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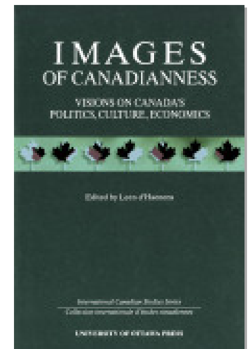

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ON TRACK FOR TAFTA?
DEVELOPING CANADA-EU TRADE RELATIONS IN THE 1990's

by Donald G. MITCHELL

I INTRODUCTION

Fish and fur; disputes over these two commodities have dominated the Canada-EU trading agenda throughout the last two years. As a result, the future of Canada's trade with its largest trading partner after the United States[1] is often seen in terms of obstacles instead of opportunities. While there are obstacles that do present a challenge to closer economic integration between the two areas, there are also enormous opportunities which a rapidly expanding European Union offers for Canada, and vice versa. While booming Asian markets and *promises* of an APEC (Asia-Pacific Economic Cooperation) free trade agreement have captured the attention of business and trading strategists worldwide, the development of regional cooperation and democracy in Asia has not maintained the same frenetic pace. This discrepancy in the world's most rapidly developing region threatens to spark trading wars or even something hotter. It also threatens to slow the momentum of WTO-sponsored trade liberalization.

In such a scenario, the introduction of a TAFTA (Transatlantic Free Trade Agreement) could provide the initiative and framework to launch a whole new wave of global trade liberalization. The world's two most integrated trading blocs, NAFTA and the EU, are arguably best-suited to initiate such change. The success of a transatlantic agreement in this role, however, depends upon its ability to shed the image of a *rich men's club* and introduce *substantial* reform that would have positive repercussions not just for the two trading blocs involved but for other parts of the world. The Canadian seizure of a Spanish vessel off the Grand Banks of Newfoundland just beyond the 200 mile-limit established by international law set off a furious political struggle between Canada and the European Union. A dispute with the Spanish had become by extension a dispute with the EU. Just as Canada was on the verge of beginning negotiations on the Canada-EU Action Plan – intended as the launching pad for greater economic integration and political cooperation – the fishing issue paralyzed negotiations.

Similarly, the possibility of an EU ban on fur caught with leg-hold traps threatened to sour good relations. Recently, however, the conclusion of a framework agreement on international humane trap standards in Brussels removed the threat of this ban. In

[1] After the United States, the European Union is the largest market for Canadian exports (7 percent of total exports) and is the source of 9 percent of Canadian imports. The United Kingdom, Germany, France, Belgium, Italy, and the Netherlands occupy third, fourth, seventh, eighth, ninth, and tenth positions, respectively, in the ranking of the top 100 Canadian export markets. DFAIT (Department of International Affairs and Trade), 1995.

December of 1996, the Canada-EU Action Plan was signed by EU Commissioner for External Economic Relations Sir Leon Brittan and Canadian Prime Minister Jean Chrétien. These two achievements suggest that it is no longer sufficient to merely study the problems at hand; there is a need to look to the opportunities that lie ahead. Other disputes may emerge – and this article will address potential future problem areas with particular regard to the enlargement of the EU – but there are also enormous opportunities which transatlantic trade liberalization would offer to both blocs.

A transatlantic free trade agreement (TAFTA) would, by the time it were negotiated, give Canada access to a single currency zone of more than 420 million people.[2] It would also link Canada to a trading partner that is in the unique position of expanding not just demographically but territorially and is likely to include close to half a billion people and twenty-five plus countries by the time the process of expansion is completed. Before launching into a discussion of the idea of a TAFTA, however, a number of other issues must be discussed: the current state of Canada-EU trade, the enlargement of the European Union, and future trade trends.

II OVERVIEW OF THE CURRENT STATE OF CANADA-EU TRADE

The European Union is Canada's largest trading partner after the United States, with total trade in 1995 worth an estimated US$29.8 billion. That same year, the European Union provided ten percent of all Canada's imports and was the destination for seven percent of its exports. Since 1976, the growth rate for Canadian exports to the EU has averaged 6.4 percent (Statistics Canada, 1996). In the past decade, Canadian exports to the EU have grown in value by seventy-two percent (Statistics Canada, 1996). Yet the most remarkable area of growth in economic activity between the two has been foreign direct investment (FDI). In 1995, twenty-seven percent of FDI in Canada came from EU countries. In the same year, over 20 percent of Canadian investment abroad (CDIA) was channeled into the EU. A decade previously, the figures stood at 17 percent and 12.4 percent respectively. In relative terms that represents an 59 percent increase in value of both CDIA in the EU and European Union FDI in Canada.

