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Confusion and Opportunity: The Challenges of Canada's Trade Negotiations

by John Weekes
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When we watch the news on television or read about trade negotiations, it always seems to be geographically oriented – including NAFTA (with the U.S. and Mexico), CETA (with the EU), CPTPP (with 10 other Asia Pacific partners including Japan), China, India or the WTO (the World Trade Organization with 164 member governments including all members of the G20). Obviously, international trade agreements are between countries, but looking at it geographically doesn't really explain why Canada is negotiating with a particular country and what Canadian interests the negotiation is advancing.

This article begins by setting out what seem to be the basic objectives that Canada brings to any trade negotiations table. Outlining these objectives helps to establish the context in which we are negotiating. Objectives such as these should be driving our negotiators' conduct.

The twists and turns of the last few years have been extraordinary. Two years ago, no one thought we would be in the middle of a difficult NAFTA renegotiation. No one thought the U.K. would vote to leave the European Union. A year ago, almost everyone thought the TPP agreement was dead. A set of basic objectives serves as a compass to help guide us through troubled and unpredictable times.

After setting out these objectives, the article will return to a more geographic focus and discuss recent major developments in trade involving Canada.

Basic Objectives of Canada's Trade Negotiations Policy

Any trade negotiation should be about improving Canada's economic prospects. It is important to look at these objectives in a long-term context. Canadian negotiators should be thinking about where the puck is going, not where it is or – worse still – where it has been. The objectives Canada pursues in trade negotiations are to:

- Manage adaptation to changing global dynamics;
- Protect current market access;
- Open new market access opportunities;
- Defend important Canadian sensitivities;
- Modernize existing trade agreements;
- Promote a progressive trade policy; and
- Ensure agreements are durable to provide a predictable framework for business planning and investment.



Important complementary government policy objectives should be to help Canadians adapt to new trade agreements by:

- Assisting business to identify and exploit the new opportunities;
- Insisting that other governments live up to their obligations including, if necessary, through dispute settlement action;
- Fostering and promoting efforts to prepare Canadians to thrive in the fast-moving 21st century global economy; and
- Providing a safety net for those who are left behind.

This list is largely economic in nature. Open, non-discriminatory trade helps to create and maintain a more peaceful world. With the continuing proliferation of weapons of mass destruction, any policies that promote a more peaceful world should be highly valued.

American Trade Policy and the NAFTA Renegotiation

The wild cards in today's trade policy firmament are President Donald Trump and his trade representative, Robert Lighthizer. The Trump administration's key interest seems to be in moving away from trade agreements which they believe fetter American power in their dealings with other nations. Trump made it clear from the outset that his administration intended to renegotiate NAFTA or to withdraw from it. The fact that NAFTA has been very beneficial to the United States, is strongly supported by business and most elected state officials, and by the leadership of the Republican majority in Congress has cut little weight – at least until recently. Remarkably, Lighthizer sees his own private sector as part of the problem and wants it to avoid undercutting his negotiating leverage.

Such behaviour by the country that more than any other has been the architect and guardian of the post-Second World War trading system is astonishing. Lighthizer seems to want to strengthen the U.S. economy by weakening Mexico's and Canada's economies. He lives in a zero-sum world, and wants to ensure that the U.S. does not have a trade deficit with anyone.

American proposals to “rebalance” NAFTA have emerged from this context. They include:

- A government procurement proposal that Canada's chief negotiator has said is “the worst offer ever made by the U.S. in any trade negotiation”;
- A proposal to change the rules of origin for light vehicles (essentially passenger cars) to require 85 per cent North American content and 50 per cent U.S. content. No NAFTA rule of origin has ever required U.S. content – only North American content. This proposal is a non-starter for both Canada and Mexico and has been rejected as unworkable by American vehicle manufacturers, parts producers and unions;



- A sunset clause that would provide for the new NAFTA to terminate every five years unless it was specifically renewed by the parties;
- Proposals that would eliminate, weaken or render merely advisory the three sets of dispute settlement procedures in NAFTA; and
- A proposal to eliminate all Canadian tariffs on dairy, poultry and eggs while maintaining trade-distorting U.S. subsidies in place.

Not surprisingly, the Canadian negotiators have refused to enter into negotiations on the basis of these proposals. However, Canada has put forward many proposals in other areas of the negotiations.



