

Canada and the China Question

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In 1891 a professor at the University of Toronto, Goldwin Smith, wrote a famous and highly controversial book call *Canada and the Canadian Question*. He argued that Canada was an unnatural and artificial entity. He maintained that the Canadian system of government was inferior to the American model and that Canada was an absurdity for geographic, ethnic, economic and political reasons. Its ultimate destiny, he thought, would be absorption by the United States.

Generations of Canadian political leaders have proven Goldwin Smith wrong. In the 21st century the country faces another important and equally controversial question. Is Canada prepared to move out of the American orbit and align itself with the new world order envisaged by China? The future of Canada-China relations to say nothing of Canada's economic prosperity depend on the answer to that question.

This paper places the discussion in the context of Canadian history and surveys the Canada-China relationship since establishment of diplomatic relations in 1970. It outlines arguments in favour of a free trade agreement and lessons of the recently concluded China-Australia Free Trade Agreement. The article points out obstacles and impediments to closer Canada-China relations and concludes with an answer to the China question.

An Overview of Canadian History and Economic Policy

After the settlement of Quebec in 1608 the area now called Canada was, for 150 years, a small French colony never exceeding 60,000 people. Its main economic activity was the provision of beaver and other furs to the European market.

Ceded to Britain in 1763 the colony was transformed when the American Revolution resulted in an influx of settlers who preferred to remain under the British Crown. Some military battles with the Americans ensued including the war of 1812 but aside from some skirmishes and border issues Canadian-American relations have been peaceful for 200 years. Due to migration English soon replaced French as the dominant population and fishing and farming replaced furs as the main economic activity.

A Westminster form of representative and later responsible government was established between 1791 and 1848 culminating in 1867 with the Confederation of four separate colonies into the present day Canada.

For fifty years Canada was a self-governing British colony with an economic plan known as the National Policy.² The pillars of the National Policy were immigration to expand the population and fill the empty lands of western Canada; railways to unite the disparate colonies that stretched

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² See P. Russell, *The National Policy 1879-1979*, *Journal of Canadian Studies* vol 14, 1979. Also John H. Dales, *The Protective Tariff in Canada's Development*, University of Toronto Press, Toronto, 1966.

from the Atlantic to the Pacific ocean and tariffs designed to protect the Canadian market. The major source of capital came from Britain.

In 1911 an election was fought on the issue of free trade with the United States but the Liberals who favoured free trade were defeated by the Conservatives who favoured continuation of the National Policy.

Canada's participation in the Great War (1914-1918) led to significant changes both economic and political. Canada was an independent signatory to the Treaty of Versailles which ended the war and this was the first step toward full independence granted by the *Statute of Westminster (1931)*.

The Second World War had an even greater impact. Canada emerged with the third largest standing army and one of the healthiest economies. Oil was discovered in 1947 and American capital replaced British capital in the development of Canadian natural resources.

American companies began to create subsidiaries in Canada to avoid tariffs and to serve the growing Canadian market. The National Policy was never officially rescinded but it gradually gave way to increased continentalism. This produced a reaction known as economic nationalism.³ The basic idea was that Canadians were willing to put up with a slightly lower standard of living compared to the USA, a slightly more limited variety of consumer goods, a lower dollar, and various other inconveniences in order to maintain their identity as a separate country.⁴

In 1967 Canada celebrated the centenary of its creation and amid much enthusiasm and patriotism a new Prime Minister, Pierre Elliot Trudeau, was elected in 1968. One of his early acts was to establish diplomatic relations with China. He also undertook a review of Canadian foreign policy which resulted in a proposal for a so-called Third option. The Third Option called for more diversification and relations with other countries mainly Europe. The idea was to reduce dependency on the United States and vulnerability to adverse decisions by American policy makers.

For example in August 1971 President Richard Nixon introduced a ten percent import surcharge designed to counter the increasing presence of Japanese goods in America.⁵ The policy blindsided Canada which was actually America's largest trading partner and Mr. Nixon exacerbated the situation by continually referring to Japan as the largest partner. Canadian attempts to obtain an exemption from the import surcharge were largely ignored.⁶

Trudeau's Third Option was never implemented and in the 1980s economic nationalism suffered a major setback when Ronald Regan and Prime Minister Brian Mulroney signed the Canada-United States Free Trade Agreement. It led to even closer integration of the two economies.⁷ The

³ Abe Rotstein and Gary Lax ed., *Getting It Back: A Program for Canadian Independence*, Clarke Irwin, Toronto 1974.

⁴ D.L.B. Hamelin, ed., *The Price of Being Canadian*, Canadian Institute on Public Affairs, Toronto, 1961.

⁵ See Richard N. Cooper, Trade Policy is Foreign Policy, *Foreign Policy* vol 9, Winter 1972-73, Also Douglas A. Irwin, The Nixon shock after forty years: the import surcharge revisited, *World Trade Review*, vol 12, No. 1, January 2013.

⁶ Bruce Muirhead, From Special Relationship to Third Option: Canada, the U.S., and the Nixon Shock, *American Review of Canadian Studies*, Autumn 2004.

⁷ Peter Morici, *A New Special Relationship: The Free Trade Agreement and U.S.-Canada Economic Relations* The Institute for Research on Public Policy and the Centre for Trade Policy and Law at Carleton University, 1991.

Canada-United States trade agreement was subsequently expanded into the North American Free Trade Agreement (NAFTA) to include Mexico.