Measured in absolute terms, the change is even greater. European Union FDI in Canada increased between 1985 and 1995 from US$14.8 billion to US$33.5 billion, an increase of 126 percent. In the same time period, CDIA in the EU rose from US$6.7 billion to US$25.1 billion, a 275 percent increase. By comparison, over the same period, CDIA in the United States dropped from 54 to 53 percent of total CDIA and

[2] This estimate is on the basis of the advent of EMU (European and Monetary Union) and the introduction of a single currency, the *euro* in 1999. By 2005-08, when negotiations for a TAFTA might begin, the EU is widely expected to have expanded to include Poland (38.8 million people), the Czech Republic (10.4 million), Hungary (10.3 million), Cyprus (740 000), and possibly more Eastern and Southern European countries. That would bring the Union's current population of 370 million to over 420 million people.

the United States' FDI in Canada dropped from 76 to 65 percent of total FDI in Canada. These translate as relative decreases of two and thirteen percent, respectively.

2.1 Britain and Germany

Britain remains Canada's largest European trading partner, accounting for Cdn$5.47 billion in imports to Canada (2.4 percent of the Canadian total; almost a quarter of all imports from Europe) and Cdn$3.75 billion in exports from Canada (1.5 percent of the total; twenty-five percent of the European total). The UK is Canada's second largest source of FDI after the US and was the second largest destination for CDIA, surpassing Japan on both accounts. It is also the second largest market for business services. Great Britain acts as a gateway into Europe for many Canadian businesses which find common language and customs to be a business advantage. Many of the largest Canadian companies –names like Bombardier, Nortel, and Seagram's – have major investments in the UK. Similarly, over six hundred Canadian companies are owned or controlled by UK firms (Government of Canada, 1996). London also is Europe's preeminent (and one of the world's largest) financial centers. In the short-term, Britain's relationship with Canada is unlikely to change substantially. Longer term, however, in the context of Canada's relationship with the EU – in particular Germany – the primacy of Great Britain as Canada's principal European partner will be seriously challenged.

Since 1989-90, the strategic importance of Germany for Canada's European trade strategy has grown enormously. Through reunification, the Federal Republic grew to encompass 360,000 square kilometers and 81 million people, second only to Russia as Europe's most populous nation. Moreover, Germany provides the dynamic trade and investment link between Western and Eastern Europe. With companies like Volkswagen – who invested enormous amounts in the rebirth of Czech automotive manufacturer Skoda – leading the way, Germany's economic *Ostpolitik* is the catalyst for much of the economic growth in Central and Eastern Europe. Finally, the establishment of the EMI (European Monetary Institute) and as of 1999, the ECB (European Central Bank) in Frankfurt is likely to make it a rival if not a successor to London as Europe's preeminent financial center. That distinction will remain a point of contention for years to come; what is clear, however, is that Germany will be Canada's key European partner in the 21st century.

In Canadian *investment* terms, Germany is a distant second to the UK. In 1995, German FDI in Canada stood at US$4.97 billion (versus the UK's US$16.5 billion) and CDIA in Germany reached US$2.36 billion (versus US$13.8 billion invested in the UK). While Germany may lag behind the UK in terms of investment, its trade with Canada is growing at a far greater rate than that of the UK. In 1995, German exports to Canada reached US$4.8 billion and imports from Canada reached US$3.15 billion. The figures for Britain are US$5.5 and 3.9 billion respectively. A decade ago, the value of Canadian trade with the UK was close to double that of Germany. Today, it is

roughly seventeen percent greater.[3] The trend is clear and may even mean that Germany will surpass Britain as Canada's primary European partner *before* the end of the century.

Canada's third largest EU trading partner is France. The importance of France has increased as a result of an enormous boom in investment, tourism, and the service industry. Between 1985 and 1995, CDIA in France grew from Cdn$190 million to Cdn$1.9 billion and French investment in Canada from Cdn$1.5 to Cdn$5.3 billion. Tourists from France spent close to half a billion dollars in Canada in 1995 while services account for a third of total trade with an estimated value of Cdn$1.6 billion. In addition to the purely economic nature of this relationship, a cultural affinity with Eastern Canada has helped to foster closer ties between the two countries. For a real insight into the European Single Market, however, one needs to take a closer look at Belgium.

