Overview of the Research Findings

Stephen Tapp, Ari Van Assche and Robert Wolfe

As a small open economy, Canada's prosperity and growth depend critically on international trade and investment — economic activities where new global realities are challenging long-held policy goals and approaches. International collaboration and cooperation are needed to improve consumption and production possibilities and spur innovation, but troubling signs are emerging that such cooperation may be at risk, as protectionist sentiments are rising around the world. With Donald Trump's election as president of the United States, Canada's largest trading partner is fundamentally reassessing its trade policies and seeking to reset global trade relationships on more favourable terms for American businesses and workers. With such high stakes in this complex and rapidly evolving context, it is now more important than ever to comprehensively examine new global trade realities and consider appropriate policy responses.

In this volume, the culmination of a multiyear IRPP research initiative, 31 leading researchers and practitioners from Canada and abroad analyze how longer-term structural changes and emerging trends in global commerce, technology and economic and geopolitical power are affecting Canada, and what these changes mean for policy. We examine interconnected issues such as the new business models that have emerged as production becomes more fragmented and global; the rise of trade in intermediate inputs and services as well as foreign direct investment; technological transformations that are altering who trades what and how; and the shift in global economic activity toward emerging markets, which has dispersed power and raised new challenges for the Canadian economy, as well as for global trade negotiations and governance.

We have three main objectives for this volume. First, to contribute new empirical evidence for Canada. Second, to develop a guiding analytical framework to explore the policy implications of the findings. And third, to propose a carefully considered, forward-looking suite of trade-related policy priorities that will promote the growth and productivity of the Canadian economy. In this overview chapter we summarize our contributors' findings, mostly written over the course of 2015 a nd 2016.[1] The appendix is a summary of the authors' policy recommendations. In the concluding chapter, we consider the results of this research in the political context of early 2017, summarizing our policy implications and recommendations in light of recent developments.

The volume is structured in five parts. The first two parts, on firm-level trade and global value chains, develop the overarching analytical perspectives. They describe new patterns in Canada's integration into the global economy and interpret these developments through the lens of recent advances in the academic literature. The third part examines how these new global realities are affecting the design of Canadian commerce policies. The chapters in the first three parts are full-length research papers, written by North American and European academics from the fields of economics, international business, public policy and law, and by researchers in governmental organizations and think tanks. The chapters in the fourth part are generally shorter commentaries that present perspectives from several prominent trade practitioners and stakeholders. The volume concludes in part five with the editors' summary of this research initiative and its key policy priorities.

Firm-Level Views of Canadian Trade

The authors in part one of the volume examine Canadian trade policy using a firm-based approach. Whereas trade theory in the 1980s and 1990s typically focused on industries — implicitly assuming that firms in the same industry are similar to one another — twenty-first-century trade theory focuses on firms. This new perspective has revealed vast differences, or heterogeneity, among firms in the same industry in a variety of important activities (such as exporting and innovation) and performance measures (such as productivity). These differences affect a firm's likelihood of succeeding in domestic and global markets; they also help explain why different types of firms respond differently to changes in the trade environment and trade policy, and thereby provide a better understanding of the distributional effect of trade on firms and workers. These chapters emphasize the strong links between trade and productivity, the importance of distributional considerations and the benefits of policies that reduce the fixed costs of participating in global markets.

International Trade with Firm Heterogeneity: Theoretical Developments and Policy Implications

Beverly Lapham

Leading off this part, Beverly Lapham reviews the recent developments in theoretical trade models and explores their policy implications. She focuses on a seminal model developed by Marc Melitz that emphasizes firm-level differences and decisions. This important model highlights the fixed costs of entering foreign markets and the upfront and uncertain nature of this investment. It predicts that exporters will tend to be larger and more productive than non-exporters — predictions that have been confirmed for Canada and many other countries. An important idea in the basic model is that only the most productive firms are profitable enough to cover the high costs of entering foreign markets. As a result, only "better" firms become exporters (in other words, there is so-called positive self-selection into exporting), though it is now increasingly clear that the act of trading can also raise firm-level productivity.

The Melitz model not only allows us to understand which firms trade and why, it also identifies a new channel through which trade policy can enhance a country's productivity — by shifting the economy's resources from lower-productivity firms to higher-productivity ones. When access to foreign markets improves, more productive firms that previously served only the domestic market enter those foreign markets and expand their production, as do existing exporters. Less productive firms exit because of increased foreign competition and higher domestic wages. Detailed estimates of the impact of the Canada-US Free Trade Agreement attribute over 60 percent of the productivity gains in Canada's manufacturing sector, after tariff cuts, to this type of industrial restructuring, as opposed to growth that occurred within firms.

Lapham also reviews recent extensions to the model. These include work that models how complementarities between exporting and importing can raise a firm's productivity; the use of foreign direct investment, rather than exports, to serve foreign markets; the links between trade and innovation; the impact of trade on the labour market and the potential for increased wage inequality; and how trade can reduce the markup of selling prices relative to production costs.

The results of this literature suggest that policy-makers should pay more attention to the effect of trade policies on existing and potential traders, trade flows and the distributional effects of trade on firms and workers. They also emphasize the importance of policies that lower the fixed costs of participating in international markets, and they highlight the need for greater coordination of traditional trade policies (such as tariffs and trade negotiations) and nontraditional policies that are closely related to trade (such as boosting productivity and innovation).

Trade and Productivity: Insights from Canadian Firm-Level Data / Global Value Chain Participation and the Productivity of Canadian Manufacturing Firms

John Baldwin and Beiling Yan

In these two chapters John Baldwin and Beiling Yan demonstrate the value of using Canadian firm-level data to empirically investigate the close relationship between trade and productivity, which Lapham's chapter on trade theory features so prominently. In "Trade and Productivity," they begin by presenting suggestive evidence at the aggregate level that Canada's trade as a share of gross domestic product (GDP) and its business sector productivity have tracked each other quite closely in recent decades. Their analysis then uses firm-level data to reveal the underlying micro drivers of this macro relationship. In line with the theory, they find that export participation and export intensity increase with firm size; that Canadian exporters make an outsized contribution to economic activity (for instance, between 1974 and 2010, average labour productivity was 13 percent higher for exporters than for non-exporters in the manufacturing sector); and that imports are an important source of productivity gains because they can provide access to cheaper and higher-quality inputs (between 2000 and 2007, a remarkable two-thirds of Canada's effective multifactor productivity came from other countries).

Baldwin and Yan stress that the benefits from accessing new markets are not automatic: firm-specific factors matter and the size of these benefits may be attenuated by macroeconomic factors such as exchange rate movements that affect exporters' competiveness. Businesses that succeed abroad tend to be adaptable and innovative, introducing new products and processes. Investment is also a key part of the story and helps to explain why the largest productivity gains are often found for new entrants into export markets, which typically grow faster than more experienced exporters. When firms enter new markets, they often accumulate capital and invest in advanced technologies, research and development, and training. These activities develop their capacity to learn from and adopt international best practices. Larger markets — whether international or interprovincial — can also raise productivity by allowing firms to specialize production, exploit economies of scale and increase their capacity use.