Figure 1: Canada's Foreign Minister Chrystia Freeland addresses the media with Mexico's Economy Minister Idefonso Guajardo and U.S. Trade Representative Robert Lighthizer at the close of the third round of NAFTA talks involving the United States, Mexico and Canada in Ottawa, Ontario, Canada, September 27, 2017. (Reuters/Chris Wattie)

A key challenge for the Canadians (and the Mexicans) has been how to engage the U.S. team in real negotiations. Lighthizer clearly believes in the U.S. rebalancing proposals and sees a real opportunity as Trump's instrument to advance approaches that he has privately supported for decades. The situation is further complicated by the fact that the American negotiators including the U.S. chief negotiator have no authority to cut a deal on anything.



At the January negotiating round in Montreal, the Canadians moved from a stance of explaining the shortcomings of the U.S. proposals to engaging in certain areas on the basis of new ideas designed to initiate a discussion that could lead to solutions. Thus, new ideas were advanced:

- on automobile rules of origin;
- to improve the review provisions of NAFTA in lieu of a sunset clause; and
- to respond to U.S. proposals on investor state dispute settlement.

At the conclusion of the Montreal round [Lighthizer told the press](#) in part, “More importantly though, we finally began to discuss some of the core issues. So this round was a step forward, but we are progressing very slowly.” While his tone was still quite abrasive he did not reject the Canadian proposals. And, it appears there was substantial engagement at the last round in Mexico City on the Canadian ideas for both the automobile rules of origin and the review provisions.

Wisely, the Canadians (and the Mexicans) have embarked on a two-pronged engagement with the United States. On the one hand, they are negotiating with Lighthizer and his team, but at the same time they are working with a wide range of economic and political stakeholders in the U.S. to influence Congress, which in turn will pressure Trump and other members of his administration to modify the American negotiating approach. After all, Congress, not the president, is responsible under the constitution for regulating foreign commerce. This initiative has generated some positive results. In fact, Lighthizer is reported as [complaining](#) that discussions between Canadian officials and U.S. stakeholders are diminishing his leverage in the negotiations.

This advocacy work in the U.S. has tapped into a well of concern in American business circles (including notable agricultural producers in the Midwest) that the president might invoke NAFTA Article 2205 that allows a party, after six months' notice, to withdraw from the agreement. This work has led American business circles to realize that the Canadian government's approach to NAFTA and its renegotiation is closer to their own view of what is needed than is the U.S. government's position. It is now becoming clear that the efforts of U.S. business and pro-NAFTA elected officials have reduced the likelihood that Trump will opt to withdraw from NAFTA.

While some good progress on modernizing NAFTA has been made during the renegotiations, many serious differences remain and they will take a long time to address. It is increasingly likely that the negotiations will continue through the Mexican elections in July, the U.S. midterm elections in November and on into 2019. If the political landscape shifts, it is hard to predict what will happen. It is not inconceivable that the negotiations could simply peter out. And, of course, the president is negotiating under [trade promotion authority](#) delegated from Congress under the *Bipartisan Congressional Trade Priorities and Accountability Act* of 2015.

This authority expires on July 1 unless it is extended. For that to happen, the president must request an extension by April 1. Lighthizer has said publicly that the president will request an extension and if he does, it is unlikely that Congress will disapprove.



As long as negotiations continue, Canadian businesses will face uncertainty about the rules that will govern the trade relationships in North America. However, the prospects of weathering the storm are improving as are the prospects of achieving a long overdue modernization of the 25-year-old NAFTA. Of course, the President remains unpredictable and with the protectionist Peter Navarro back in a position of real influence after the departure of Gary Cohn as Trump's chief economic advisor bad surprises are entirely possible.



Figure 2: Representatives of members of the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) trade deal pose for an official picture after the signing agreement ceremony in Santiago, Chile. (Reuters)

Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP)

The most significant trade policy development in 2018 has been agreement among the 11 countries (absent only the United States) that originally signed the TPP in 2016 to move forward with a slightly revised version – now called the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP). Almost no one expected the agreement to survive Trump's announcement a year ago that the U.S. was withdrawing from the project. Remarkably, Prime Minister Shinzo Abe's government decided to play a major leadership role in salvaging the deal. The Japanese were driven by strategic political considerations. They were alarmed at the Americans' retreat from Asia and by their weakening support for global trade rules. They were also concerned that American withdrawal would greatly strengthen China's role in the region. By bringing the CPTPP into being, the Japanese used their market as leverage to encourage the Americans to reconsider their approach. The reason Trump has been musing about possible American interest in joining a revised TPP is that American agricultural producers – many of



whom voted for Trump – now realize that that the president's action has shut them out of the Japanese market. That is because being outside the new CPTPP they will face higher tariffs than their competitors inside the agreement. In addition, the Japanese have decided that it is in their interest to have a major trade agreement with high-quality rules that encourage market forces in the Asia Pacific area. Such rules establish a reference point that countries can use in negotiating with China.