2.2 Belgium – The Single Market Test Case

Figures for Canada-Belgium trade are somewhat misleading if taken at face value. On one level, the figures overstate the volume of trade and on another, they leave out important commercial considerations. The barrier-free nature of the Single Market and its location as a northern European, coastal country mean that a significant volume of Canadian imports are registered as entering Belgium even though their final destination is elsewhere in Europe. To a degree unmatched elsewhere in Europe, Canadian companies have a strong local presence in Belgium. Bombardier, the aircraft/subway car manufacturer is the single largest employer in the Belgian town of Bruges. McCain, the Canadian frozen food conglomerate, has beaten the Belgians at their own game; it is the nation's largest producer of French fries in a country that invented the food!

The establishment of local subsidiaries has meant a drastic reduction in transportation costs to the export market and also provides these Canadian companies with tariff-free access across the EU market. Furthermore, the standardization of legal and technical norms across the EU has meant that companies can operate much more easily across the Union. A Canadian firm that has established a subsidiary or joint-venture within say, Belgium, is free to do business as far away as Greece or Finland with few technical restraints. The challenges and opportunities for foreign-owned subsidiaries operating in the EU were discussed by Buckley et al. (1995: 77-86). The authors examined the experience of ten Canadian firms that entered the European market. The companies were operating in sectors as diverse as lumber and satellite equipment yet shared comparable strategies and faced similar obstacles. While the degree of

[3] In 1985 Canadian exports to the UK were valued at Cdn$211 million and to Germany, at Cdn$104 million. By 1991, exports to the UK and Germany had risen to Cdn$2.53 billion and Cdn$1.995 billion, respectively. Aside from the enormous increase in both figures, the most interesting thing is how much Germany gained on Britain as Canada's prime European target for exports; the latter's lead dropping from roughly 100 percent to 20 percent to the current 17 percent.

commitment varied according to the financial means of the company, all the companies that had achieved success had done so by actively engaging themselves within the Single Market.

In the case of the lumber company, it was a case of creating a number of joint-ventures with local companies. Other wealthier firms, such as Bombardier mentioned earlier, have wholly-owned foreign subsidiaries in operation. Aside from the material gains to be had from a presence in Europe, those companies with a strong presence on the continent benefit from a better and more up-to-date understanding of the EU's complex legislative changes and opportunities. For many of these companies, it is a concern that "polarization of economies into major trading blocs is raising barriers to business between the leading world markets and that a direct investment presence in key consumer markets is necessary to achieve profitable growth" (Buckley et al., 1995: 83). This will be key in 1998 when the monetary union becomes a reality on May 1st. All participating currencies will be locked together on December 31st. The majority of EU countries will no doubt qualify. Three, Britain, Sweden and Denmark, will decline to participate, for the time being anyway, despite their technical readiness. Greece will certainly stay out because it cannot yet apply the required standards of economic and monetary rigour.

2.3 Central and Eastern Europe

What then about opportunities for Canadian business in Europe beyond the EU, more specifically, in the rapidly growing markets of Central and Eastern Europe? The Canadian private sector is working closely with DFAIT and CIDA (Canadian International Development Agency) to provide entrepreneurial expertise for the development of local business and investment opportunities for Canadians in the region. Much of CDIA and trade in Central and Eastern Europe has been focused upon construction, telecommunications, and other infrastructural projects. The success of these joint projects is evident from recent trade statistics.

Table 1: *Canadian Trade with the Visegrad Triangle Countries 1992-95*

	1992	1994	1995	% Growth '92-'94	% Growth '94-'95*
Czech Republic	**	96.67	138.77	**	43
Hungary	73.24	75.75	84.73	3.5	12
Poland	114.25	156.66	235.36	37	50

* millions of dollars

** independent figures for the Czech Republic are not available before 1994.

Amidst the general optimism about the emerging markets of Central and Eastern Europe, however, there is some cause for concern. An otherwise smooth last round of EU enlargement was ruffled by the problem of trade disputes between the EU, on the

one hand, and Canada and third-party countries on the other.[4] The entry of Sweden, Finland and Austria into the Union meant the extension of higher EU tariffs to these countries. As the EU undergoes future enlargements, Canada is likely to face future tariff increases to Central European markets which will, in all likelihood, mean reduced access to these markets. While Canadian trade with the Central and Eastern European countries (CEEC's) has not yet reached particularly large levels, it is growing extremely rapidly as the table above suggests.