The effects of NAFTA and free trade agreements generally were and continue to be hotly debated by economists and members of the general public. Proponents see them as a win-win situation with lower prices and increased choice for consumers. Critics see them as a wholesale transfer of jobs from high wage countries to lower wage countries which have decimated employment among the middle class in both the United States and Canada. They are blamed for an increasingly inequitable distribution of income. This debate is rehearsed in every election and is particularly significant during the 2016 American election campaign. Both Democratic and Republican candidates characterized the agreements as part of a corporate agenda and promised major changes if not outright renunciation. The impact of such policies for Canada would be considerable.

The brief survey of Canadian history raises a number of points to be kept in mind when considering relations with China.

- Canadians have an ambivalent relationship with the United States. They appreciate the economic benefits of living beside a rich neighbor but are cautious about possible loss of sovereignty or simply being culturally swamped.
- Canadians, more so than Americans, are willing to accept government involvement in the economy to provide services the private sector is unwilling or unable to provide.
- Exports have always been key to the Canadian economy but Canadians are not unanimous in their support for free trade agreements.
- There are important political and cultural traditions that distinguish Canada from the United States.

Canada China Relations

Economic relations between Canada and China have expanded considerably since the People's Republic was proclaimed. In the early years the issue of trade policy was closely tied to the debate over whether to grant official recognition.⁸

By the late 1950s successive years of poor harvests in China had created a profound food shortage. Despite a United States led economic embargo of China, Canada decided to sell large quantities of wheat and barley to China. Exports grew from about \$9 million in 1960 to over \$185 million by the end of the decade.

Following the establishment of diplomatic relations a Canadian-Chinese Trade Agreement was signed in 1973. It allowed for the mutual extension of "most-favoured nation" status – each country agreed to apply import tariffs against one another that were as low as those applied against other "most-favoured nations." That same year, a Canadian trade fair was held in Beijing, attracting about 600 Canadian officials and business leaders. It was the first such foreign trade fair attended by Chinese Premier Zhou Enlai. In addition, the two countries established a Joint

⁸ S. Beecroft, *Canadian Policy Towards China, 1949–1957: The Recognition Problem*, in Paul Evans and Michael Frolic eds. *Reluctant Adversaries: Canada and the People's Republic of China, 1949–1970*, University of Toronto Press, Toronto, 1991.

Economic and Trade Committee that provided a forum for discussion of economic and trade-related concerns between Canadian and Chinese officials.

Canadian exports to China had doubled by 1973. So too had Chinese exports to Canada. As the Chinese market became more accessible, Canada began to export a wider variety of products. By 1978, wheat's share of total exports to China had fallen to 69%. Sulphur, wood pulp, newsprint and metals such as aluminum and copper all emerged as significant exports.

Following the death of Chairman Mao, economic reforms, known as the Open-Door Policy, were aimed at reforming the national economy and lifting the restrictions on foreign commercial relations. The policy had four components: the creation of special investment zones; the attraction and efficient investment of foreign capital; increasing foreign trade; and the import of modern technology and management techniques.

From the perspective of Sino-Canadian trade, China's 1978 economic reforms led to a considerable increase in the number of formal trade policy initiatives between the two countries. The Canadian Department of External Affairs established the Canada-China Trade Council, later renamed the Canada China Business Council (CCBC). The organization was to act as a link between the two countries to further trade relations.⁹

The Canadian-Chinese Trade Agreement was revised and a Treaty of Chinese-Canadian Economic Co-operation was signed. This latter treaty defined the potential contribution that Canada could make to Chinese economic development in a number of high-tech goods and services, notably in the areas of light industry, communications, the construction of power stations, petroleum and coal exploration, and various mining projects.¹⁰

In 1980 Canada granted "preferential" trade status to China, reducing tariffs on imports by over one-third from the regular "most-favoured nation" tariff rate. However, many products were excluded from this agreement, meaning that the actual effects of "preferential" status were relatively minor. Four years later, in an effort to support Canadian marketing efforts in China, the Export Development Corporation concluded an agreement with the Bank of China for a \$2-billion financing facility to support the purchase of Canadian equipment and services. In 1986, the two countries signed a double-taxation agreement, ensuring that goods produced in one jurisdiction and sold in the other would not be subject to overlapping taxation.

Chinese exports to Canada grew exponentially between 1978 and 1988, averaging an increase of 26% per year. While Canadian exports to China did not match this growth rate, the increase was still considerable. From 1978 to 1988, Canadian exports to China grew by an average of nearly 18% per year.¹¹ By 1980, two-way trade had grown to just over \$1.0 billion. By 1987, that figure had more than doubled to \$2.2 billion; one year later, it had increased to \$3.6 billion. By 1988, China was Canada's sixth-largest trading partner worldwide.

Problems began in 1989 after protests in Tiananmen Square. Canada recalled its Ambassador and the House of Commons unanimously condemned the actions of the Chinese government. Most governmental relations came to a halt and in 1992 three Canadian Members of Parliament, were

⁹ Michael Holden, *Canada's Trade Policy and Economic Relationship with China*, Parliamentary Research Branch Paper PRB 04-32e, November 2, 2008.

¹⁰ *Ibid.*

¹¹ *Ibid.*

expelled from China after meeting relatives of the dissidents and trying to organize a public demonstration.

Later in 1992 a five day Ministerial Trade Mission marked restoration of some government to government relations. Canada promised to support China's membership in the GATT, forerunner to the World Trade Organization. The election of a Liberal government led by Jean Chrétien in 1993 marked a full return to the politics of engagement.