It is important for Canadians to realize that for Japan, the CPTPP is important not just as a trade agreement but as a geopolitical agreement that enhances Japan's role in an area where the major players are China and the U.S. The Japanese would not look kindly on any country that upset their strategic plans. Certainly, if Canada had damaged this initiative it would have dashed any prospects of obtaining free trade with Japan for at least a decade.

Fortunately, Canada decided to join the CPTPP. This is a very good deal for Canada and it would have been a disaster if we had not embraced it. As the Canada West Foundation has pointed out, the CPTPP is even more beneficial to Canada than if the U.S. were a party to it. Under former president Barack Obama the U.S. used its leverage to open the Japanese market, notably for agricultural products. Then, under Trump, the U.S. backed away, leaving all the benefits on the table for Canada and the other CPTPP partners. In all probability, the U.S. will return to the CPTPP but probably not until Canadian exporters have enjoyed several years of preferential access. This should give Canadians a significant marketing advantage which should serve Canadian interests well even after the tariff discrimination is eliminated.

When the CPTPP was signed on March 8, Canada became an original signatory. If Canada had not done so, Canadians would eventually have needed to negotiate accession to the agreement and the admission price would have been significantly greater. And, of course, if we waited until the U.S. joined, the price would have become even greater. Our focus now should be on making sure that Canada ratifies the agreement as soon as possible to ensure that Canadian exporters benefit immediately from the first round of tariff cuts. Canadians will lose out if other CPTPP competitors get preferential access to the Japanese market first.

The Comprehensive Economic and Trade Agreement (CETA) with the European Union

This very important agreement for Canada came provisionally into effect in September 2017. Significantly, it provides Canadian exporters with a substantial advantage over their American competitors in the world's largest market. A couple of years ago, the U.S. and the EU were pursuing their own bilateral agreement – the Transatlantic Trade and Investment Partnership agreement (TTIP). So when Canada completed the CETA negotiations it appeared that the U.S. would complete its own negotiations with Europe soon afterwards. This would have meant that Canadian exporters would have enjoyed a competitive advantage over their American counterparts for a short time. However, under Trump's trade policy, that period of preferential access will last for a good number of years.



The combined effect of Canada having preferential access to both the EU and the markets of the CPTPP countries at the expense of its U.S. competitors should make Canada a more attractive site for investment, including from American companies denied equivalent access to these markets by their President's trade policy.

Free Trade Negotiations with China?

In November when Prime Minister Justin Trudeau made an official visit to China, Canada and China seemed to be on the cusp of initiating bilateral free trade negotiations. It did not happen at that time but discussions between the two partners continue with a view to finding a way forward to negotiations. There is a good possibility that these efforts will be successful within a matter of months. It is important to note that these discussions are about initiating negotiations, not completing them. There are [strong arguments](#) on both sides as to why an agreement would make good sense but these negotiations would be complex and would take a number of years to complete. However, launching the project would have a positive effect on the bilateral management of the trade relationship by signalling the two governments' commitment to deepening this relationship.

Conclusion

Canada's trade leaders face no shortage of challenges in 2018 but we are on considerably firmer ground than we were a year ago. The NAFTA negotiations continue and the threat of U.S. withdrawal from the agreement has lessened. CETA has finally been implemented on a provisional basis and the CPTPP has become a reality – but without the United States.

The NAFTA negotiations should remain the top priority but the government should accord a high priority to ratifying the CPTPP and securing its implementation. The government should also assist Canadian businesses to take advantage of both CETA and CPTPP and to consolidate market access gains during the window in which Canadians have better access to these two enormous markets than Americans.

The government should also give a big push to starting free trade negotiations with China.

Finally, other challenges need to be addressed, including working with other like-minded countries to strengthen the WTO in the medium term. It remains the most logical forum for managing the challenges of technological change and the forces of globalization. It also offers the best chance of putting all countries on an even playing field and thereby making a significant contribution to global security and world peace.

▶ **About the Author**

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