When Austria, Finland and Sweden joined the EU, a dispute arose over higher tariffs on Canadian exports of seafood, aluminum, wood products, and snowmobiles to these countries. If one considers that these are the primary Canadian exports to Scandinavia and Austria, we can also confidently predict likely problem areas that Canada might face in the next round of enlargement. These will be: electrical equipment, machinery, construction materials (and contracts), and wood products, which constitute the largest share of trade between Canada and the CEEC's. Problems of trade diversion may also develop. While the rapidly expanding markets of Central and Eastern Europe are currently open to all external partners and Canada shares Most Favoured Nation (MFN) status with the Czech Republic and Poland (and GPT – General Preferential Treatment – agreements with those two plus Hungary), these advantages are likely to be erased by the future admission of these three countries into the EU. The extension of EU tariff barriers to Poland, the Czech Republic, and Hungary is likely to severely weaken Canadian competitiveness in these markets. As the EU grows to absorb not only these three but, in stages, seven other Eastern European countries which have signed Association Agreements with the Union, the problem threatens to recur at each stage.

In the last round of EU enlargement, it took eleven months for the Canadian government to negotiate a satisfactory compensation package for the higher EU import duties introduced on large number of products to Austria, Finland, and Sweden. Negotiations for previous enlargement rounds have taken up to five years and even today, there remain outstanding tariff compensation issues between Canada and the EU. How should Canada tackle these trade disputes?

The aim of the Canada-EU action plan is to resolve current trade/political sticking points and lay the groundwork for a free trade agreement. This, however, is both a long-term as well as an optimistic goal. In the meantime, Canada can try and coax the EU into a more cooperative stance by further developing its own existing regional trade agreements. Canada is a key member of NAFTA and is expanding trade with Latin America, most notably Chile, with whom Canada recently signed a free trade agreement.

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[4] This group is largely made up of WEOG countries (Canada, Australia, New Zealand, Japan) and the US; in other words, western industrialized countries not included in the Lomé Convention group of developing nations who enjoy tariff-free trade with the EU in almost all sectors.

The expansion of NAFTA would make Canada an increasingly attractive point of entry for European firms that want to gain access to the North-South American markets and force the EU to take steps to increase its appeal to its prosperous transatlantic partners. Yet at the same time, this runs contrary to Canada's wish to diversify its trading base – in other words, to reduce its dependence upon the US. Rather, in the case of Europe, Canada is trying to reinvigorate Canada-EU trade, with an eye to the coming attraction of an expanding, single-currency market with 370 million-plus people. A third strategy would be for Canada to publicly push for a lowering of EU tariffs rather than simply accept an extension of EU tariff levels with each successive wave of enlargement.[5] For this, there are two imperatives. Firstly, Canada cannot expect to do this alone. Rather, it must take advantage of its membership in the WTO and foster support for tariff reduction among WEOG countries who face the same obstacle in trading with Europe. Secondly, Canada must start this process of lobbying *before* each successive wave of EU enlargement begins. Rather than waiting till this loss of markets occurs and then applying for compensation to the EU afterwards, Canada must work to prevent this market restriction *beforehand.* Sympathetic to Canada's complaints, Dr. Lorenz Schomerus, State Secretary in the German Ministry of Finance, argues that European regional integration should not run counter to multilateral trade liberalization (Senate of Canada Report, 1996: 26).

III TOWARDS A EUROPEAN TRADING BLOC?

A recent European Commission report, *Reinforcing Political Union and Preparing for Enlargement,* calls for the EU to act more cohesively in the area of trade policy and representation in international organizations. Because of the disparate interests of its member states, "the Union's negotiating position is weakened in many cases (...) the Treaty [on European Union] should include provisions explicitly designed to enable the Union to speak with one voice and defend all the relevant interests more effectively" (European Commission Opinion, 1996: 26). The EU is trying to invigorate its economic and trade policy so as not to be outmatched by the booming economies of Asia-Pacific and Latin America and a resurgent United States. This is already evident in the number of cases of dispute settlement at the WTO in which the EU, rather than individual EU member states, has participated. A real European trade bloc, however, is unlikely to exist as long as the *Deutsche Mark* is competing with the *franc*, pound and *lira*. Only when the *euro* gathers strength, are we likely to see the emergence of a real European trading bloc.