In 1994 Prime Minister Chrétien made the first Team Canada trade visit to China, bringing nearly 500 political and business executives with him. In 1996 the Chairman of the Standing Committee of the National People's Congress visited Canada as did the Vice Premier and Foreign Minister. Atomic Energy of Canada Limited signed a contract with the China National Nuclear Corporation for the sale of two CANDU-6 reactors

In 1997 President Jiang Zemin paid a state visit to Canada after attending the APEC Meeting in Vancouver. During the visit the two sides agreed to build a 21st century-oriented China-Canada partnership and signed many agreements. In 1999 Premier Zhu Rongji made a week-long visit to Canada. The two sides signed the Environmental Cooperation Action Plan, A Memorandum of Understanding on Cooperation in Combating Crime and three Protocols on Quarantine and Health Requirements.

In 2001, 2003 and 2005 Prime Ministers Chrétien and Martin led Team Canada trade delegations one of which was the largest trade mission in Canadian history with nearly 600 participants, eight provincial premiers and three territorial leaders. Dozens of agreements were signed including a strategic partnership which provided a framework for future relations..

Canada's official policy toward China has not changed since the those days. The policy is

- to work with China towards China's greater adherence to internationally accepted standards on human rights and the rule of law;
- to ensure that China's economic rise benefits Canada by increasing two-way trade and investment in goods and services;
- to work with China to advance shared interests such as health, the environment, and regional peace and security; and
- to position Canada as a preferred destination for Chinese immigrants, students and visitors.¹²

The election of the Harper government in 2006 signaled a change in the relationship. In one of his early speeches Mr. Harper said that human rights would play a much larger role in Canadian foreign policy. Regarding China he said specifically that Canada would not "sell out" important Canadian values to promote trade with China.¹³

In 2006 Parliament conferred honorary Canadian citizenship on the Dalai Lama and the following year the Prime Minister met with the Dalai Lama in his parliamentary office causing the Chinese Embassy to protest this as interference in China's internal affairs.

¹² Foreign Affairs and International Trade Canada, *Canada-China Relations*, http://www.canadainternational.gc.ca/china-chine/bilateral_relations_bilaterales/China-FS-Chine-FD.aspx?lang=eng

¹³ <http://www.cbc.ca/news/world/won-t-sell-out-on-rights-despite-china-snub-pm-1.570708>

In 2013 after much negotiation the China National Offshore Oil Company purchased Nexen, Canada's 6th largest oil company for 15 billion dollars. The sale was approved by the Harper government but it announced that future sales to state owned enterprises would be allowed only in exceptional cases.

Mr. Harper did made two visits to China in December 2009 and in February 2012. President Hu Jintao visited Canada for G20 meetings in June 2010. During the Harper years the Canada-China Investment Treaty and the Canada Hong Kong tax Treaty were signed and in 2015 Toronto became the first RMB trading hub in North or South America.

Canadian imports from China continued to grow reaching 65 billion in 2015. Exports grew somewhat reaching 20 billion the same year.¹⁴

The 2015 Election and its aftermath

Relations with China were not discussed to any great extent during the 2015 election which saw Mr. Harper defeated by Justin Trudeau and the Liberal Party. Trudeau's first meeting with Chinese President Xi took place in November 2015 at the G20 meeting in Turkey. Mr. Trudeau said he wanted to set a fresh approach in the relationship. The Chinese President said that his country would always remember the bold initiative of Pierre Trudeau in establishing diplomatic relations. A former Canadian Ambassador to China observed that China tends to associate the good times to eras when the Liberals are in power. The challenge, he noted, "will be to move the relationship beyond some nostalgic notion of Canada-China relations and advance Canadian interests with a really important global player."¹⁵ The same point has been made by other China experts.

There have been calls for a quick and substantial set of policy adjustments to put Canada back on track after a decade in which the engagement of China was intermittent, conflicted and narrowly economic. While deeper and broader engagement of China is in Canada's national interest, simply turning back the clock to the strategic partnership of a decade ago is neither wise nor likely. Rather than a restoration we need a reinvention based not merely on past foundations but on a new narrative that is more ambitious and more strategic.¹⁶

Other voices have called for a new approach to Canada China relations and even the possibility of a Free Trade Agreement.¹⁷ Peter Harder, President of the Canada China Business Council and John Manley, president of the Canadian Council of Chief Executives argued that "China is looking around the world to build stronger trading relationships. Its negotiators have concluded

¹⁴ http://www.canadainternational.gc.ca/china-chine/bilateral_relations_bilaterales/China-FS-Chine-FD.aspx?lang=eng

¹⁵ Canadian Press, November 16, 2015, <http://www.nationalnewswatch.com/2015/11/16/trudeau-vows-to-strengthen-china-relations-as-xi-praises-vision-of-pms-dad/#.VkpFZ03lsdV>

¹⁶ Wendy Dobson and Paul Evans, Living with Global China, in Asif B. Farooq and Scott Mcknight, *Moving Forward: Issues in Canada China Relations*, Asian Institute, University of Toronto and China Open Research Network (CORN), Toronto, 2016, p. 3.

¹⁷ Wendy Dobson and Paul Evans, The Future of Canada's Relationship With China, Institute for Research in Public Policy, Montreal, November 2015; Laura Dawson and Dan Ciuriak, *Chasing China*, Dawson Strategic and Ciuriak Consulting, January 2016; Asif B. Farooq and Scott Mcknight, *Moving Forward: Issues in Canada China Relations*, *op cit*.