In "Global Value Chain Participation," Baldwin and Yan analyze how a firm's participation in global value chains (GVCs, which are explored in more detail in part 2 of the volume) affects its productivity. They use a rich dataset of over 30,000 Canadian manufacturing firms over the period 2002-06. The authors define a GVC participant as a firm that imports intermediate goods and exports intermediate or final goods, and they investigate what happens over time to the productivity of firms that enter and exit GVCs.

Their results present strong empirical evidence of a causal link between GVCs and firm-level productivity. They find that Canadian manufacturing firms that joined GVCs became more productive than firms with similar characteristics that did not. This productivity advantage was evident within the first year and grew over time. The largest gains were made by firms that initially exported to other advanced economies. In contrast, firms that dropped out of GVCs — by no longer importing, no longer exporting or both — became less productive than firms that continued to belong to GVCs. This loss took longer to materialize, but after the first year the productivity disadvantage was similar in size to the gains enjoyed by GVC starters. The largest and most immediate losses for GVC quitters were incurred by firms that stopped importing from developing economies. Both the positive productivity effects of joining GVCs and the negative effects of quitting them were statistically significant and economically relevant, cumulating in firm-level productivity performance gaps of 8 to 9 percent on average after four years.

The authors also carefully document the pathways by which Canadian firms enter and exit GVCs, and they disentangle the relative productivity contributions of exporting and importing for two-way traders. They find that firms that enter GVCs are primarily importers that start exporting, while those that leave GVCs are largely two-way traders that stop exporting. Moreover, the productivity benefits from exporting are larger and longer-lasting than the positive effect of importing.

Baldwin and Yan's analysis suggests that policies that facilitate GVC participation should be at the heart of Canada's trade and productivity agenda (something that is echoed in other chapters, such as those written by Lapham and by Van Assche). It also has implications for the objective of increasing the share of Canada's exports to emerging markets: productivity gains from joining value chains involving emerging markets might be smaller than those from joining value chains involving advanced economies, and there may be a more immediate productivity loss incurred if these trading relationships eventually sever.

Going Global: Canadian SME Trade and Emerging Markets

Sui Sui and Stephen Tapp

Previous firm-level studies find that small and medium-sized enterprises (SMEs) generally are less successful exporters than large firms. In Canada, the policy response to this has been to encourage SMEs' participation in international trade, particularly in faster-growing emerging markets that would also help to diversify Canada's trade. This detailed analysis of Canadian SMEs' exporting activities finds evidence of SMEs' increased market diversification — as the share of Canada's total exports to emerging markets rose from 4 percent in 2001 to 10 percent in 2014 — and notes that these markets increasingly are the first stops in the export journeys of Canadian firms. Sui Sui and Stephen Tapp also identify several ways that SME trade differs from that of large firms: SMEs are less likely to export, they reach fewer markets (often only the United States) and their average export revenues are much lower (partly because their activities are more concentrated in industries with lower export revenues). The silver lining is that SME trade is naturally more "inclusive," because the export revenues are spread more broadly across many more firms.

The authors report, in line with findings in other chapters, performance premiums for Canadian SMEs that export, relative to non-exporters. They also show that SMEs that export to emerging markets perform slightly better, on average, than those that export to other destinations.[2] In seeking the larger rewards in these faster-growing emerging markets, however, firms can incur higher risks. Firm-level performance gaps between top and bottom Canadian exporters are particularly pronounced in these markets. In general, the chances of surviving in emerging markets are better for firms that are more experienced in the domestic market and/or that exported first to other advanced economies, so-called gradual exporters. But this is not the only recipe for success. A smaller number of firms operating out of Canada successfully reached emerging markets early in their operations (they are known as "born global" firms), particularly markets for higher-technology services.

Sui and Tapp highlight key roles for the federal government, as a "trouble-shooter" to help address problems existing exporters face and as an "information provider" to survey market conditions and help potential exporters make well-informed decisions based on their particular circumstances. They say government information should be tailored to the needs of younger and smaller firms — including first-time traders — that generally need more external assistance and may be more receptive to implementing the changes needed to succeed in emerging markets. Given the surprisingly low take-up (about 5 percent) of government support by Canadian exporters, policy-makers should continue efforts to raise awareness of existing programs and design them to better meet the needs of SMEs. As well, they say, government should try to lower the costs Canadian firms face to engage with international markets (particularly emerging markets), costs that disproportionately restrain SME trade. This can be accomplished by implementing trade and investment agreements, simplifying customs procedures and promoting cross-border electronic commerce.

The authors note that SMEs might be able to employ strategies other than exporting directly to emerging markets that could provide benefits at lower risk. As an example, high-potential SMEs can start by building up their resources and capabilities in less challenging foreign markets first, or by selling intermediate goods or services to larger North America-based multinationals that are active in emerging markets.

Technology-Enabled Small Business Trade in Canada: New Evidence from eBay Marketplaces

Usman Ahmed and Hanne Melin

Like Sui and Tapp, Usman Ahmed and Hanne Melin consider how to scale up Canada's international trade by small firms. However, their focus is not necessarily on emerging markets but on how new technologies can facilitate the process. Traditional trade is dominated by large multinational companies that make high-value, regular shipments of a standard range of products that they export using commercial trucks, ships and cargo containers along well-established trade corridors. Ahmed and Melin highlight a new type of technology-enabled trade that is developing thanks to better information flows, enhanced connectivity and growing trust in online transactions. In contrast to traditional trade, technology-enabled trade features more small businesses and newcomers that ship lower-value, niche or customized products, often using the postal system, on an irregular basis, to idiosyncratic locations. Frequently consumers find the firms, rather than the firms finding the consumers.

Analyzing a unique dataset of Canadian firms from eBay Marketplaces from 2008 to 2013, Ahmed and Melin describe the ways technology-enabled international trade differs from traditional "offline" trade, and they identify impediments to online cross-border trade and policies to address them. They find that technology-enabled firms are much more likely to export and reach more countries than their offline counterparts (an annual average of 19 markets reached on eBay by online traders compared with fewer than 3 reached by offline traders). They also show that trade patterns in technology-enabled markets are more inclusive, with more new entrants (particularly smaller firms), and that the sales are less concentrated among the top firms.

They note, however, that technology-enabled small businesses face unique challenges, which need to be acknowledged in trade policy discussions if the full potential of these new trends is to be realized. One way government can do this is to significantly raise Canada's low-value (*de minimis*) threshold on duty-free imports, which would lower transaction costs for consumers. For traders, government should reduce the cost of moving lower-value shipments across borders, as well as the time it takes and the uncertainty involved. They say that with expanded partnerships between customs agencies and businesses, customs risk assessments — determinations of which goods require additional border screening — could be updated to process goods faster at the border. For instance, valuable information not readily available for traditional trade, such as feedback ratings generated by online transactions, could help expedite customs procedures.