Constant speculation about the fate of the *euro* experiment and EMU in general was silenced by the public launch in Dublin in December 1996 of the design for the *euro* paper notes. The event put to rest any doubts that even the most hardened skeptics had as to whether EMU would "fly". On January 1st, 1999, the new currency will be

[5] While standard EU tariff levels are quite low on many items (3.6 percent), there are a number of key sectors in which high tariffs make it very difficult for Canadian companies to compete in these European markets. For example, EU tariffs on telecommunications equipment – one of the world's fastest-growing and most lucrative sectors – were recently raised from 4.5 to 7.5 percent.

launched; now, it is simply a question of where. Will it be introduced in just six core countries: France, Germany, Austria, and the Benelux, or will it be extended to include Italy, Ireland, and the three Scandinavian member states as well? Some argue that an initial *mini-currency* union would not work for two reasons. Firstly, they claim, it would be difficult to differentiate between core and non-core countries when the decisions are based upon often very minor differences in economic performance. Secondly, to not admit a country that is very close to meeting the requirements for EMU membership – particularly if such a country has undertaken severe austerity measures as a means of doing so – risks provoking a popular backlash against EMU in that country. The most obvious example of this is Italy where a real effort is being made to bring the *lira* into line for 1999.

Instead, critics of the mini-currency approach argue in favour of a *maxi-currency* union that would include up to ten or eleven member states. This would, in theory, prevent the creation of a sufficiently large bloc of member states who might oppose the selection of core EMU members. Of course, this begs the question whether EMU is more an economic means to a political end or an economic end unto itself. While some argue that EMU is primarily a political goal, its potential economic advantages would be enormous: a genuine single currency market incorporating at least 200 million people at the outset which would attract investors previously turned off by the number of different currencies and their inherent exchange rate headaches.

IV FROM A G-7 TO A G-3?

The whole notion of a shift from a G-7 including Canada to a G-3 (the EU, the US and Japan) excluding Canada hinges largely on the success of EMU and the *euro* experiments. Even if it were adopted by ten EU member states in 1999, the *euro* would not become a reserve currency in the short term. Until the *euro* is perceived as a reliable currency, no one will want to exchange their reserve *Deutsche Marks* or dollars for it. Yet at the same time, it will not be perceived as a stable currency until businesses and banks put faith in it. This will leave the nascent currency in a difficult but not impossible position. The creation of a single currency and a European Central Bank (ECB) does not preclude EU member states acting individually on financial matters. There will be fifteen finance ministers of the ECB, one from each member state. Britain and possibly Italy will be left out of the EMU initially but that does not mean that they will cease to have a presence in international economic and monetary affairs.

The combination of the limited initial impact of the *euro* on reserve currency holdings combined with the fact that from its inception, EMU is not likely to incorporate all 15 member states mean that the shift from a G-7 to a G-3 configuration is unlikely to occur soon. Nevertheless, the emergence of a cohesive European bloc in international economic and monetary affairs at a later stage is inevitable, which would leave Canada as the awkward smaller partner at the G-7 table.

In spite of the potential offered by EMU, there has been a noticeable decline in the relative importance of the EU as a destination for Canadian exports. This is partially explainable by two distinct regional trends. Despite Canada's desire to move its trade strategy away from a dependence on the United States, the nation's share of trade with its southern neighbour has grown in relative terms at the expense of the transatlantic relationship. Much of the reason for this growth lies with the passage of the NAFTA which dramatically opened up trade and investment flows between Canada and the US. The second reason for this relative drop is because of a growth in Canadian trade with Latin America, China, Japan, and Southeast Asia. While trade among the APEC countries is booming and there is talk of creating an APEC free trade zone, discussions are moving at "a glacial pace" (The Economist, 1996, December 7: 15).

The slowing of European economic growth over the last two decades has meant a drop in the EU's share of Canadian trade. Nevertheless, as the statistics cited earlier show, Canada-EU trade continues to show robust growth. The sheer size of the European market ensures its value as a target for Canadian business. In spite of sluggish growth rates – the forecast average for EU growth in 1997 is 2.3 percent – the EU market is so lucrative and integrated that its GDP grows by US$200 to 220 billion annually, the equivalent of discovering a market the size of Taiwan's each year.