14 free-trade agreements in recent years, and five more are in the works. China is on the move. It's time for Canada to join the action."¹⁸ Even a former Conservative minister of Foreign Affairs, Peter Mackay, said he thought the new government should pursue opportunities with China.¹⁹

The Business Council of Canada and the Canada-China Business Council commissioned a report in January 2016 asserting that a Canada-China free trade deal would create 25,000 jobs and add almost \$8 billion to the economy within 15 years. The report attempted to quantify the impact for Canada using 33 sectors covered in the China-Australia Free Trade Agreement to estimate the likely outcome for an agreement with Canada.²⁰

It argued that a free trade agreement with China would result in about \$7.8 billion in increased GDP by 2030 in value terms, a boost of about 0.14 percent in real terms²¹ The comparable gains for China are about \$5.6 billion or about 0.02 percent over the same period. It further demonstrates that the agreement would divert trade away from the United States in the amount of \$2.7 billion in GDP by 2030.

Economic gains would be measured not just in new export sales opportunities but also in lower-priced imports for consumers and as inputs for manufacturing. The combined effect results in an estimated increase of \$5.7 billion to Canadian household income by 2030. The economic activity will result in greater Foreign Direct Investment in Canada: the increase in the foreign-owned capital stock in Canada would amount to 0.11 percent or \$982 million in 2030.

By 2030, Canada's overall exports to China were projected to grow by \$7.7 billion annually and total shipments by \$10.4 billion. For example automotive exports to China would increase by more than \$1.4 billion annually, chemicals/rubber/plastics by some \$688 million, machinery and equipment by \$584 million, and approximately \$1.7 billion more per year in exports of oil seeds and vegetable oil.²²

Employment was also projected to increase as a result of increased demand and the additional economic activity stimulated by the agreement. This could amount to about 25,000 additional jobs in Canada across all skill levels.

In January 2016 China's Vice-Minister of Financial and Economic Affairs, Han Jun, visited Ottawa to discuss the prospect of negotiating its first free-trade deal with any North American country. He said if there is an FTA arrangement between China and Canada, "you can see a flooding of potash, agricultural products and energy products from Canada to the market of China. What is China most in need of? We have a shortage of agricultural products. China is the biggest importer of agricultural products in the world and, also, we are one of the countries with the highest dependency on imported energy from other countries."²³

¹⁸*Globe and Mail*, January 23, 2016. Harder was subsequently appointed to the Senate and is now the government leader in the upper chamber.

¹⁹Josh Wingrove, Trudeau to Woo More Chinese Investment, *Globe and Mail*, March 21, 2016.

²⁰ See Laura Dawson and Dan Ciuriak, *Chasing China*. <http://dawsonstrat.com/files/2016/01/Chasing-China-Web-Ready.pdf>. Also Dan Ciuriak, Ali Dadkhah and Jingliang Xiao, *Quantifying a Canada-China Free Trade Agreement*, Ciuriak Consulting Inc.; C.D. Howe Institute; BKP Development Research & Consulting, January 19, 2016. http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2720074.

²¹ Dawson and Ciuriak. Table A.

²² Dawson and Ciuriak Table B

²³ Robert Fife, China open to historic free-trade deal with Canada under certain provisos, *Globe and Mail*, January 14, 2016.

He noted that China will come to the table with its own demands, namely the removal of restrictions put in place by the former Conservative government on Chinese state-owned investments in Canada's oil and gas sector.

A public opinion poll commissioned by Vancouver-based Teck Corp. which has 22% of its revenue generated in China seemed to suggest that Canadians are open to the idea of enhanced relations.²⁴ It identified three different segments in Canadian public opinion regarding China. Just over a third of Canadians (36%) are supportive, just over a quarter (28%) are generally opposed to a closer relationship and the rest could best be described as conditionally supportive.

When it comes to the idea of a free trade deal with China, "the results suggest a degree of openness that might not have been there a decade ago. Canadians will naturally have concerns about being competitive enough with Chinese companies, but also recognize the potential economic upside is significant too."²⁵

The new government of Justin Trudeau promised to take a different approach to foreign policy. In the first six months the Liberals announced a policy of re-engagement with the United Nations and specifically its intention to seek a non-permanent seat on the security council by 2021, something that had been denied the Conservatives.

Mr. Trudeau also withdrew from the bombing mission in Syrian by recalling Canada's six jet fighters and promising instead to increase training and humanitarian aid. Canada immediately took in 25,000 Syrian refugees with a promise to consider more by the end of 2016. The Liberals promised to re-engage with Russia and re-establish diplomatic relations with Iran. China was largely absent from these early policy statements although in April 2016 a meeting of the full cabinet invited consultant Dominic Barton, author of *China Vignettes: An Inside Look at China* to speak about China's impact on global economic growth and how that will affect Canada.²⁶

To direct Canada's new foreign policy Trudeau appointed a former leader of the Liberal Party, Stephane Dion, as Minister of a newly renamed Department of Global Affairs. A political scientist by training and a well-respected intellectual Mr. Dion reached into academia to name several advisors including one expert in China policy.²⁷ In a speech on new foreign policy directions to a Canadian think tank Mr. Dion said Canada's policy would be centred on diplomatic re-engagement.²⁸

In another foreign policy address at the University of Ottawa on March 28, 2016 Mr. Dion described the new direction as "responsible conviction" a vague term that puzzled many analysts. Some felt it was an attempt to assure Canadians that the new government was going to continue to follow a "principled" foreign policy as the Conservatives had claimed they were doing.

²⁴ Abacus Data, *Canada China Relationship*, January 20, 2016. <http://abacusdata.ca/the-canada-china-relationship/#sthash.rSX7J9jd.dpuf>.

²⁵ *Ibid.* Other polls paint a somewhat more negative picture of Canada-China relations. The US based Pew Research Centre has revealed that Canadian favourability of China has dropped from 58% in 2005 to as low as 39% in 2015."