Ahmed and Melin recommend that small businesses be better integrated into "trusted trader" programs. These programs allow the private sector to share in the security responsibilities of customs in exchange for trade facilitation benefits. Mutual recognition agreements, which allow a trusted trader in one country to be recognized as such in other countries, could greatly increase the benefits of participation for SME participants. The authors also highlight other policy issues that are on the horizon, including the benefits of bringing the postal system into mainstream trade policy discussions; the need for a technologically neutral financial services policy to support the growth of digital payment systems; and the importance of international regulatory cooperation on consumer protection laws.

Canada's Integration in Global Value Chains

In recent decades, lower trade costs and technological innovations have allowed companies to split their production processes into different tasks, which can then be separated in space and time along global value chains (GVCs). World trade and production increasingly are structured around GVCs, particularly in industries such as electronics, transportation equipment, textiles and apparel. As a result, most international trade now involves exchanging not finished goods but intermediate inputs. In this part the authors show how the world economy has become more interconnected, demonstrate that Canada's engagement with overseas markets through foreign affiliates has increased, and discuss the importance of being a location that can attract and retain high-value-added tasks.

Global Value Chains and the Rise of a Supply Chain Mindset

Ari Van Assche

Ari Van Assche provides an overview of recent academic research on GVCs, including the "task approach to trade." He examines how being integrated into GVCs has changed the way firms engage in international business and outlines the implications for trade policy. Whereas traditionally firms viewed international trade as a way to expand their sales into foreign markets, companies in GVCs have developed a "supply chain mindset." For these firms, global business is about not just the destination but also the journey. International expansion is a way to reduce production costs, access foreign technology and diversify exposure to supply chain shocks. At the same time, these firms are concerned about the complexities of moving goods, people and information across borders in multistage production systems.

Van Assche presents new cross-country empirical evidence that GVCs are generally good for growth — although he notes that further research is needed to assess the underlying direction of causality. In particular, he finds that countries that have integrated into GVCs tend to have faster output and employment growth. This suggests that increasing GVC integration likely would provide broader economic benefits for Canada, which unfortunately has not kept pace with other countries in this regard. Van Assche's estimates imply that if Canada's GVC trade as a share of GDP had remained the same over the period from 1995 to 2009, rather than falling by 1.5 percentage points, its real GDP per capita growth would have been nearly 0.2 percentage points higher per year over that period, other things being equal.

The policy implication that most stands out from the new GVC reality, Van Assche says, is the importance of connectedness. To retain and strengthen competitiveness, trade policies should help facilitate Canadian companies' ability to connect rapidly and reliably with foreign value chain partners. Moreover, since the productivity of the export sector depends critically on its ability to connect to the most competitive foreign suppliers, policy-makers should focus not only on greasing the wheels on the export side but also on eliminating barriers on the import side. In addition, beyond the barriers that exist at the border, such as tariffs, policy-makers should also seek to remove trade impediments "behind the border," such as differences in product standards. The quality of the transportation infrastructure, communications networks and the regulatory environment all affect the ability of firms to integrate into GVCs. To implement this policy agenda, the government needs to better communicate the economic benefits of GVCs to the public as well as improve coordination of policies among government departments.

Leveraging Global Supply Chains in Canadian Trade Policy

Emily Blanchard

Another implication of the rise of GVCs, according to Emily Blanchard, is the growing importance of international ownership. Globally integrated supply chains, foreign investment and cross-border portfolio holdings mean that Canadian companies' operations now often extend beyond our geographical borders. This is muddying the distinction between national and foreign economic interests. Intuitively, when domestic constituencies hold a direct economic stake in foreign export markets, their home government has less incentive to levy tariffs and other import restrictions. Indeed, the growth of international ownership can provide stronger incentives for governments to liberalize trade. In other research, Blanchard finds empirical evidence that countries with more US offshoring activity — particularly developing countries — enjoy better tariff preferences in the American market.

Blanchard says that governments need to update their approaches to tariffs, input trade, rules of origin and re-exporting. Longer supply chains magnify the inefficiencies of trade barriers. When products cross more borders more often, tariffs — which apply to the total value of goods crossing borders and not the incremental value added in each country — discourage production fragmentation, as the same product can encounter trade barriers multiple times along its journey. Canada took a step in the right direction by removing tariffs on manufacturing inputs, but Blanchard recommends that policy-makers consider going further by removing the remaining import tariffs. This would greatly reduce the regulatory and customs burden on Canadian businesses and customers and would improve production efficiency.

GVCs allow countries to leverage a reinforcing trade-and-investment relationship, especially through preferential agreements. Blanchard warns, however, that Canada should pursue new trade and investment deals selectively and consider their potential costs. For instance, some provisions in these agreements have been criticized for challenging countries' sovereignty through overzealous investor protections. Such agreements could also leave behind countries that are currently outside GVC networks. The resulting diversion of trade and investment could widen the gap between the integrated rich countries and peripheral have-nots. Furthermore, in the long run, such deals would create a "spaghetti bowl" of overlapping rules, potentially undermining multilateral efforts at the World Trade Organization (WTO). To guard against this outcome, Blanchard recommends that Canada maintain an active role in the WTO.

New International Evidence on Canada's Participation in Global Value Chains

Koen De Backer and Sébastien Miroudot

Until recently, GVC analysis was limited to specific case studies such as the production of the iPhone, or to business surveys. But with new data like those developed by the Organisation for Economic Co-operation and Development (OECD) in the Trade in Value-Added (TiVA) database, the extent to which production is fragmented across countries can now be assessed for individual countries. This approach provides a more accurate picture of how much value added each country contributes along supply chains in various industries.

Koen De Backer and Sébastien Miroudot use TiVA data covering 39 advanced and key emerging market countries to describe broader global trends in GVCs and indicate where Canada fits into these trends. They show that production processes have become increasingly international: around the world, firms are importing more in order to produce exports, and GVCs are becoming longer and more sophisticated. The share of foreign value added in gross exports increased from 18 percent in 1995 to 24 percent in 2011.

Canada has increased its GVC participation over the past two decades, though not as much as other regions of the world have, particularly Asia and eastern Europe. In part this reflects Canada's trade linkages with its major partner, the United States, which were already well established by the mid-1990s. Since then, Canada's exports have shifted away from manufacturing and motor vehicles toward the resources sector, which relies far less on foreign content. De Backer and Miroudot find that this shift has had only a minor effect on Canada's overall GVC participation. That is, the strong increase in natural resource prices over the 1995-2011 period is not a sufficient explanation for why Canada fell behind other countries in GVC trade in recent decades.

They highlight the challenges Canada's manufacturing sector is facing in an increasingly open and competitive global economy. In the auto sector, for example, Canada appears to be losing ground to suppliers in Asia and Europe. The data also reveal that services contribute more to international trade than conventional gross trade statistics convey. Moreover, Canada's exports have lower-than-average services content in most industries, particularly in business services, where there might be considerable room for growth.