As Peter Cook (1996, October 2: 3), the *Globe & Mail*'s Brussels-based correspondent argues, "the value of the European market is that it corresponds exactly to Canada in terms of income levels and economic needs and is somewhere where we have a great deal of success selling high value goods" and, he continues, "with a single currency, that will be enhanced." The implications of a single currency for the world's largest trading bloc are enormous. The US dollar remains the world's global currency. Although this will not change overnight, the emergence of the *euro* threatens to eventually topple the dollar in *some* parts of the world as the reserve currency of choice. As the EU grows – with EMU to eventually incorporate all member states – and develop closer ties and freer economic trade with the New Independent States and Mediterranean rim countries, the whole idea of the *euro* as a reserve currency gains greater credibility.

Imagine the European Union thirty years from now. Its large elderly population – Europe's Achilles heel and the single largest reason demographers depict a doomsday scenario for Europe – will have largely died off. It will be a bloc of twenty-five plus countries with a single currency spread across most of its constituent countries and a young, well-educated population of close to 450 million.

Contrast this with Southeast Asia where in many areas, the inability of democratic development to keep pace with economic growth and a failure to organize closer economic cooperation threaten long-term prosperity in the region. Admittedly, the enormous diversity of the Southeast Asian nations – a fact which many westerners fail to recognize – makes APEC's challenge for the 21st century a daunting one. Nevertheless, without a solid framework for regional dialogue, rising economic

competition threatens to ignite political disputes. Such a scenario is not, I will stress, a short-term trend. It is clear that the momentum lies with the Asian emerging markets both now and in the coming decades. Longer-term, however, it remains to be seen how well these economies will sustain their growth.[6]

V THE BACKGROUND TO TAFTA

If a larger, leaner EU offers major opportunities in the coming century to Canada, what does an EU-NAFTA free trade agreement represent? Ideally, TAFTA would create a free trade zone representing close to fifty percent of the volume of world trade. It could also act as an enormous catalyst for global trade liberalization. By uniting the world's two single largest trading blocs, it could establish a precedent for future cooperation.

Here too, this begs the question of whether such an agreement is primarily economic or political in intent. Ultimately, the whole notion of TAFTA serves as an economic means to a political end. By this I mean that the economic gains of such a free trade agreement would be neither enormous nor sudden.[7] While these gains would be by no means insignificant, the political value of such an agreement outweighs the economic advantages.

What are the practical gains to be made? Firstly, exposing industry to transatlantic competition (and this is particularly true of European industry) would force it to become far more efficient and, by extension, more competitive. If European industry were able to open up to transatlantic competition and weather the major phase of restructuring that would be inevitable for it to survive such competition, it would find itself with tariff-free access to the entire NAFTA market including the rapidly growing Mexican and possibly even the Chilean economy.[8]

[6] This is the thrust of an article by Gerald Segal (1996) in which he argues that in future: i) the peaking of Asia's demographic bulge, ii) a decline in traditional family networks/rise in welfare costs, iii) flagging APEC activism, and iv) declining growth rates will all bring about a slowing in the Asian economic boom. This, Segal argues, combined with the onset of a single European currency, reform of the welfare state, and the "dying out" of the older generation will mean a radical rejuvenation of the European continent. While this is not likely to happen as nearly as Segal implies, some of his arguments do hold some validity and help to define Europe's value to Canadian trade in the 21st century.

[7] This opinion is expressed by a number of contemporary commentators on transatlantic trade, including Robert Wolfe of the Queen's University Public Policy Center. Thomas J. Duesterberg (1995), formerly assistant secretary of commerce for international economic policy in the US government, argues that any such trade agreement must be seen in terms of what Zbigniew Brezinski calls the "geopolitical situation." Duesterberg (1995: 77) concludes: "Non-economic factors in favour of an EU-NAFTA free trade and investment agreement may be more compelling, in fact, than the economic considerations."

[8] While Mexico is a fully integrated member of NAFTA, Chile signed a free trade agreement with Canada in December, 1996 and enjoys low-tariff trade with Mexico through the MERCOSUR trading arrangement but does not yet have a free trade agreement with the United States.

Trade blocs such as the EU and NAFTA are increasingly inward-oriented. Although this is inevitable to a certain extent, when the proportion of regional trade as a percentage of total trade exceeds seventy percent, as is the case with the EU, the bloc risks reaching an unhealthy balance.[9] An EU-NAFTA free trade agreement would give the EU a means of increasing its market share of extra-European trade, which has fallen significantly since the Single European Act in 1986.