²⁵ In 2010 the Asia Pacific Foundation of Canada national opinion polls of Canadian views on Asia found that only 18% of Canadians supported Chinese foreign direct investment in China.

²⁶ See <http://www.cbc.ca/news/politics/deliverology-liberal-cabinet-retreat-1.3553024>

²⁷ *Hill Times*, April 29, 2016.

²⁸ Eva Salina, Catherine Tsalikis, How to Build a New Foreign Policy for Canada, February 5, 2016 <https://www.opencanada.org/features/how-build-new-foreign-policy-canada/>

However unlike the previous government it would be less ideological and recognize that choices in international relations were not black and white but many shades of grey.

The new policy was criticized as basically a continuation of the status quo.²⁹ There was nothing in either speech about relations with China but many indications that even closer relations with the United States would continue to be the first pillar of Canadian policy.³⁰

As the new Canadian government ponders its relations with China it is instructive to examine the recently concluded China Australia Free Trade Agreement.

The Australian Experience

In June 2015, following nearly ten years of negotiations, Australia and China completed what some have called the most comprehensive free trade agreement that China has ever signed and one that contains “best-ever” Chinese commitments in a number of sectors. Since Canada and Australia have similar economies and similar histories of trade with China what are the lessons for Canada from the ChAFTA?³¹

In Agriculture ChAFTA will eliminate 95 percent of all tariffs when it is fully implemented after eleven years. Tariffs on Australian wine, meat and seafood, currently between 10 and 25 percent, will be eliminated within four years. Tariffs on barley were eliminated on entry into force whereas Canadian barley continues to face a 3 percent tariff.

Market access for Australian beef is quota-limited: 170,000 tonnes for the first 4 years, gradually increasing to a little over 200,000 tonnes after 10 years. There are no restrictions on market access for pork or seafood. Australia will also benefit from an exclusive duty-free quota on wool.

Certain agricultural sectors such as canola oil and vegetable oils are excluded from ChAFTA because they are designated “significantly sensitive staples” by China. Rice and sugar are also excluded.

When it comes to natural resources, 99 percent of Australia’s resources, energy and manufacturing exports will enter China duty-free upon full implementation. The tariff of 3 percent on coking coal was removed on entry into force and 6 percent on thermal coal will be eliminated after two years. Tariffs up to 10 percent will be eliminated for refined copper and alloys, aluminum oxide, zinc, aluminum, nickel and titanium dioxide, many on entry into force. Tariffs of up to 10 percent on pharmaceuticals, including vitamins and health products, will be eliminated either immediately or within four years.

In the area of services China has gone beyond its GATS commitments in a number of areas but many fall short of full liberalization. For example, China has agreed to allow wholly owned Australian hospitals, but only in four provinces and three cities. However, Australian service suppliers will be able to establish for-profit aged care institutions throughout China. In tourism,

²⁹ See for example Campbell Clark, Liberal’s new foreign policy end up in familiar territory, *Globe and Mail*, March 30, 2016.

³⁰ Mike Blanchfield, Dion digs at Tories with new foreign policy label: responsible conviction, *Canadian Press*, March 29, 2016., <http://www.nationalnewswatch.com/2016/03/29/dion-digs-at-tories-with-new-foreign-policy-label-responsible-conviction-2/#.VvvUbvkrLNN>

³¹ This section is drawn largely from Laura Dawson and Dan Ciuriak, *Chasing China: Why an economic agreement with China is necessary for Canada’s continued prosperity*, Dawson Strategic and Ciuriak Consulting, January 2016.

Australian services suppliers will be able to construct, renovate and operate wholly Australian-owned hotels and restaurants in China.

Labour mobility also makes significant strides in ChAFTA. New Investment Facilitation Arrangements (IFAs) will operate under the framework of the Australian visa system. These will allow certain Chinese-owned companies that invest in Australian infrastructure projects above AU\$150 million to negotiate labour market access flexibilities.

In architecture and urban planning, Australian firms will be allowed to obtain more expansive business licenses to undertake higher-value projects in China.

Both sides have committed to expand their education services relationship. Australia and China signed an MOU aimed at improving recognition of qualifications and promoting exchange opportunities. Although the Australian government is making much of the commitments in ChAFTA on education, the only firm Chinese commitment is the listing of 77 Australian providers on the Chinese Ministry of Education website. According to Australian government sources, 88 percent of Chinese students studying in Australia in 2013 chose to study at institutions listed on the website. China has agreed to ongoing discussions about adding new Australian schools to the site.

One of ChAFTA's unusual elements is the services chapter in which Australia uses a NAFTA-style negative-list approach while China uses a GATS-style positive list. Negative list approaches identify only what is excluded from the agreement while a positive list itemizes everything that is included. Positive-list agreements tend to include fewer trading areas and do not deepen trade as much as negative-list agreements. So, in the services deal struck between China and Australia, the latter provided more inclusive liberalization. Nevertheless, despite retaining the positive list, China opened up more services sectors to Australia than it has in the past.³²

In financial services China has committed to deliver improved access to Australian financial service providers in the banking, insurance, funds management, securities, securitization and futures sectors. ChAFTA also designates an official RMB clearing bank in Sydney allowing trading of Chinese currency in Australia. The allocation of an RMB 50 billion quota will allow Australian-domiciled fund managers to purchase equities and bonds directly from China's mainland securities exchanges in Shanghai and Shenzhen.³³

Australian banks will enjoy much greater access to the Chinese market. China has agreed to reduce the waiting period for Australian banks to engage in RMB-denominated business from three years to one year. China will remove the two-year profit-making requirement as a precondition to providing local currency services. Australian bank subsidiaries in China are the only foreign bank subsidiaries to enjoy an FTA commitment guaranteeing their eligibility to engage in the credit asset securitization business.