De Backer and Miroudot's findings underscore the interconnected nature of the global economy. For the OECD as a whole, one out of every four workers are involved in production for final consumers in foreign markets; in Canada, the estimate is nearly one-fifth of employment, or 3.5 million jobs. These results highlight the potential for macroeconomic shocks and policy changes to spill over across countries and for local supply disruptions to ripple through the global economy.

In this context of increasingly interrelated imports and exports, De Backer and Miroudot echo the warning of other authors in this volume that protectionist policies are ultimately counterproductive. Canadian policy-makers looking to boost jobs and growth at home should focus on attracting high-value-added activities, such as research and development, product design and customer services. As well, they emphasize that policies should help ease adjustment costs for displaced workers struggling to find new jobs and learn new skills.

Chasing the Chain: Canada's Pursuit of Global Value Chains

Daniel Koldyk, Lewis Quinn and Todd Evans

Dan Koldyk, Lewis Quinn and Todd Evans build on Blanchard's finding that international ownership matters in a GVC world. They provide a comprehensive look at Canada's economic links with the rest of the world by analyzing customs-based and value-added exports, outward investment, foreign affiliate sales and business strategies. They conclude that Canadian businesses are far more engaged with overseas markets and less dependent on the United States than is commonly believed.

Much as in other countries, Canadian-controlled businesses are changing the way they participate in the global economy and adopting a more diversified business model. Export Development Canada calls this the "integrative trade" approach, and in Canada it means increasingly engaging with overseas value chains. Now foreign affiliate sales in the United States have been surpassed by sales in other overseas markets; sales in emerging markets alone are projected to exceed those in the United States by 2018. Moreover, Canadian foreign affiliates are not simply producing outsourced goods; they are also delivering a wide range of services, including financial intermediation, marketing, after-sales services, logistics, and information and communications technology. In fact, the value of Canada's foreign affiliate services sales has overtaken that of goods production and is now twice as large as services exports.

Koldyk, Quinn and Evans conducted two dozen interviews with business executives, which, together with survey results, provide further evidence that the integrative trade approach is here to stay. They stress that this shift does not necessarily mean replacing onshore output with offshore output. Doing business well abroad also means doing it well at home. Moreover, some critical production tasks simply cannot be performed offshore, and some activities are being brought back onshore after failed experiments abroad.

Canadian companies continue to serve the US market in various ways: through exports, foreign investment and affiliates. For other foreign markets, however, the dynamics are rapidly changing toward much more reliance on outward investment and foreign affiliates. This approach allows Canadian firms to increase production efficiency, capture consumption growth in emerging markets, tap South-South trade networks and overcome market access barriers. Overseas activities can increase revenue streams, generate follow-on exports and contribute to the Canadian economy through profit repatriation, which is subject to Canadian taxes. Such activities can also support Canadian jobs in the front office, on the shop floor, in research and development, and in a wide range of professional services such as accounting, consulting and legal services. Finally, the authors say that our understanding of these issues and how policy should respond would benefit from better and timelier data, particularly on value-added trade and foreign affiliate sales.

By Road, Rail, Sea and Air: The Role of Transportation Networks in Moving Canada's Merchandise Trade

Jacques Roy

Canada's competitiveness in global markets and the reliability and efficiency of its transportation infrastructure go hand in hand. Jacques Roy examines the role that infrastructure plays in moving goods in and out of the country by four key transportation modes: road, rail, sea and air. His analysis is based on detailed Transport Canada data and insights gleaned from interviews with industry stakeholders and transportation officials. Roy finds that Canada's overall transportation and logistics networks perform reasonably well compared with those in other countries, but there is room for improvement in several areas, such as addressing road congestion in major Canadian cities, increasing container port competitiveness, improving rail and air cargo capacity and boosting cost competitiveness.

Over the past decade, the shares of Canada's merchandise trade that have been transported by sea and air have increased, and shares transported by road and rail have fallen. These trends could be reinforced if recent trade deals with European and Pacific Rim countries are implemented. A key driver of these trends has been Canada's stagnating trade with the United States, along with the growth in its trade with the rest of the world. The US share of Canada's overall merchandise trade has shrunk from 76 percent in 2002 to 63 percent in 2012. These changes matter for transportation use, because Canada's trade with the United States relies mostly on roads, rail and pipelines, whereas trade with the rest of the world relies primarily on marine and air modes (sea transport is primarily used for trade with Asia, while air is the dominant mode used for trade with western Europe).

The value of Canada's trade moved by sea nearly doubled between 2002 and 2012. The biggest increases in marine traffic were on the west coast at the ports of Vancouver and Prince Rupert. This is probably because of increased trade with Asia, particularly China. Canadian ports are generally well equipped to handle bulk products, but the competitiveness of our container ports is more fragile. Recent challenges include labour disputes, disruptions in rail capacity in the winter to transport containers further inland to their final destinations and concerns that climate change might reduce river depth and handling capacity along the St. Lawrence Seaway.

Canada's air cargo market faces the perennial challenge of its small size, which limits freighter capacity and reduces its cost competitiveness relative to US alternatives. This competitive disadvantage is exacerbated by relatively high taxes and landing fees in Canada. The rail system, meanwhile, is facing capacity constraints and service issues, as well as safety concerns and regulatory reviews after the tragic accident in Lac-Mégantic in 2013.

Roy notes that countries that lead the global logistic performance rankings have invested heavily in major hubs to efficiently connect transportation modes. As the federal government looks to increase infrastructure spending, it should earmark significant funding for improving the nation's trade-related infrastructure, which would support its internal and international trade, thus increasing longer-term prosperity.

Canadian Commerce Policies in an Interconnected World

The theoretical analysis and new empirical findings in the previous parts reveal important trade policy challenges. The authors in this part examine in more detail where and how policy-makers might address some of these challenges, including by assessing the potential to do so in alternative negotiating venues. They highlight the central importance of the WTO for the health and coherence of the global trading system, as well as the need for better international regulatory cooperation and increased foreign competition in key service sectors in Canada.

Canadian Trade Policy in a G-Zero World: Preferential Negotiations as a Natural Experiment

Robert Wolfe

Robert Wolfe analyzes international trade negotiations in what he calls a "G-Zero" world: one where no group of countries, including the G-7 or the G-20, is able or willing to take the lead on international trade issues. In recent years, global power has shifted and become more diffuse, in large part due to the emergence of China. With talks at the WTO largely stalled, negotiators have turned to other venues, hoping that it will be easier to create new trade rules with smaller groups of like-minded countries. What is unfolding, says Wolfe, is an experiment by negotiators to determine which types of agreements can work, by varying the topics covered, the number of participants, the negotiating methods and the legal relationship of the results to the WTO. Canada has participated actively in this experiment, concluding two major trade deals — the Comprehensive Economic and Trade Agreement (CETA) across the Atlantic and the Trans-Pacific Partnership (TPP) across the Pacific — although these agreements, at the time of our writing, must still overcome significant opposition if they are to be implemented. In pursuing this preferential — instead of multilateral — approach, will negotiators succeed in effectively rewriting the global trade rules for the twenty-first century? Wolfe thinks not, and he foresees an eventual return to the WTO.