A transatlantic agreement would give NAFTA countries access to the emerging markets of Central and Eastern Europe, the Mediterranean rim (Turkey, Cyprus, Algeria, Tunisia) and the New Independent States (NIS) on the same terms as currently enjoyed by EU member states based on the Association Agreements which these countries have signed with the EU. While the economies of Russia and its NIS neighbours continue to perform sluggishly, experiencing low or even negative economic growth, they hold huge potential one or two decades from now. For all its faults, the Soviet Union did an excellent job of educating its citizens. Many of the countries of the former Soviet Union also have enormous natural gas, oil, and other mineral reserves. While the region is still sorely lacking in capital for investment, a well-educated labour force combined with enormous energy resources provide it with the key elements for future growth.[10]

Despite the potential benefits, there are many obstacles to the development of a TAFTA, most of which stem from an absence of political will. The most frequent criticism of the NAFTA proposal in the run-up to its signing in 1988 was that Canada and the US would be unable to compete with Mexico where labour costs were dramatically lower. The laws of comparative advantage prevented this from becoming a problem. Nevertheless, the belief that freer trade will mean job losses remains and politicians on both sides of the Atlantic are reluctant to push for further trade liberalization if it threatens their popularity in any way.

With the deadlines for EMU and EU enlargement looming, the Union is unlikely to devote much time to developing a TAFTA in the next decade. This stems not so much from lack of will – the NAFTA market is eyed hungrily by those in Brussels – but from lack of time. The EU is simply too preoccupied with ongoing projects at the moment to devote the necessary attention to developing such an agreement.

If political will is the single greatest obstacle to the development of a TAFTA, what chance does such an agreement stand? As a sweeping free trade agreement covering all aspects of trade, none. As a smaller-scale initiative aimed at freeing up trade in a few, clearly-defined sectors and goals, it stands a much greater chance of succeeding. Moreover, the political rewards of such an effort could be reaped before an agreement is even signed. The onset of meaningful discussion of trade liberalization, let alone negotiations, would breathe new life into a static transatlantic agenda.

[9] Cfr. Duesterberg (1995: 77).

[10] The most vigorous advocates of this view are Richard Layard & John Parker (1996).

VI THE PRACTICAL FRAMEWORK

Firstly, we must define what an EU-NAFTA free trade agreement would logically consist of. There are three main areas to be targeted for liberalization: trade, investment, and industrial standards. What sectors should be tackled first? It is perhaps easiest to answer this question negatively, i.e., by identifying what should *not* be tackled first, namely, agriculture and textiles. The difficulty with which textiles were incorporated into the GATT negotiations and the controversy surrounding agricultural subsidies in North America and even more so in Europe make these an inauspicious area to deal with first. Even though the potential gains are enormous, tackling agriculture would be so complex that it would be more likely slow the momentum for liberalization in other sectors than achieve real progress.

A better area in which to start would be foreign investment. As the figures quoted towards the beginning of this article suggest, transatlantic investment is already so prevalent that the removal of restrictions in this sector would, in all likelihood, prove to be a *relatively* non-complex place to begin. A successful start to TAFTA negotiations in this sector would provide it with the impetus necessary to tackle more complex and controversial sectors. Yet even changes to current investment rules would not be without controversy as measures such as local-hiring quotas for foreign subsidiaries would come under scrutiny.

Telecommunications, computing, and other high-technology industries have been the focus of much attention recently. One of the principal aims of the recent WTO conference in Singapore was to launch trade liberalization in this booming sector. Yet initiating real change will be difficult in an industry in which every country wants to champion the cause of its own national firms so as to ensure a competitive share in what is widely-viewed as the high-growth industry of the next century.

The impending conclusion of the Mutual Recognition Agreement (MRA) between Canada and the EU on product standardization will eliminate many of the technical headaches associated with trade liberalization. The agreement could also pave the way for transatlantic harmonization of other regulatory legislation. Ultimately, these agreements would provide an incentive (i.e.: common standards) for EU countries to orient more of their trade towards the NAFTA markets, and vice versa.

