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SAFETY IN THE MARKETPLACE: FREE TRADE AS A CANADIAN SECURITY REQUIREMENT

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Exercise Solo Flight

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SAFETY IN THE MARKETPLACE: FREE TRADE AS A CANADIAN SECURITY REQUIREMENT

The presidency of Donald Trump has given rise to some of the most disruptive changes in international relations since World War Two. Shifts of US policy away from global engagement to isolationism have had, and will continue to have, broad implications for many areas of governance globally. Given the deep interconnectedness of its bilateral relationship with the US, it is therefore inevitable that Canada will feel these effects strongly.

Of the diverse policy sectors affected by American policy changes, none is more fundamental to Canada than its national security. To date the Trump administration has indicated no intention to change the continental defence construct in a meaningful fashion, so Canada's "traditional" military security does not appear to be under increased threat anytime soon.¹ However the same optimistic case cannot be made for the economic element of Canadian security. President Trump has indicated clearly his displeasure with the North American Free Trade Agreement (NAFTA), repeatedly singling it out as a target for the protectionist platform that secured his election.² NAFTA has become woven so deeply into Canadian patterns of trade that any disruption to it cannot help but alter the economic landscape for the worse.

A liberalized international trade order has become more than a fringe benefit for an export-dependent state like Canada: free trade is now a key requirement that must be safeguarded in order to secure its economic resiliency. This paper will examine the value of existing free trade agreements to Canada's economy, with an initial focus on NAFTA. It will be shown that

¹Tom Roeder, "Leaders: Tweets, tariffs don't shake NATO, NORAD alliances," *Colorado Politics*, last updated 10 April 2018, <https://coloradopolitics.com/leaders-tweets-tariffs-dont-shake-nato-norad-alliances/>.

²Stephen Gandel, "Donald Trump Says NAFTA Was the Worst Trade Deal the U.S. Ever Signed," *Fortune*, last updated 27 September 2016, <http://fortune.com/2016/09/27/presidential-debate-nafta-agreement/>.

the maintenance of an environment that supports such free trade agreements now constitutes a pressing security issue for Canada. An exploration of key issues that threaten the development of international free trade will lead to a discussion of opportunities and policy recommendations going forward.

Economic Effects of Free Trade

Over the past 30 years Canada has benefited considerably from liberalized international trade, most obviously with the United States. The Canada-US Free Trade Agreement of 1987 was supplanted by NAFTA with the inclusion of Mexico in 1994. The resulting market access allowed exports as a share of Canada's Gross Domestic Product (GDP) to rise rapidly, from a fairly stable historical 25 percent before 1990 to over 44 percent by 2000.³ Over three quarters of Canadian exports now go to the United States, and they have quadrupled in value over this time.⁴ This invigorated trade has created unprecedented prosperity for Canada, although the distribution of these new riches has been uneven.

Notwithstanding its sustained growth, Canada's economy has been part of a broad trend of widening inequality since the liberalization of trade. The Canadian Gini coefficient increased from a historical low of 0.28 in 1989 to 0.32 by 2009, while adjusted median income remained almost flat despite huge gains in GDP.⁵ Wealth inequality is even more pronounced, with the gap

³The World Bank, "Exports of goods and services (% of GDP): Canada," Last accessed 15 April 2018. <https://data.worldbank.org/indicator/NE.EXP.GNFS.ZS?locations=CA>.

⁴Trading Economics, "Canada Exports 1971-2018," Last accessed 15 April 2018. <https://tradingeconomics.com/canada/exports>.