Even if major preferential trade deals are implemented, Wolfe argues that their institutional weaknesses — such as the absence of robust surveillance mechanisms, active secretariats and effective dispute settlement mechanisms — ultimately mean that such deals will not be useful stepping stones toward a coherent global trading system. Weak institutions will be a significant hindrance to important aspects of the contemporary trade policy agenda, such as regulatory cooperation. Wolfe also points out that some major negotiations deliberately omit China for geopolitical reasons, which significantly limits their potential impact. Moreover, proliferating preferential deals create confusing overlaps and inconsistencies between agreements that many firms involved in GVCs will find unmanageable.

According to Wolfe, these problems are better addressed, in principle, in the multilateral WTO forum, which functions as Canada's free trade agreement with 163 other countries, including all of our largest trading partners. Strengthening the WTO as an institution, therefore, should be a central, longer-term objective of Canadian trade policy. This objective will require overcoming obstacles to agreement on long-standing issues and bringing new topics into the mix. Wolfe sees the WTO as Canada's best hedge against uncertainties about future trade and investment patterns, especially not knowing today which new markets Canadian firms will wish to pursue in 10 or 20 years. He says that losing what is left of the moribund Doha Round of trade negotiations would not be the end of the world for the WTO, but losing the WTO would be disastrous for megaregionals, which effectively are WTO side deals that depend on rules, such as subsidies and trade remedies, that must be determined multilaterally.

The crucial missing element needed to create a more coherent global trading system is accommodation between the United States and China. Canada cannot resolve this impasse between its two largest trading partners, but through the recent exploratory discussions on a possible free trade agreement with China, Canada has chosen to negotiate with rather than around the world's largest trader. Wolfe endorses this decision, saying it will advance both sides' knowledge about how China can be further integrated into the global trading system. More important — given that one of the paramount, perennial objectives of Canada's trade policy continues to be maintaining access to the US market and to US-centred supply chains that is at least as good as that of any other country — Canada will want to participate in any plurilateral negotiations initiated by the United States, just as it must be willing to discuss new American ideas about improving the North American Free Trade Agreement (NAFTA).

International Regulatory Cooperation in a Supply Chain World
Bernard Hoekman
In today's trade environment of GVCs and low tariffs, the regulatory policies that restrict the international flows of goods, services, knowledge and professionals become more prominent. Examples include product regulations to achieve health, safety or security objectives; licensing requirements for services providers; and certification procedures for production processes. The economic gains from better international regulatory cooperation are substantial, but realizing them will require new policy approaches.

Bernard Hoekman discusses three important obstacles to regulatory cooperation: mandate gaps between trade negotiators and domestic regulators; coordination gaps within and between governments, and between government and business; and information gaps within and across countries. Ultimately, he says, "policy silos" are at the root of the problem. Typically regulations are developed independently by officials with little incentive or ability to take into account the cross-border economic effects of their decisions. The result is a plethora of minor differences across jurisdictions in regulations that have similar policy objectives but impose redundant or inconsistent requirements. These differences raise the cost of doing business, to the point that regulatory compliance has now become a top concern for companies involved in GVCs. The differences also hinder global trade, and estimates suggest that much larger gains could be achieved from better regulatory cooperation than from further tariff cuts.

Hoekman proposes a new way to improve regulatory cooperation by breaking down the policy silos that separate regulatory and economic policy-making. What is missing from current approaches, he argues, is a cross-cutting, deliberative mechanism that focuses on the forest rather than on the trees, encourages learning and builds trust through regular interactions among stakeholders. He advocates the creation of supply chain councils, composed of senior representatives from government, business and labour, that would function as advisory bodies in the various industries. These councils would identify areas with the most to gain from regulatory cooperation and establish performance indicators to monitor the implementation of policy reforms.

He maintains that Canada's most urgent regulatory policy challenge is to achieve better convergence of North American and European standards through continued efforts in the Canada-US Regulatory Cooperation Council and the regulatory cooperation forum for Canada and the European Union that would be part of CETA. Over the longer term, he says, Canada should take a leadership role on these issues at the WTO, because the global nature of production ultimately means that regulatory cooperation should be open to all countries. Multilateral cooperation is particularly important for countries like Canada that lack the political or economic weight to drive regulatory convergence on their own. Canada should also support regulatory cooperation in forums with broader membership, such as the OECD and Asia-Pacific Economic Cooperation, in order to build momentum to tackle these issues.

Problems with regulatory coordination exist within countries, not just between them. In Canada, individual provinces often set their own regulations in an uncoordinated approach that creates internal trade barriers. Hoekman recommends that a Canadian regulatory cooperation council be set up to help modernize the outdated Agreement on Internal Trade.

The Restrictiveness of Canada's Services Trade Policy in an International Context

Sébastien Miroudot

Regulatory cooperation is especially important for trade in services. While services traditionally were regarded as largely nontradable across international borders, the information and communications revolution has made them easier to trade over long distances. Developments such as the fragmentation of production in GVCs, the rise of foreign affiliates that can provide the local presence needed to sell services abroad and the high services content embodied in traded goods are all providing a better appreciation of the important role that services play in international trade. They also highlight the role of this huge sector as a driver of aggregate productivity, with large upside potential from beneficial policy reforms.

In an environment of continual technological change, countries that adopt policies to facilitate the seamless provision of services and data across international borders stand to benefit most from these developments and from new business models. So is Canada's policy stance helping or hurting its services trade? Sébastien Miroudot looks at this issue in an international context using the OECD's Services Trade Restrictiveness Index, a database that identifies trade barriers based on laws and regulations currently in place in 42 countries (the 34 OECD members, plus major emerging economies). In 2015, Canada ranked around the middle of the pack overall in terms of trade restrictiveness. Beneath the country averages, however, the restrictiveness of services trade varies significantly by sector. In most sectors (15 out of 22), Canada's policies are less restrictive than the sample average. For instance, Canada has a relatively open regime for foreign professionals, particularly in legal and engineering services, accounting, insurance, architecture and computing. But it has higher-than-average barriers in air transportation, broadcasting, courier services, telecommunications, construction, wholesale and retail trade, and motion pictures. Some services — transportation, telecommunications and finance, in particular — are used as key inputs by other industries. Increasing competition in these "networked" service sectors, which are essential drivers of productivity, would have positive spillovers for the Canadian economy.