Some have argued that TAFTA represents a threat to global trade liberalization.[11] Critics argue that such an agreement risks creating a "rich men's club," tacitly endorsing the idea that trade liberalization is best reserved exclusively for the western industrialized world. Certainly, the main economic motivation behind such an

[11] Bergsten (1995: 105-20), a former adviser to the APEC, argues that "as the urgency of competitive liberalization has accelerated, the regional approach has increasingly come to the fore [in which] regional groupings are demonstrably willing to proceed more boldly." While Bergsten acknowledges that the "fears of some that regionalism would derail globalism have been overcome to date," he sees a veiled threat in a TAFTA.

agreement lies with the fact that the European markets share a similar standard of living and are consequently an ideal market for Canadian products. In this sense, TAFTA is a consciously western-oriented idea. On the other hand, the EU and NAFTA also represent the two most sophisticated and integrated trading blocs in the world and are arguably in the best position to forge ahead with global trade liberalization.

It is crucial that the WTO be seen as an integral part of the development of a TAFTA. In other words, a TAFTA must not be perceived as a final act but rather a step on the road to WTO-sponsored *global* trade liberalization.[12] If that could be achieved, then a TAFTA would be much more likely to gain the popular support needed to be able to shed its "rich men's club" image and gain serious, widespread consideration. The single most important step in this direction over the last three years has been the conclusion of the Canada-EU Action Plan signed in December in Ottawa by Prime Minister Jean Chrétien and EU Commissioner Sir Leon Brittan.

The plan is the most wide-ranging agreement of cooperation achieved since dialogue began with the 1976 Transatlantic Framework Declaration engineered by former Canadian Prime Minister Pierre Trudeau. Encompassing economic, political, and trade relations as well as technical cooperation, the Action Plan aims to eliminate the potential for disagreements such as the recent fishing dispute and lay the foundation for closer, lasting ties. More specifically, the Action Plan calls for a joint study into the removal of remaining trade barriers and incorporates agreement on labour rights and *extraterritoriality*, the issue at the heart of the Grand Banks fishing dispute (European Commission, 1996). The Action Plan should also ensure a speedy conclusion to the MRA which, as the *Cassis de Dijon* case did for the EU in the mid-1980's, would eliminate testing of Canadian products entering the EU and vice versa.[13]

Delays in the conclusion of the Canada-EU Action Plan threatened to derail the project entirely. Had this occurred, at a time when the United States had already reached a wide-ranging agreement with the EU, Canada would have risked losing much of its influence in the transatlantic forum. The MRA, however, is a sign of the reverse.

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[12] Former US Secretary-of-State Warren Christopher was quoted as saying "any free trade agreement must advance our key objective of global trade liberalization; it must be compatible with an effective WTO and not disadvantage developing nations." Taken from Wolfe (1996: 365).

[13] The landmark legal case, named for the liqueur that a French importer was attempting to export to Germany, eliminated the need for national testing of products being traded within the EU.

VII CONCLUSIONS

When, if ever, will a TAFTA occur? In the next decade? Unlikely. Neither the EU, which is too preoccupied with EMU and eastern enlargement nor North America, absorbed by closer economic integration with Asia and South America is ready to initiate serious discussion on the matter. This does not mean, however, that a transatlantic agreement is just a pipe dream. A TAFTA would offer significant opportunities to its members. Rather, the problem lies with the fact that the potential economic benefits of such an agreement would neither be immediate nor immediately apparent. Consequently, discussion of a TAFTA tends to get de-prioritized in favour of issues perceived to be more pressing.

The second problem a TAFTA faces has to do with the current economic climate. In a boom cycle such as much of the world is enjoying now, there is little incentive to alter any of the existing political structures. The 1996 US presidential elections are a good example of this. Bill Clinton was re-elected not so much because of his personal popularity but because the majority of the electorate believed that government continuity was the best way to ensure sustained economic growth. In short, *if it ain't broke, don't fix it.* For similar reasons, the idea of a TAFTA is currently not a popular one.

In the words of a former US government official, "what is lacking now, perhaps, is the crisis atmosphere that [...] engenders heroic wisdom and leadership" (Duesterberg, 1996: 80). It may indeed be the case that in less prosperous times, when *political* solutions are sought for economic woes, a transatlantic free trade agreement will come to be more clearly recognized for the potential it holds. In the absence of such an agreement, Canadian business must take advantage of the many opportunities that the European Single Market offers and increase its presence within the EU. Only by fostering trade ties between the two continents *now* can the foundations be built for a transatlantic free trade agreement in the future.

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