting jurisdictions in the South China Sea. In recent years, Canada has let its interest in ASEAN wane. This is changing, with the establishment in 2016 of an embassy dedicated exclusively to relations with the bloc, and the announcement in the summer of 2016, following ministerial-level meetings, that officials on both sides had been charged to prepare the terms of reference for a feasibility study on negotiating a Canada-ASEAN FTA.[21] If Canada were able to successfully negotiate an agreement with ASEAN, and if RCEP is concluded this year, as is hoped, then the Canada-ASEAN agreement could possibly be a stepping-stone to Canadian inclusion in RCEP. RCEP has an open accession clause allowing accession by any state with an agreement with ASEAN.[22]

RCEP is by no means a done deal. The goal of the 16 participants is to conclude it this year but there are challenges. The main obstacle is the lack of agreement among and between the non-ASEAN negotiating partners, for example between Japan and China, or between China and India, where there are no pre-existing agreements to build on. Frankly, India's presence as a negotiating partner presents a whole range of challenges given the protectionist stance that country has adopted on many trade issues. The result is likely to be a fairly low-ambition agreement with lots of exceptions and carve-outs, long transition periods, and nothing like the degree of market access achieved through the TPP.[23]

While it is easy to criticize this level of ambition and likely achievement, nevertheless we should not minimize the contribution that RCEP, if achieved, will bring. While it could potentially go further, it will still represent movement toward greater trade opening. Businesses that are fortunate enough to find their products covered by the agreement will benefit, as will consumers. Rules of origin will be harmonized. To achieve the compromises necessary to forge an agreement that includes economies as disparate as Japan, Korea and Australia on the one end of the scale, and Laos, Myanmar and Cambodia on the other, with China and India in the mix, will be no small achievement.

If the RCEP is completed, and if TPP in some form proceeds, the long-term goal of reaching a FTAAP will have taken another step forward. Both RCEP and TPP are seen as tracks toward the larger objective of a regional agreement. FTAAP[24] may always remain an aspirational goal, but as a vehicle that would include both China and the U.S., as well as all the other major (and many minor) economies of the Asia-Pacific region, it is seen by many as the end game, or at least a target to work towards in order to keep trade discussions moving in the right direction. Canada needs a seat at the FTAAP table beyond our presence in APEC, given that any FTAAP will emerge from a binding trade agreement, not from the loose and consensus-based APEC framework.

In the meantime, there is China to deal with. Canada and China have been dancing around each other for a while now, but the Trudeau government's accession to power seems to represent an opportunity that Canada should not squander.[25] While all the talk about a new golden era of Canada-China relations contained a lot of hyperbole, (because relations between the two countries were really not that bad prior to the Liberals taking office), nonetheless, the accession of Trudeau *fils* has allowed both countries to build on the legend of Trudeau *père* as the person who made the key breakthrough in the establishment of Canada-China relations in 1970. Justin Trudeau's election was a convenient way to turn the page from the Harper era's sometimes confrontational policy. While relations with China could not be described as smooth under Harper, there were achievements, notably the conclusion and implementation of the Foreign Investment Promotion and Protection Agreement (FIPPA),[26] completion of an initial trade complementarities study,[27] approval of a major Chinese investment (with some reservations) in the oil industry, the designation of Canada as a renminbi (RMB) exchange hub and the adding of Canada as an approved destination country for Chinese tourists.

The two countries have agreed to begin exploratory discussions toward a bilateral trade agreement, but this will move slowly.[28] Dealing with a still largely restricted economy such as China's is complex and difficult, and Canadian public opinion is very much divided on the benefits of greater opening of trade with China. Fewer than half of Canadians support free trade negotiations with that country, according to a poll conducted in 2016 by the Asia Pacific Foundation of Canada.[29] Despite its own spotty record on market liberalization, in the early days of the Trump administration China has seized the initiative to establish itself as one of the leading public champions of open markets.[30] Whether its actions will match the rhetoric remains to be seen but there are encouraging signs such as the announcement of new liberalization measures under the rubric of the Twenty Measures.[31] The forthcoming 19th Congress of the Chinese Communist Party this fall will be important in affirming what direction Chinese economic policy will take. If China is truly committed to a policy of market opening, reaching a trade agreement with Canada would help move things in the right direction.