Most of Canada's reported barriers in services relate to foreign entry and the treatment of foreign investment. For example, in all sectors of the economy, at least 25 percent of the members of corporate boards must be Canadian residents or citizens. In addition, in sectors where the *Investment Canada Act* applies, investments are subject to screening, whereby foreign investors acquiring Canadian businesses that are valued above established thresholds must show likely net benefits to Canada, while domestic investors have no such obligations. Miroudot points out that the legal regime for services trade needs to be updated by committing in international agreements to lock in the openness of the de facto trading regime, which is more liberal than Canada's commitments under the WTO's General Agreement on Trade in Services.

The Potential to Enhance Canada's Services Trade in CETA, the TPP and TiSA
Erik van der Marel

While Miroudot focuses on the relative restrictiveness of Canada's services policies, Erik van der Marel analyzes the potential to increase Canada's services trade through the major preferential negotiations underway. Services feature prominently in CETA and the TPP, and Canada also participates in the plurilateral 50-country Trade in Services Agreement (TiSA) negotiations. Looking at the services that Canada exports and those that other trading partners import, van der Marel finds that the country groupings in these three trade agreements are all reasonably good matches for Canada.

He examines the potential to increase Canada's services trade using gravity analysis, which predicts countries with which Canada is "undertrading" and "overtrading" in services when the observed trade is above or below the gravity model's predictions. He finds that Canada has room to expand its services exports to the United States, even though it is already quite active in that market, as well as to several countries in the European Union — most notably, France and the United Kingdom — where Canada currently is far less active. By contrast, Canada may be overtrading in services with China and Hong Kong, as well as with some Caribbean tax havens (the latter related to financial services flows from Canada to those countries).

In order to pursue gains through trade negotiations, van der Marel says, implementing the TPP would benefit Canada's services trade — particularly with the United States. Naturally, the implementation of CETA could improve Canada's services trade with the European Union, but van der Marel notes there were some missed opportunities, as several sensitive sectors were kept off the negotiating table. TiSA could expand market access to a much broader set of countries, although the ultimate level of ambition in this deal remains to be seen. Here, the author says, Canada could push for additional market access beyond simply locking in the status quo, something that could benefit all the agreement's signatories.

The author argues, however, that Canada does not necessarily need to wait for negotiated trade agreements to be implemented in order to develop a more competitive services sector. Canada has plenty of opportunities to remove domestic restrictions unilaterally, or to lock in existing trade preferences, particularly in services sectors that are important inputs to the rest of the economy but where barriers to foreign entry remain high, such as in transportation, finance and telecommunications. These actions, he says, would provide broader economic benefits to Canada's economy over the long run, even if outstanding trade agreements are not implemented quickly.

Navigating the Maze: Canada, Rules of Origin and the Trans-Pacific Partnership
Sandy Moroz
Another complicated aspect of trade negotiations deals not with trade in services but with goods trade. Rules of origin define how much production and input sourcing of a good must occur in a free trade area for the producer to benefit from tariff preferences. Finding agreement on these rules has always been important, but the stakes have increased due to the growth of GVCs and preferential trade deals.

Sandy Moroz examines how, in regional trade agreements, negotiators can weave together a disjointed web of rules under separate trade deals, creating a common rulebook for a larger combined free trade zone. For instance, 32 free trade agreements, each with its own set of rules, are currently in force among subsets of the 12 TPP signatories. If implemented, the TPP could significantly reduce compliance costs for producers selling in the larger combined market. Firms would have to deal with only one set of paperwork, and they would be able to source inputs originating from any TPP country at preferential tariff rates (allowing them to buy from the lowest-cost or highest-quality suppliers within the zone) and supply TPP-originating inputs to producers in other TPP countries.

Ultimately, the gains from the TPP's single set of rules depend on how they compare with those under existing deals between TPP countries. Here Moroz breaks new ground and finds that, for many agricultural products and for textiles and apparel, the TPP negotiators largely accommodated parties' sensitivities by using the most restrictive rules of origin in existing free trade agreements involving TPP signatories. On the other hand, TPP rules for most non-agricultural products would allow TPP producers to import more inputs from outside the TPP area than provided for under the current rules. For example, in the controversial auto negotiations, the TPP rules are more liberal than the NAFTA rules and would allow Japanese car producers to maintain their Asian-based supply chains — an outcome that caused concern in North America, particularly among smaller parts producers.

Moroz argues that the potential effects of the TPP on Canada's auto sector need to be seen in their proper context. The central question the sector faces is where in North America vehicles will be assembled in the future. In this regard, Canada's ability to keep vehicle production and attract new investment will depend not so much on the removal of tariffs on Japanese-made vehicles and less restrictive TPP rules of origin but on a suite of other, more general competitiveness factors — including labour productivity, infrastructure, regulations and the medium-term outlook for the Canadian dollar, as well as Canada's policy response to incentives offered by governments elsewhere in the region. Moroz says the auto sector will face increased international competition regardless of whether Canada joins the TPP, but he concludes that ultimately Canada's participation would offer its auto firms more opportunities.

Although the TPP's rationalization of rules of origin is valuable, even better would be an effort by the WTO to develop a harmonized set of preferential rules of origin. Achieving multilateral agreement would not be easy, but meanwhile individual countries could weave together existing trade agreements without harmonizing rules across agreements. Canada has included such a provision in its free trade agreements since NAFTA, though it has not yet been activated.

Ultimately, Moroz says, Canada's dependence on the United States remains the dominant factor in its approach to rules of origin negotiations. Accordingly, Canada needs to continue to seek rules that reflect the importance of the United States as both a major supplier of inputs and a major market for outputs in many Canadian sectors.

Canadian Investment Treaty Policy: Stay the Course on Progressive Developments

Andrew Newcombe

One of the most controversial topics in recent trade negotiations has been the design of rules to settle disputes between foreign investors and host countries — so-called investor-state dispute settlement (ISDS). Advocates of ISDS say that by respecting due process and property rights and by requiring minimum standards of treatment, investment treaties can protect and promote foreign direct investment as well as the rule of law and good governance. But in recent years, as the number of international investment agreements and ISDS claims grows, criticism of the international investment regime has increased. Critics are concerned about many issues, including that ISDS tribunals have the power to review host country laws and question the domestic policy decisions taken by sovereign governments to protect human health and the environment (although they cannot directly order changes). Moreover, these tribunals can order countries to pay damages to foreign investors if commitments are violated.

Andrew Newcombe helps put this debate in context by providing an overview of the international legal framework governing foreign investment. He examines the main critiques of the investment treaty regime and reviews the most significant changes to treaty practice over the past decade in Canada and the United States that try to address concerns. He shows that investment treaty policy has evolved significantly over the past decade and that Canada has been at the forefront of these developments. He argues that Canada should continue to play a leadership role and make improvements to its investment agreements, which balance the protection of foreign investment with domestic regulatory flexibility. He sees the updated investment chapter in CETA as a model to build on in Canada's future investment agreements (that is, the amendments that include the Investment Court System and other provisions designed to affirm the right of host countries to regulate in the public interest, such as the Joint Interpretative Instrument).

