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Commentary October 2008

EU-Canada Economic Partnership: Where Next?

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Just days after the Canadian election, the long-planned EU-Canada Summit took place in Québec City. Canadian Prime Minister Stephen Harper, French President and the current holder of the European Union presidency Nicolas Sarkozy and the President of the European Commission José Manuel Barosso met. But they represent political entities which have yet to adopt a clear vision of a future trade agreement.

The fact that the previous Harper government set the election date three days before the summit was mirrored by the decision of the now former EU Trade Commissioner Sir Peter Mandelson to head home to help U.K. Prime Minister Gordon Brown sort out the financial sector crisis. No decisions were made at the summit but nevertheless much was at stake.

Harper decided not to publish the Joint Study by Canada and the EU on the costs and benefits of a deeper economic partnership until after Election Day. There may have been good reason to hold back. The study shows that the costs and benefits of more liberalized economic relations are very unevenly distributed between both entities and even more so within the EU and within Canada. Not all the provinces may have been happy when they fully understood what a strong dose of liberalization in transatlantic exchanges will really mean for their own domestic affairs.

Even more problematic was the fact that the joint study was prepared on the assumption that we are heading towards an even more liberal global economic order. This may now be questioned. When the smoke of the financial crisis has dispersed, the 'world of globalization' and with that the concept of economic liberalization will never be the same again. It has been demonstrated that global markets, just as is the case with any market, need global rules of the game which include a monitoring and supervision regime that is up to the job. Bilateral international agreements will have to reflect the new situation. The initiative for a New Bretton Woods as it was headmastered by Sarkozy (and Brown) reflects a European stance on the issue that may not be shared by the new minority government.

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Canada as a resource-dependent economy with a sluggish record in terms of labour, capital and material productivity is in dire need of a stringent international economic policy strategy. Despite being an extremely trade-dependent economy, Canada's trade portfolio looks suspiciously similar to those of smaller developing countries, which mainly trade a small portfolio of goods and services with a limited number of local partners. Canada's dependence upon U.S. markets as a destination for exports has slightly decreased in the last ten years, but this dependence remains very high with almost 80% of Canadian exports destined for south of the border last year. The standard model of international trade often predicts that trade with neighbours of geographical proximity will be high – so there is no surprise in Canada's high export and import shares with its neighbour to the South. However, in a global economy international trade not only is determined by geography, but also by economic and political factors. Economically speaking, what matters is an attractive palette of goods and services that are in high international demand. Exporting raw materials and riding the wave is bad politics. Politically speaking, what matters is a well-designed international trade policy that brings together unconnected, or under-connected, markets.

The fact that Canada is only just opening negotiations for a Canada-EU economic partnership agreement suggests that Canada has deliberately neglected to cultivate this dimension of its trade strategy for many years. While it may have been noble to sit out the long-running failure of global trade negotiations started in Doha, it was a mistake not to design an alternative trade strategy or Plan B for the country. Unlike the U.S. and many other developed economies, Canada limps along behind the pack in negotiating and signing Regional Trade Agreements. The 1978 Canada – EU Framework Agreement has long been a spent force. It is high time that Canada modernized its approach to the EU. While the EU has 27 bilateral trade agreements in place and the United States has nine, Canada only has agreements with five other states. Given the level of discontent in some political camps north and south of the border with NAFTA one may argue that a minority government has to be cautious in their trade strategy. We think that such a cautious attitude generates more costs than benefits.

Being the largest trading bloc in the global economy, with over 15% of global merchandise exports coming from the EU (while the U.S. share is 12%) the European Union with its 27 member economies seems to be a suitable partner for a trade agreement. It has been reported that such an agreement would trigger $40 billion in cross-border trade, in particular in trade with services. Although such econometric simulations need to be taken with a grain of salt, it seems safe to assume that Canada as a whole has a lot to gain in opening up to the EU. Increased competition would boost the competitiveness of prices and attractive products. The effects on production in terms of export opportunities and import competition may differ from sector to sector. As most of the benefits of deeper integration with the EU are expected in the service industry, the worldwide collapse of the financial industry may dwarf many of the effects being simulated in the econometric exercise. Still, getting the EU on board as an economic partner is a worthwhile undertaking.

The question though is why the Harper government has decided to handle the preparation of the agreement in such a low-profile way and to postpone the publication of the joint study, which serves as a basis for the negotiations, until after the federal election? It seems to us that a number of factors help to explain the secrecy. Contrary to the suggestion made in earlier leaks, EU officials will only sign a final agreement if the rules on public procurement are compatible with EU practices, not least the ones established with the creation of the Common Market. The Europeans are keenly interested in opening up to European bidders what are currently mainly closed competitions for public procurement. The assumption is that European companies could be strongly competitive in those sectors. However, such a market opening can only happen if all the provinces are on board both with respect to government procurement markets and ensuring services markets, in general, are non-discriminatory and competitive, something that has yet to happen. Many barriers to interprovincial trade in services exist. While the 1995 Agreement on Internal Trade partially addressed this problem, many exceptions remain. Public procurement is still a political tool of provincial governments to practice a type of industrial policy and to provide local actors with financial perks. At this point only the Province of Québec appears to be fully on board as last week it signed an agreement with France to guarantee mutual recognition of professional diplomas and experience.

There are also disagreements over appropriate levels of regulation that have yet to be resolved either bilaterally or multilaterally. European regulators often favour stronger regulations that can restrict market access for countries exporting goods and services to Europe. The sheer size of the EU suggests that Canada needs the EU markets more than the EU needs Canadian markets. Accordingly, the Europeans will not be willing to make too many significant concessions towards Canadian sensibilities. It is extremely doubtful that Harper's open federalism will allow for the creation of a Canadian single market – a necessary base from which to negotiate with the Europeans on an equal footing. Regardless, any new Canadian government will need finally to get its act together in designing a trade strategy that suits the 21st century.