China will allow Australian insurance providers access to China's statutory third-party liability motor vehicle insurance market, without local establishment or equity restrictions.

³² *Ibid.* p. 14

³³ These commitments are nearly identical to what Canada negotiated through the RMB hub established in Toronto in 2015.

For the first time in an FTA, China has agreed to allow Australian financial service providers to establish joint venture futures companies with up to 49 percent Australian ownership and extend national treatment to Australian financial institutions for approved securitization business in China. Australian securities firms in China will benefit from new commitments, raising foreign equity limits to 49 percent (above China's WTO commitment of 33 percent) for participation in underwriting domestic shares and guaranteeing the ability to conduct domestic securities funds management business.³⁴

In legal services ChAFTA provides China's first-ever treaty commitments on commercial association between law firms. In addition to guaranteeing existing access for Australian law firms in China, it also guarantees Australian law firms have the ability to establish commercial associations with Chinese law firms in the Shanghai Free Trade Zone (SFTZ). These commercial associations will be able to offer Australian, Chinese and international legal services, without restrictions on where clients are located.³⁵

With regard to foreign investment Australia made significant FDI concessions, raising the screening thresholds for private Chinese investments in non-sensitive sectors to AU\$1,094 million from AU\$252 million. This is on par with thresholds for Chinese private investment in Japan, South Korea, New Zealand, and the United States. However, all investments must originate from China to qualify for the higher threshold, and not come from offshore accounts. Foreign investment in residential real estate is excluded from ChAFTA.

ChAFTA does not eliminate mechanisms already put in place by the Government of Australia to review investment by Chinese State Owned Enterprises. However Australia has liberalized the screening threshold at which private Chinese investments in non-sensitive sectors are considered by the Foreign Investment Review Board (FIRB). Australia retains the right to screen Chinese investments at lower thresholds for agricultural land, agribusiness, and sensitive sectors. Furthermore, all investment by Chinese SOEs will be subject to review, regardless of transaction size. The Foreign Investment review Board will consider factors such as whether investors operate at arm's length and on a commercial basis when it applies the national interest test. In Australia, there is no real definition of what is necessary to pass the national interest test, and the FIRB does not need to disclose how it arrives at a particular conclusion.³⁶

While Australia's agreement with China created a great deal of new market access, Australian negotiators were unable to generate Chinese concessions in sugar, rice, cotton, wheat, maize, or canola. Australia obtained a market access quota for its important wool industry but it was not able to negotiate reduced tariffs for wool. Milk powder and beef are also subject to quota limits under special safeguards.

The investor-state dispute settlement with the right of Chinese firms to sue Australian governments for policy changes that adversely affect their interests was also a controversial provision. Another provision that could attract public criticism is the right of Chinese investors

³⁴ Department of Foreign Affairs and Trade Australia, Fact Sheet: Trade in Services, *China Australia Free Trade Agreement*, August 26, 2015. <http://dfat.gov.au/trade/agreements/chafta/fact-sheets/Pages/fact-sheet-trade-in-services.aspx>

³⁵ *Ibid.*

³⁶ Andrew Lumsden et al, *The National Interest Test and Australian Foreign Investment laws*, July 15, 2015. <http://www.clmr.unsw.edu.au/article/market-conduct-regulation/state-capital/the-%E2%80%9Cnational-interest-test%E2%80%9D-and-australian-foreign-investment-laws>.

who invest over AU\$150 million to bring in temporary migrant workers to Australia without local labour market testing. Australia retains the right to screen Chinese investment but the threshold has quadrupled to just over AU\$1 billion. Chinese investment is excluded from sectors deemed sensitive by Australia such as agriculture, media, telecoms and defence.³⁷

Despite some problems and risks in being an early adopter Australia stands to benefit by an estimated AU \$18 billion over the next decade. In a recent interview a former Australian Prime Minister and expert on China was asked if he had any advice for Canada. He said: “My only advice to anyone negotiating a free-trade agreement with our Chinese friends is China has produced some of the toughest negotiators in the world on trade, so be tough.”³⁸

Obstacles

Despite the Australian agreement and the change in government in Canada the prospects for a Canada-China free trade agreement have not really changed. One obstacle is a general skepticism with free trade agreements related to the debate that has emerged in the United States presidential election campaign. Many blame free trade agreements for the loss of jobs and the unequal distribution of wealth. Canadian media follow US elections almost as closely as Americans and this trashing of free trade may have cooled some enthusiasm across the border.

It also appears that Mr. Trudeau, unlike his father, is not prepared to be significantly out of step with the Americans. With China playing an important part in the United States election the younger Mr. Trudeau seems less likely to make decisions in this area until he sees the nature of the new American administration in November.

The Liberal government has been reluctant to fully embrace the Trans Pacific Trade Agreement negotiated by the previous government. Ratification is proceeding slowly and once again it is likely that no final decision will be taken until the United States ratifies or rejects the TPC.³⁹

Even the Canada-EU Free Trade agreement which the new government has embraced, is causing problems. Several EU members have problems with provisions relating to “investor-state dispute settlement” provisions. Basically they allow foreign investors to sue governments in special arbitration courts for damages the host government’s policies may cause to investors interests. There is no cap on the potential compensation and no judicial review of the decisions. Critics of this provision claim it is not only an unacceptable loss of sovereignty but enables foreign investors to subvert environmental and social policies.