It will be a challenge for Canada to pry open some of the more restricted areas of the Chinese economy, given the size of our market compared to that of China, but if we are selective and strategic, we should be able to make progress in areas of real potential for Canadian business. An initial agreement does not have to be all-encompassing and could cover select sectors. Financial and health-care services offer good prospects for growth for Canada, for example. We can also ensure that our agricultural exports are not impeded by specious non-tariff barriers and that our resource products get equal access with those of our competitors. In a negotiation with China, Canada enjoys some strategic leverage, being a country endowed with resources China needs and located on the U.S.'s doorstep. Unlike Korea, or perhaps Japan, countries that were initially cool to the idea of spending much in the way of time and resources to reach an agreement with Canada, the Chinese are eager to get going.

Canada should seize this opportunity, as the Trudeau government appears to be doing. At the same time, we need to put some eggs into other baskets, particularly plurilateral baskets. That is why the negotiations with ASEAN will be an important channel to pursue, and why it is a good idea to keep our options open on the TPP Minus One, TPP Plus or whatever form emerges. It will require a significant commitment of resources as Canada will have its hands full dealing with Trump's "tweak" of NAFTA, or a more substantive revision as was recently suggested by Commerce Secretary Wilbur Ross.[32]

NAFTA is one of the wild cards that could affect all of the various options for better trade architecture in the Pacific. Canada's attractiveness to investment by Asian countries is based in large part on the access that NAFTA gives to the U.S. market. If the Canada-U.S. border thickens, and rules of origin become more restrictive, prudence will tend to drive future Asian investment to U.S. locations. At the same time, NAFTA revision could also work to spur greater Canadian interest in Asia. If the taken-for-granted U.S. market becomes more restrictive for Canadian exporters, there will be an even greater need for trade diversification. We are already seeing this as the threats to Canadian softwood lumber exports to the U.S. have given fresh impetus to finding new markets overseas.[33]

What the result of the NAFTA negotiations will be is anyone's guess at this point. Hopefully, it will preserve most of Canada's access to the U.S. market. We have managed to get the Canada-European Union Comprehensive Economic and Trade Agreement (CETA) across the line, a major achievement in this era of anti-globalization sentiment, and let's hope we can preserve the essential elements of NAFTA. At the same time, we need to keep our eye on what is happening with Asia where there are many significant changes — the apparent unravelling of U.S. commitment to construct the economic architecture of the region, China's assertion of leadership on the trade front, ASEAN's growing role, a need to cement our negotiated access to the Japanese market and the fluid situation with regard to the kind of structure that may emerge from the TPP's wreckage.

Trump may have whisked away the original TPP basket, but there are still plenty of options available for Canada to pursue its interests in the Asia-Pacific region. Asia is going to be the main engine of growth well into the future, and Canada needs to embed itself as part of the region for both economic and strategic reasons. Negotiating additional bilateral arrangements, such as with China and Japan, will be important building blocks, but participation in a regional trading bloc such as with ASEAN should also be pursued as a priority. While NAFTA's uncertain future and the Trump administration's policy directions are casting a shadow over the global trading system, Canada can still act to maximize its options to exploit the opportunities presented by the Asia-Pacific region.

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Hugh Stephens has more than 35 years of government and business experience in the Asia-Pacific region. He is currently Distinguished Fellow at the Asia Pacific Foundation of Canada and Vice Chair of the Canadian Committee on Pacific Economic Cooperation (CANCPEC) and an Executive Fellow at the School of Public Policy at the University of Calgary. He is also an Associate Faculty member in the School of Business at Royal Roads University, Victoria, B.C. and a Fellow at the Canadian Global Affairs Institute. Before returning to Canada in December 2009, he served as Senior Vice President, Public Policy (Asia Pacific) for Time Warner, based at the company's regional headquarters in Hong Kong, and continued to serve as a Senior Advisor to the company until 2013. Prior to joining Time Warner in 2001, Mr. Stephens spent 28 years with the Department of Foreign Affairs and International Trade (DFAIT), including postings to five Canadian missions in Asia. His final assignment was as Assistant Deputy Minister for Policy and Communications at DFAIT.

Canadian Global Affairs Institute

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