⁵Conference Board of Canada, "Canadian Income Inequality: Is Canada becoming more unequal?" last accessed 20 April 2018. <http://www.conferenceboard.ca/hcp/hot-topics/caninequality.aspx>.

between median and average net worth increasing by 44 percent in just 10 years.⁶ This is not to suggest a direct causal link between inequality and the advent of NAFTA; however clearly free trade has failed to prevent Canadian inequality from increasing since its adoption. While unchecked inequality risks become a destabilizing influence, it is assessed that there is still time for the issue to be managed successfully.⁷

The evidence above implies that elements of Canadian policy have so far failed to adapt to this new economic reality, but there are indications that change is possible. For example, a universal basic income (UBI) is one moderately radical alternative that is being proposed to address growing inequality. The province of Ontario has already embarked on a tentative first step by implementing a trial basic income program in three communities, suggesting that the political will can exist to meet this challenge.⁸ Some critics have suggested eliminating free trade in order to check this trend; however this is not practical in the Canadian context.

Because its population constitutes too small a market to consume all of what it produces, Canada is reliant on maintaining a high volume of export-driven trade to sustain its economy. Unlike the USA, such a small market cannot support a complete high-value advanced manufacturing sector of its own. Between the geographic dispersal of its populace and competitive costs abroad, Canada is reliant on producers elsewhere for many such products. These interlinked factors make easy access to international markets a matter of vital importance.

⁶Statistics Canada, "Survey of Financial Security, 2016," last accessed 20 April 2018, <https://www.statcan.gc.ca/daily-quotidien/171207/dq171207b-eng.htm>; Parisa Mahboubi, "The High Cost of Canada's Increasing Wealth Inequality," *The Globe and Mail*, 27 December 2017.

⁷Konrad Yakabuski, "Income inequality in Canada: What's the problem?" *Globe and Mail*, last updated 25 March 2017, <https://www.theglobeandmail.com/news/national/time-to-lead/income-inequality-in-canada-whats-the-problem/article15470499/>.

⁸Canadian Broadcasting Corporation, "Ontario basic income pilot project to launch in Hamilton, Lindsay and Thunder Bay," last updated 27 April 2017, <http://www.cbc.ca/news/canada/hamilton/wynne-announcement-hamilton-1.4082476>.

Free Trade as a Security Issue

Given that NAFTA alone has stimulated such an increase in Canada's trade activity, it is clear that free trade agreements can be an effective way to build national wealth. The loss of a portion of Canada's trade as significant as NAFTA then would constitute an economic shock. Decreases in revenue would deprive Canadian institutions of resources needed to deliver the services that citizens have come to expect. Potential security effects would be interlinked, profound and widespread, including but not limited to: increased unemployment and poverty, reduced defence spending, and domestic political instability. Absent the development of some powerful new engine of growth then, the need to sustain free trade is thus tied to every aspect of Canada's domestic security. Free trade can also influence Canada's security beyond its borders.

Advocates of globalization often refer to a causal relationship between increased trade and decreased conflict between states. Building on Kelly and Thibaut's Interdependence Theory of power, liberal scholars like Polachek and Oneal have argued that countries dependent on each other economically would be unlikely to enter into conflict, because the costs of disruption would outweigh the advantages gained by fighting.⁹ For Canada, an implication is that economic interdependencies could underwrite its security without requiring the massive investments in "hard" military capability that could otherwise be required. This offers a tempting line of reasoning given the immensity of the potential cost savings, but it is not without flaws.

⁹Caryl Rusbult and Paul Van Lange, "Interdependence Theory," in *Encyclopedia of Power*, last accessed 20 April 2018. <http://sk.sagepub.com/reference/power/n190.xml>; Solomon Polachek, "Conflict and Trade," *Journal of Conflict Resolution* 24, no. 1 (1980): 56; John Oneal and Bruce Russett, "The Classical Liberals Were Right: Democracy, interdependence, and conflict, 1950-1985." *International Studies Quarterly* 41, no. 2 (1997): 267.