The Investment Treaty with China, negotiated by the Harper government, contains these provisions and has been loudly criticized by some. “China retains the right of investment screening in line with all its existing laws. So if a mayor of some Chinese city invokes a municipal law to keep out a Canadian company arbitration is not an option. By contrast aggrieved Chinese companies can haul Ottawa before a panel of three international lawyers over actions by politicians, regulators, the courts or any other body at any level.”⁴⁰

³⁷ Dawson and Ciuriak, *op. cit.* p. 16.

³⁸ Interview with Global News, April 3, 2016, <http://globalnews.ca/news/2615350/excitement-from-international-community-with-a-more-activist-canada-rudd/>

³⁹ Much criticism of the TPP in Canada revolves around provisions about intellectual property. See testimony by James Basillie to Senate Foreign Affairs Committee, March 24, 2016.

⁴⁰ Gus Van Harten, Chinese checkmate, *Report on Business*, April 2016, p. 10. For a full discussion of this point see Gus Van Harten, *Sold Down the Yangtze: Canada’s Lopsided Investment Deal With China*, Lorimer, Toronto, 2015.

A second obstacle is the view among some of the public policy community that China lacks certain qualities required of a free trade partner. It is sometimes compared unfavourably to other Asian states including Japan.

Japan is more technologically advanced than China and its large multinationals are highly profitable juggernauts whose products are prized around the world for quality and sophistication. Tokyo is, along with New York and London, one of the world's three principal financial hubs, where global capital is managed with unparalleled skill and speed. Japan is a successful democratic society under the rule of law, with a deep commitment to a stable world order. Japan is a staunch member of the Western alliance... Our third foreign embassy opened in Tokyo in 1929, and some of our biggest companies have been doing business there for decades. The Japanese have been investing in Canadian industries as diverse as forestry, autos, video gaming, food processing and oil sands production.⁴¹

A third obstacle outlined by a former Canadian Ambassador is that Canadians seem unwilling to see China as it is rather than as what they would like it to be. "This reflects our nostalgia for a vanishing world in which our main international concerns – security, prosperity and our considerable stake in a healthy global commons – have largely been worked out through our relationship with the United States."⁴²

A fourth obstacle is that Canada has underestimated or ignored structures and mechanisms that could help to manage the relationship. "It should not surprise us that China, a state that still sees value in central planning and control, should prefer to manage its bilateralships along similarly bureaucratic and state centric lines. China's penchant for classifying and ordering its most important partnerships is also a means of signaling to its vast bureaucracy what is and isn't possible with particular partners."⁴³

Australia has been more successful in formalizing a strategic partnership with China. "We need to institutionalize our bilateral relations through broader and deeper direct government to government exchanges that will build trust by having officials work together side by side toward common goals and at the same time partner more effectively with China's efforts to supply more global public goods. Paralleling these efforts we need to put in place mechanisms that will defuse tensions that periodically build up due to differences in our institutions and value systems."⁴⁴

Relations are hampered by the absence of high level bilateral mechanism similar to the US-China Strategic and Economic dialogue and the Singapore-China management committee.⁴⁵ "The narrative for deeper engagement should be rewritten. It should prepare for a much larger Chinese presence in Canada and on the global stage; it should help address public ambivalence

⁴¹ Brian Lee Crowley, Japan, not China is key to Canada's Asia Pacific aspirations, *Ottawa Citizen*, March 27, 2015. <http://ottawacitizen.com/news/politics/crowley-japan-not-china-is-key-to-canadas-asia-pacific-aspirations>

⁴² David Mulroney, After 45 Years it is Time to Grow Up, in Asif B. Farooq and Scott Mcknight, *Moving Forward: Issues in Canada China Relations*, *op cit.* p. 114

⁴³ *Ibid.*

⁴⁴ Jeremy Paltiel, Restoring Strategy to the Strategic Partnership: Canada and China Reimagined, in Asif B. Farooq and Scott Mcknight, *Moving Forward: Issues in Canada China Relations*, *op cit.* p. 13

⁴⁵ Wendy Dobson and Paul Evans, The Future of Canada's Relationship with China, in *IRPP Policy Horizons Essay*, Institute for Research on Public Policy, Montreal, November 2015.

and the expanding list of irritants, frictions and anxieties. It should also recognize the opportunities and shared interests in providing global public goods in areas including climate change and clean technology, stabilization of international financial system and disease control.”⁴⁶

Similarly in the area of military to military exchanges Canada should increase co-operation in areas like peace keeping, search and rescue, disaster relief and humanitarian assistance. “We should aim to build a cohort of officers who are on a first-name basis with Chinese counterparts. As part of a broad based effort to refocus our attention on the Asia Pacific, funding for military exchanges and joint exercise must be budgeted on a priority basis.”⁴⁷

A sixth obstacle, particularly during the Harper years was that Canada “has been obsessed with a distinction between pursuing commercial and diplomatic opportunities versus promoting human rights”⁴⁸ As a result Canada adopted a “cool politics, warm economics” policy toward the PRC. It remains to be seen if the Trudeau government understands that a good relationship is based on more than economics.

A seventh obstacle relates to public opinion. All democratic governments worry about their standing in the court of public opinion but the Trudeau government seems particularly concerned about this. While some public opinion polls commissioned by industries doing business with China seem to show some movement in Canadian opinion toward China. Other polls indicate this is still a problem.