Canada has been involved in many investment disputes, whether in regard to investors' claims or as a respondent state (mainly under NAFTA's chapter 11). In Newcombe's view, Canada's legal counsel have generally been successful in defending Canada against questionable claims. When viewed in the context of the stock of foreign direct investment in Canada, awards to date in favour of foreign investors represent a very small fraction of those investments (less than 0.025 percent). Moreover, he sees no convincing empirical evidence to demonstrate that ISDS rules have prevented Canadian policy-makers from regulating in the public interest.

The author concludes that Canada has an interest in continuing to support international investment obligations that are supported by ISDS. The fundamental rationale, he says, for the international investment regime is to protect investments by adhering to and enforcing international standards. Canada and other countries have a systemic interest in supporting an international standard of ISDS that extends beyond any single agreement. Furthermore, Canada and other advanced economies cannot expect other countries to accept the obligations in modern international investment agreements if they are not willing to be bound by them.

Canada and the European Union have committed to pursue, with other trading partners, establishment of a multilateral investment tribunal and appellate mechanism to resolve foreign investment disputes. Newcombe says that although this is a positive development, it is unlikely to succeed in the short term unless it gains the support of major economic powers, such as the United States and China, which is unlikely. Thus, he says, even though a comprehensive multilateral investment framework to replace the current regime of thousands of agreements clearly would be more efficient and effective, it should be a long-term goal, not a short-term priority.

Practitioner Perspectives on Canadian Trade

Constructive discussions about how best to redesign Canada's trade policies necessarily extend beyond the halls of government and academia, motivating our desire to assemble various practitioner perspectives. The contributors to this part represent business, labour, industry associations and nongovernmental organizations. Many of their recommendations are in line with suggestions elsewhere in the volume. For instance, there is consensus that Canada's trade performance has been disappointing thus far in the twenty-first century, and that a concerted effort is required to address this situation. Several authors urge Canada to move quickly to implement what is possible from CETA and the TPP — large trade deals that, as we write, are formally concluded but still outstanding — and to make progress on trade talks with important emerging economies, particularly China and India. Jim Stanford, however, challenges this view that implementing more trade agreements will necessarily benefit Canadians and Canadian companies. In addition, authors in this part stress several needs: to simplify regulatory procedures and tariffs; for government to better promote its existing trade support programs; and for Canadian policy to ultimately encourage the growth of firms rather than, in effect, rewarding firms for staying small. The final three commentaries consider Canadian trade in a broader global context, where trade policy now must take account of environmental concerns and address the imperative of achieving more inclusive growth.

How Business Can Help Free Trade

Perrin Beatty and Cam Vidler

Leading off the business perspectives, Perrin Beatty and Cam Vidler argue that the rise of new trade centres in emerging markets has shifted global power and made it harder to achieve global cooperation on trade issues. Relying on governments alone to liberalize trade will not work. Businesses have a key role to play in shaping the trade policy agenda and in effectively communicating the gains of free trade for consumers, workers and entrepreneurs. They say that business groups like the B20 Coalition and the World Economic Forum need to strengthen ties with their foreign counterparts and adopt a multipronged approach to target various pressure points in today's increasingly fragmented trade policy regime.

Beatty and Vidler offer three lessons for the business community. First, freer global trade will not be achieved in one big bang. Businesses must work incrementally at all levels. They should not give up on the multilateral trade system, but they cannot afford to put all their eggs in the WTO basket. A regional approach to trade negotiations seems to be here to stay. At the same time, much can also be done outside traditional trade negotiations, in forums such as the G-20 and in national capitals around the world.

Second, inclusiveness matters. The rise of new trade powers means that industry groups in OECD countries have to forge new partnerships with their counterparts in emerging markets and work with them to build a common vision.

Third, trade cannot be addressed in isolation. Businesses have to ensure that policies affecting trade — in areas such as energy, climate change, product safety and privacy — are effective and better coordinated. Half-measures or fragmented approaches will only engender public opposition, put companies at a competitive disadvantage and ultimately sap the will of countries to liberalize trade rules. Beatty and Vidler stress that maintaining positive momentum in the global trading system is an uphill battle, and that everyone needs to contribute. For Canada, especially — a middle economy highly exposed to cracks in the trading system — indifference is not an option.

Canada's Global Firms and the Future of Trade Policy

John Manley and Brian Kingston

John Manley and Brian Kingston say that an international commerce strategy that positions Canadian firms to take advantage of global markets is central to securing our long-term prosperity. They demonstrate that large firms are the main drivers of Canada's international trade, accounting for almost three-quarters of the total value of the country's goods exports in 2014.

The authors identify Canada's declining competitiveness in the US market as a key policy challenge. They note that, in 2015, for the first time in history, the goods trade between the United States and China exceeded Canada-US goods trade. To address this issue, they propose improving infrastructure at the border and streamlining market access between the two countries by adopting a default policy of "align or explain" for Canada-US regulatory cooperation. This would allow Canada to maintain its own standards for health, safety and the environment in cases where the "national interest" justifies it.

Manley and Kingston call on Canada to implement what is possible from CETA and the TPP, to conclude the long-drawn-out talks with India and to eliminate our remaining tariffs unilaterally. They point out that Canada sends a smaller share of exports to emerging markets than do most other advanced economies, and they say we need to continue the efforts to diversify our trade. Perhaps the largest element missing from Canada's current trade strategy, they say, is a comprehensive plan to improve the country's engagement with China, a key part of which would be to officially launch bilateral trade talks.

Small Business Traders in Canada

Ted Mallett

Ted Mallett provides a perspective from Canadian SMEs, 10 percent of which are direct exporters of goods or services, and which collectively accounted for over a quarter of the value of Canada's goods exports in 2014. Mallett notes that because the fixed costs of international trade — such as the time required to learn about new markets or the effort needed to apply for government trade support programs — are often similar for both large and small firms, trade costs disproportionately restrain SME trade, particularly for small, lower-value shipments.

The author addresses the question of how federal government policy can encourage trade by Canadian SMEs. First, the government should undertake an economic impact assessment of its border fees, including a thorough review and consolidation of the overly complicated tariff classifications. This would make trading internationally easier for all Canadian firms, but particularly for SMEs and first-time traders. Second, it should waive the duties on small-value shipments. Some of these duties exceed the value of the product or service, rendering such trades uneconomical and unnecessarily burdening the government, in exchange for little revenue. Third, it should try to fill information gaps. Firms need more clarity and consistency on customs procedures and costs before they trade. For example, the Canada Border Services Agency could devote more effort to making its website more accessible for SMEs and first-time traders. Finally, the government needs to design trade programs with SMEs' needs in mind and promote them better. Most SMEs have limited awareness of and do not use programs that encourage trade.