Some realists like Barbieri contend that international trade can actually *promote* conflict.¹⁰ In a zero-sum narrative, if a trade relationship entails an imbalance of dependencies; one country loses out to the other in some fashion. This can exacerbate tension between states rather than defuse it. Under this realist paradigm there are ample situations where Canadian trade relationships could be seen as unequal. Historically Canada has relied heavily on the export of low-value primary resources in exchange for higher-value secondary goods, resulting in large trade deficits with powerhouses like the United States or Japan.¹¹ This may not be a pretext for war, but to a realist it places Canada in a “subordinate” position and thus limits its freedom of action (this critique is examined more closely further in the paper). However subsequent scholarship has established considerably lower correlation between asymmetric dependencies and conflict, without discounting it entirely.¹² On balance then, Canada could indeed advance its security agenda through free international trade, but it will be important to build balanced partnerships to do so.

There are early indications that Canadian trade “disadvantages” may be diminishing on their own already. Canadian international trade is gradually shifting away from primary resource extraction towards the export of services and investment. For example, the C.D. Howe Institute points out that “in a quietly revolutionary reversal of history, Canadians now sell more high-

¹⁰Katherine Barbieri, “Economic Interdependence: A Path to Peace or a Source of Interstate Conflict?” *Journal of Peace Research* 33 no. 1 (February 1996): 42.

¹¹Statistics Canada, “Canada's Balance of International Payments (current account)”, last accessed 21 April 2018, <http://statcan.gc.ca/tables-tableaux/sum-som/l01/cst01/econ01a-eng.htm>

¹²Dale Copeland, *Economic Interdependence and War* (Princeton: Princeton University Press, 2014), 5; Paul Clarke, “Interdependence Theory, China, and American Security Interests,” (PhD thesis, Auburn University, 2006), 22.

value-added commercial services to the United States than they purchase from it.”¹³ Canadian financial, information technology, and management services are now globally recognized industries, and have become three of Canada’s top ten export sectors by value since 2005.¹⁴ If Canada can sustain this transformation, it has the potential to reduce or reverse long-standing negative current account balances by limiting susceptibility to global commodity prices.¹⁵ With the development of advantages such as these, free trade could actually become a vehicle for the development of Canadian power.

Canadian options are fairly constrained in terms of how it can develop and deploy influence internationally, particularly in traditional “hard” power terms. Canada’s interest in developing its military capacity is famously tepid, and there is little indication that this balance of priorities will change in the foreseeable future.¹⁶ However by virtue of Canada’s position as one of the world’s top ten economies, it can wield significant economic power to advance its interests abroad. A recent example is the renegotiation of the Trans-Pacific Partnership (TPP). Prime Minister Trudeau clearly felt confident enough to extract additional concessions from the

¹³Daniel Schwanen, “Free Trade Transformed Canada’s Economy,” *Globe and Mail*, last updated 27 March 2017, <https://www.theglobeandmail.com/globe-debate/free-trade-transformed-canadas-economy/article16124601/>.

¹⁴John Greenwood, “The services industry: Canada’s secret economic playground?” *McLean’s*, last accessed 21 April 2018. <http://www.macleans.ca/economy/economicanalysis/the-services-industry-canadas-secret-economic-playground/>.

¹⁵Stephen Poloz, “From Hewers of Wood to Hewers of Code: Canada’s Expanding Service Economy,” speech, C.D. Howe Institute, Toronto, Canada, 28 November 2016; Statistics Canada, “Canada’s Balance of International Payments (current account)”, ... ; Valery Charnavoki and Juan Dolado, “The Effects of Global Shocks on Small Commodity-Exporting Economies: Lessons from Canada,” *American Economic Journal: Macroeconomics* 6 no.2 (2014): 207–237.

¹⁶Public Safety Canada, “Securing an Open Society: Canada’s National Security Policy,” last accessed 16 April 2018, <https://www.publicsafety.gc.ca/cnt/ntnl-scrpt/scrng-en.aspx>; Department of National Defence, “Canada Defence Policy: Stable, Predictable, Realistic Funding,” last accessed 16 April 2018, <http://dgpapp.forces.gc.ca/en/canada-defence-policy/themes/stable-predictable-realistic-funding.asp>.

other TPP signatories by disrupting its joint announcement ceremony in a highly public way.¹⁷ This subsequently led to the incorporation of several progressive Canadian demands into the Comprehensive Progressive TPP (CPTPP). Given the face-saving sensitivity of the powerful Japanese in particular, this constituted a bold (and yet arguably successful) application of Canadian power.