One study by a professor, now a special adviser to the Minister of Global Affairs, shows that while most Canadians believe China will be more powerful than the United States, only about a third see China as highly important to their economy or support a free trade deal.⁴⁹ Only 14% support the prospect of a Chinese state owned enterprise owning a controlling stake in a major Canadian company. A majority believe that human rights situation in China is deteriorating, that it does not respect the freedoms of its people and that its growing military power is a threat. More than half believe that China’s influence is threatening the Canadian way of life.⁵⁰

In light of these obstacles, some of his own making, Mr. Trudeau has taken a cautious approach toward China. He has given priority to improving Canadian relations with the United States which also deteriorated under Mr. Harper. In his first six months Mr. Trudeau visited the US four times including a state dinner at the White House and two trips to the United Nation.

Nor were these quick day trips which can easily be done from Ottawa. He spent 13 days in the United States on these trips for the purpose of talking to the media, to universities, to interest groups, even taking the time to pursue his favourite hobby, boxing, in a famous American gym.⁵¹ He understands how to parlay celebrity into raising Canada’s profile and improving the bilateral relationship.

⁴⁶ Wendy Dobson and Paul Evans, *Living with Global China: Agenda 2016* in Asif B. Farooq and Scott Mcknight, *Moving Forward: Issues in Canada China Relations*, *op cit.* p.10

⁴⁷ *Ibid.* p. 19

⁴⁸ Paul Evans, *Dancing with the Dragon*, *Canadian Literary Review*, April 2013.

⁴⁹ Pascale Massot, *The Political Economy of Canadian Public Opinon on China*, in Asif B. Farooq and Scott Mcknight, *Moving Forward: Issues in Canada China Relations*, *op cit.* pp.25-35

⁵⁰ *Ibid.*

⁵¹ <http://www.cbc.ca/news/politics/trudeau-united-states-visits-1.3552373>

Mr. Trudeau could take a similar approach to China. This might involve one or more visits beyond the short stays associated with a summit or G20 meetings. A few well chosen events and speeches or perhaps even a family vacation could turn Canadian opinion toward China fairly quickly.

Timing is significant because with the Trans Pacific Partnership in limbo there is incentive for Canada to seek an alternative plan such as an economic agreement with China. And for China the possibility that the TPP might be ratified gives it a reason to look more favourably on an arrangement with Canada as a counterbalance. Once the US election is over and positions are settled there might be less pressure on both sides to negotiate a free trade agreement.

Conclusion: Canada and the China Question

In recent times China has articulated a new vision of the global order based on the notion of a “community of common destiny” The “One Belt One Road” idea is designed to unite the planet through infrastructure and trade. Its goal is to lift millions around the world out of poverty just as it has done within China.

This is a grand vision and not one that will be accomplished in a single or even multiple 5 year plans. But as an idea and a vision it deserves to be mentioned in the same breath as the American post war Marshall Plan or Victor Hugo’s idea for an united Europe.

A Chinese vision for the world would be a more pluricentric one with several regional powers. It would be unlike the cold war world with two competing ideologies striving to impose themselves on the rest of the world. It would also be unlike the present single uni-power world where the United States deploys its military forces to try and shape events to its interests. A multi-polar world characterized by more tolerance for different kinds of governance structure and less talk about universal values would likely be a more peaceful and prosperous world.

Canada needs to insert itself into this vision just as we inserted ourselves into and embraced the concept of British Empire and later the American post war vision of rules-based internationalism. The challenge is for Canadians to recognize and assist in the transition from a world order “premised on American primacy that can no longer be maintained to an order that has not yet taken shape.”⁵²

The challenge for the Canadian government is to make the case that “engaging a country is not the same as agreeing with it. But “there is no downside to partnering with China in areas of common concern and using our influence on China’s direction. Partnering with China is a daunting challenge given our ideological differences, institutional incompatibilities and distinctive value orientations. However co-operation is possible without compromising our core liberal and democratic values – and indeed necessary if Canada is to maintain a significant role in global governance.”⁵³

A small but optimistic sign that Canada might be moving in the right direction occurred in April 2016 when a group of Chinese engineers met in Ottawa with some parliamentarians to discuss a project to build a 340 mile rail link to some potentially rich resource areas in a sparsely

⁵² Paul Evans and Wendy Dobson, *Living with Global China*, *op. cit.* p. 9.

⁵³ Jeremy Paltiel, *Restoring Strategy to the Strategic Partnership*, *op. cit.* p.14.

populated area of northern Ontario.⁵⁴ The idea to build the line has been stalled for years because of a lack of capital and short term thinking about the price of commodities.

The engineers are expected to complete a detailed feasibility study on the rail project within four months that would then be presented to Chinese financial institutions.⁵⁵ This will be a good test of whether Canada is prepared to move beyond words and toward real projects with real impacts on Canadian society and bilateral relations.

An even better signal would be for Canada to endorse the recent Chinese idea of building a rail link from China through Russia, across the Bering Strait to Alaska and then through Canada to the continental United States.⁵⁶

The political difficulties of such a project dwarf the technological challenges. But the dream has been nurtured for years by Russian, American and other visionaries. Canada should not only lend its support to such a project but play a leading role in bringing the parties together and pushing the idea forward. That would be a kind of signal that Canada is willing to insert itself into the Chinese vision of the world. This type of big thinking, led by China and with Canada as an active supporter, could transform the world economy and international relations in ways we can barely imagine.

⁵⁴ Bill Curry, Chinese show renewed interest in Ring of Fire, *Globe and Mail* April 19, 2016.

⁵⁵ Bill Curry, Chinese engineers endorse \$2 billion Ring of Fire rail line, *Globe and Mail*, April 20, 2016.

⁵⁶ See China Daily, May 8, 2014, http://www.chinadaily.com.cn/business/2014-05/08/content_17493399.htm
Also *Washington Post*, May 9, 2016.