Playing this hand has its limits however, as Trudeau learned within weeks of the announcement of the CPTPP. Chinese officials firmly rejected the inclusion of progressive elements into any free trade deal with Canada, and exploratory talks planned for early 2018 failed to materialize during a recent state visit.¹⁸ China has since made clear its intention not to back down from this position, so free trade between Canada and the Chinese appears elusive in the near term.¹⁹

Free Trade as a Threat?

Many of the discussions around security through liberalized trade would be academic if it were advancing unopposed. However there is an array of concerns that have the potential to halt or even reverse the gains that have been made to date. Beyond the direct risk to trade, elements of free-trade opposition reflect significant security issues in their own right. Resistance to

¹⁷Craig Jennett, "Screwed' by Justin Trudeau, Leaders Fume over Scuppered Trans-Pacific Partnership Deal," ABC News, last updated 10 November 2017, <http://www.abc.net.au/news/2017-11-10/tpp-talks-stall-after-justin-trudeau-canada-fails-to-show-up/9140250>.

¹⁸Hugh Stevens, "The Trouble with Canada's 'Progressive' Trade Strategy," OpenCanada.org, last updated 8 December 2017. <https://www.opencanada.org/features/trouble-canadas-progressive-trade-strategy/>.

¹⁹"China Wants No 'Progressive' Elements in Any Free Trade Deal with Canada: Envoy," iPolitics, last updated 10 April 2018, <https://ipolitics.ca/2018/04/10/china-wants-no-progressive-elements-in-any-free-trade-deal-with-canada-envoy/>.

liberalized trade can be roughly placed into two constituencies, here categorized into “nationalist” and “legal-sovereignty” camps.

The nationalists can be seen as realists who stand to lose economically from the redistributive effects of liberalized trade. Free trade tends to maximize production and consumption efficiencies, such that “legacy” industries who fail to keep up will be eclipsed by more efficient foreign competitors.²⁰ NAFTA has had just such an impact on several previously protected American sectors that employed relatively highly-paid and low-skilled workers. Pre-NAFTA regulation had precluded some manufacturing industries from modernizing their production models, for example.²¹ Workers elsewhere could produce similar products more cheaply, and many American manufacturers began operations in Mexico instead. Debate continues as to whether free trade is the direct cause of this effect, or if it simply hastens structural changes in the global economy that would have eventually occurred nonetheless. For instance, it is suggested that many US manufacturing jobs have been lost due to improved technology rather than being simply “moved” to a lower-cost labour market.²² Regardless, these disruptions are profound and create powerful narratives that cannot be ignored by governments.

The 2016 US presidential campaign provides a case in point. Both Donald Trump and Bernie Sanders ran for their candidacies on aggressively protectionist platforms, tapping into widespread resentment generated by a perceived decline in American industrial power. American policy shows every indication of accommodating this in practice, exemplified by recent

²⁰Steven Suranovic, “Production and Consumption Efficiency Gains from Free Trade,” last updated 31 August 2006, <http://internationalecon.com/Trade/Tch60/T60-11.php>.

²¹ Heather Long, “U.S. has lost 5 million manufacturing jobs since 2000,” CNN.com, last accessed 22 April 2018. <http://money.cnn.com/2016/03/29/news/economy/us-manufacturing-jobs/index.html>.

²² *Ibid.*

advantageous as a spur for economic growth, however it attracts various legal-sovereignist critics.

One subset of this group opposes trade liberalization on “hard” security concerns. Some are uncomfortable with the fact that modern free trade agreements like the Comprehensive Economic and Trade Agreement (CETA) contain binding arbitration mechanisms that allow private business entities to challenge state governments outside the domain of their national legal systems.²⁷ The intent is to ease trade by providing impartial legal recourse for all stakeholders, however critics argue that this amounts to an abdication of state sovereignty to an unaccountable entity. Others express concern that this is symptomatic of the growing power of transnational corporations, entities which may be beholden only to distant shareholders instead of local populations.²⁸

A second subset of this camp is concerned with “soft” aspects of human security. Many aspects of national trade regulations have come into force in order to address specific security issues that extend beyond simple economic protectionism. Examples *inter alia* include labour standards, environmental safeguards, property rights, and the protection of vulnerable populations. These critics argue that liberalization of trade threatens these vital protections by diminishing the state’s ability to implement and enforce them.²⁹ In this view the competitive nature of a liberal international order creates a “race to the bottom” in which economic growth trumps other aspects of security. Unlike the rise of nationalism, many of these concerns are shared broadly between developed and developing populations, and Canada is no exception.

²⁷Corporate Europe Observatory, “The Great CETA Swindle,” last accessed 23 April 2018, <https://corporateeurope.org/international-trade/2016/11/great-ceta-swindle>.

²⁸The Council of Canadians, “Trans-Pacific Partnership (TPP),” last accessed 23 April 2018, <https://canadians.org/tpp>.

²⁹Human Rights Watch, “Q&A: The Trans-Pacific Partnership,” last accessed 23 April 2018, <https://www.hrw.org/news/2016/01/12/qa-trans-pacific-partnership#2>.

From the depredations of Canadian mining companies in Papua New Guinea to the theft of Canadian technology by Chinese firms, examples abound inward and out.³⁰ However, notwithstanding these concerns, the opinions of Canadian voters towards free trade are nonetheless becoming more favourable as they become better informed.

In 2017, two surveys regarding Chinese free trade observed a significant shift in which a majority of Canadians expressed support for such an agreement for the first time. Analysis suggests this may be tied to perception of protectionist sentiment in the United States, and an understanding of the economic implications of the loss of NAFTA.³¹ This shift in attitudes toward free trade appears to be broadly bipartisan, yet it is still far from universal. In particular, a study by Nathan Allen of the Asia Pacific Foundation of Canada found elevated concern about free trade with Asia and other emerging economies linked to the issues discussed earlier.³² Such concerns diminished toward free trade with allies or developed nations like Japan. Allen also observed that:

Although attitudes toward engagement with Asia are shaped by several underlying dispositions toward foreign policy, misinformation and low information are also a challenge. ... It is not only misperception that affects attitudes toward trade agreements but also an absence of knowledge.³³

³⁰The Guardian, “Canada mining firm compensates Papua New Guinea women after alleged rapes,” last accessed 23 April 2018, <https://www.theguardian.com/world/2015/apr/03/canada-barrick-gold-mining-compensates-papua-new-guinea-women-rape>; *Ibid.*, “Four charged in Canada with selling stolen satellite equipment to China,” last accessed 23 April 2018, <https://www.theguardian.com/world/2016/feb/29/canada-charged-with-selling-stolen-satellite-equipment-china>,

³¹ Landriault and Minard, “Canada/China Free Trade Agreement ... ,” ... : 115.

³² Nathan Allen, “Keeping Rising Asia at a Distance: Canadian attitudes toward trade agreements with Asian countries,” *International Journal* 70, no. 2 (June 2015): 303-305.

³³ *Ibid.*, 303.

Indeed much opposition to free trade is based on inaccurate or incomplete information. As the Hillary Clinton campaign learned, this does not imply that leadership should dismiss these concerns as legitimate security issues when proposing increased free trade; rather they should actively address and mitigate them.

Opportunities Moving Forward

Domestically, it must be recognized that Canadian policy has failed to spread the benefits of free trade widely enough. Wealth and income inequality risk becoming a damaging force if left unchecked, and drastic initiatives like the Ontario UBI experiment may be required to meet this challenge. Inequality has been referred in some quarters as “the new global warming”, and it should be given commensurate attention.³⁴

The isolating effects of nationalism cannot be ignored either. Economic insecurity begets more economic security as markets are shut out of trade. Regular and sustained engagement with domestic and international audiences will be critical to showcasing the benefits of openness over withdrawal. Canada is advantageously positioned here because the mutual benefits of North American free trade can be upheld as a success. Diplomatic strategies can be built on the lessons from engagements ongoing with senior American state and federal officials to preserve NAFTA.

Success will require Canada to coordinate its information activities in an unprecedented way. The Canadian NAFTA experience demonstrates how critical the role of accurate, timely, and sustained information is in formulating public opinion on such complex policy issues.

³⁴Charles Blow, "Inconvenient Income Inequality," *New York Times*, 17 December 2011.

Support for free trade is relatively unanimous across the Canadian political spectrum, providing an ideal opportunity to send a unified message to prospective partners.

Canada's focus now needs to move further abroad. The resurgence of protectionism in the United States illustrates the frailty of hedging one's security on the goodwill of a single partner. The recent conclusion of CETA negotiations with the European Union provides a major step in the right direction, and this momentum should be pursued into new markets such as MERCOSUR, South Korea, the UK, and India.

The CPTPP in particular offers considerable promise because of the withdrawal of the United States from the earlier TPP: this agreement was thus drafted without representing the interests of the US or China. The significance is that if either of the world's two largest economies wants to enter the agreement, it will now be negotiating with a unified bloc of 11 signatories comprising 13 percent of the world's GDP.³⁵ Canada and its CPTPP partners would have unprecedented control over the agenda with respect to historically contentious issues like intellectual property rights, considered crucial to the development of a "knowledge economy".³⁶

Canada should seize this unique opportunity to re-engage with China.³⁷ The Chinese government needs to boost flagging economic growth, and Canada can now offer a trade deal with a large trading bloc instead of just one country. This would allow Canada more leverage to pursue key concessions on human rights, labour, and environmental protection. It would still

³⁵Kakali Mukhopadhyay and Paul Thomassin, "The impact of Trans-Pacific Partnership agreement on the Canadian economy," *Journal of Economic Structures* 7, no. 5 (2018), last accessed 22 April 2018, <https://journalofeconomicstructures.springeropen.com/articles/10.1186/s40008-017-0102-y>.

³⁶Michael Geist, "Don't Make the TPP Mistake Again: Why Canada Needs to Maintain a Progressive Approach on IP in NAFTA," last accessed 24 April 2018, <http://www.michaelgeist.ca/2018/01/dont-make-tpp-mistake-canada-needs-maintain-progressive-approach-ip-nafta/>.

³⁷Dominic Barton, "Beyond the CPTPP: Why Canada's Relationship with Asia Needs a Long-Term Strategy," last updated 1 March 2018, <http://www.asiapacific.ca/media/news-releases/51446>.

demand careful diplomacy and true understanding of the limits of Canada's influence, but nonetheless it offers a Canadian global leadership opportunity.

While it is wise to be realistic about what can be achieved in terms of hard power, Canada can and should use its economic clout assertively to secure its interests internationally. Increasing economic influence can be a self-sustaining feedback loop, used to build power over time, and so Canada should continue to tie its greater strategic objectives to trade negotiations. The recent events with the CPTPP and China indicate that there is a middle path open. If wise realists craft the next round of Canadian trade policy within its confines in order to secure maximum advantage, the margins of this path should widen with time.

Most contentiously, Canada must be prepared for things to fail. Should isolationist sentiment continue to build in the United States, it is entirely possible to see increased American withdrawal overseas. This could include a reduction in naval presence, increasingly critical to the free movement of goods. Given the long lead times required, Canada must begin urgently to recapitalize its navy to be ready to maintain its economic lifelines unaided.

Canada is well positioned to leverage its existing economic strengths, to better secure itself by developing interdependent global trading relationships. The rise of Asia in particular presents a singular opportunity for Canadian leadership in trade liberalization. The challenge facing policymakers is how to develop Canadian economic security without falling into any of the traps that lie down the path of free trade.

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