At the same time, Mallett urges the government to maintain some of its more effective programs. These include the Regulatory Cooperation Council, which works with the United States to harmonize regulations; the Beyond the Border initiatives, which aim to streamline and simplify the cross-border movement of goods and people; and the one-for-one rule on regulation, whereby government must eliminate or modify an existing regulation before introducing a new one.

How to Promote Smart Exporting among Canadian Companies
Bill Currie

Bill Currie also examines the question of how the government can encourage trade, drawing his insights from interviews Deloitte conducted with 46 experienced Canadian exporters. Echoing Mallett's recommendation, Currie suggests actions to improve awareness of existing trade support programs. He points out that surprisingly few Canadian firms know about the various programs available, such as government supports, mentorship and networking opportunities. He says that governments and industry organizations must work together to improve the visibility and accessibility of these programs and consolidate the available information to reduce the confusion and burden for businesses seeking assistance.

Currie calls on government to structure business tax incentives around growth, not firm size. He says that many federal and provincial policies heavily favour small businesses: for example, by offering them a lower general corporate tax rate or more generous research and development tax credits, which can create a disincentive for businesses to grow. Replacing size-based qualification criteria with ones that reward growth would encourage more Canadian businesses to expand through exporting.

With the rapid growth of emerging economies, Currie says, Canada should continue to reduce its reliance on the US market and expand its linkages with other trading partners that are driving future growth. To that end, he agrees with other authors in this volume that Canada should implement what it can from outstanding trade deals and conclude agreements with emerging market countries such as India. He adds that post-agreement commercialization frameworks are essential to enable government to measure the performance of free trade deals and track progress toward specified targets.

The Supply Chain Echo and Its Effects on Canadian Businesses
Joy Nott

Joy Nott provides the perspective of an industry association. The Canadian Importers and Exporters Association (I.E. Canada) is particularly relevant to the operations of Canadian firms involved in GVCs. She stresses the need for the government to implement policies and procedures that make it easier for companies to do business in Canada and with Canada.

Much of the thinking on Canadian trade policy, Nott says, mistakenly presumes that the supply chain ends with customs clearance. In reality, even after the import has crossed the border, firms face a tangled web of regulations that can be overwhelming for many Canadian businesses that trade internationally. Canadian traders — who are increasingly importing in order to export technologically advanced goods and services — want policy-makers to mitigate the negative effects on business of the "supply chain echo," whereby trade policies, procedures and penalties can affect imports long after the goods have cleared customs and crossed borders. For example, the file on an import can be revisited many times after the actual import, often by many parties apart from the importer. Years afterwards, audits may be conducted, refund claims submitted and requests for further information made, and companies can owe the government money because of changes in the interpretation of customs policies. Having such "echoes" in its policy implementation increases uncertainty for Canadian firms and makes our country a less attractive location for doing business. In its approach to designing regulations and reducing red tape, Nott says, Canada should not necessarily seek fewer rules but should work toward simpler ones with more consistent outcomes. Such changes to Canada's policy thinking could significantly improve the global competitiveness of Canada's international traders in the business environment of the twenty-first century.

Is More Trade Liberalization the Remedy for Canada's Trade Woes?
Jim Stanford

Several commentators recommend further trade liberalization as a way to improve Canada's poor trade performance through enhanced market access abroad and increased competitive pressures at home. Jim Stanford agrees that Canada has a trade problem, but he offers a different diagnosis of its causes and proposes different policy priorities.

Stanford points out that, since 2001, Canada has ranked a disappointing 33rd out of 34 OECD countries in real export growth. He views the deterioration in the quality of Canada's exports to be as troubling as the decline in their quantity. He is also disturbed by the shift in the composition of exports to primary sectors (agriculture, energy, mining and forestry) and away from "high-value-added" sectors (automobiles, aerospace, industrial machinery and equipment, electronics and consumer products). Stanford attributes this shift not simply to higher commodity prices over this period but also partly to Canada's lack of international competitiveness in the high-value-added sectors related to its overvalued currency and to other underlying structural weaknesses. He is concerned about what he sees as a general failure to build a sufficient base of innovative, export-oriented businesses in Canada that sell value-added products and services that world markets demand.

Stanford notes that Canada's trade performance with its free trade agreement partners, particularly in manufactured goods, is worse than that with the rest of the world. Export growth has been slower with Canada's free trade partners than with other countries, but import growth has been faster. He acknowledges that the correlation between trade liberalization policies and poorer trade performance does not prove causation, but he argues that trade and investment liberalization probably has caused Canada more harm than good in the twenty-first century because of our lack of competitiveness in both cost and quality/innovation. Canadian firms have been unable to capitalize fully on a variety of new opportunities abroad, including those resulting from recent trade and investment deals. Yet those same deals have also exposed Canadian firms to increased foreign competition at home, which undermines rather than strengthens Canada's productive capacity when its firms are having difficulty meeting this global challenge.

Stanford therefore suggests that policy-makers shift their focus away from implementing more big trade deals and explore other ways to support the development and growth of globally oriented, innovative, technologically intensive firms in Canada. These firms need help to upgrade their activities and to project themselves more effectively onto the global stage. Government should help these firms to grow, rather than subsidizing small companies with perverse incentives such as lower tax rates, which discourage growth.

Stanford says that signing more free trade agreements might not be a magic bullet for Canada's trade woes, and Canada's trade policy community should be more open to this possibility. He argues that the effects of these deals can be positive or negative, depending on their provisions, the trading partners involved and the readiness of Canadian industries to grow exports and attract mobile investment. Stanford concludes that, over the past decade, trade negotiations have probably done more harm than good to Canada's trade and foreign investment, and that actively pursuing more large trade and investment deals might make things worse.

Trade and Sustainable Development
Scott Vaughan
The quest for sustainable development, which is one of the most difficult policy challenges of our time, has important implications for the global trading system. Scott Vaughan describes how environmental concerns have become a part of international trade policy over the past two decades and discusses some implications for Canada. He says that properly crafted trade and environmental policies can work together to promote better outcomes and encourage sustainable development. As a trader of environmental goods and services, Canada has much to gain from concluding trade deals such as the Environmental Goods Agreement — an ongoing negotiation among several WTO members that seeks to liberalize trade in a broad range of environmental goods, such as renewable energy. More generally, Vaughan argues that strengthening the multilateral trading system is in Canada's long-term interest and could contribute to achieving the United Nations' Sustainable Development Goals. It will not be easy, he says, but Canada has the bureaucratic capacity and diplomatic skills to make a difference.

Inclusive Trade, Inclusive Development: Opportunities for Canadian Leadership
Margaret Biggs
Margaret Biggs re-examines Canada's approach to trade and development. She starts by describing how views of the links between trade and development — in Canada, in developing countries and in global trade discussions more generally — are being recalibrated in response to global economic, political and social shifts. For instance, economic activity and power is shifting to developing economies. Technology and globalization are reorienting international trade and investment around GVCs. Advanced economies are increasingly turning their attention to "behind-the-border" issues like regulatory cooperation and investment rules. And

there is a new emphasis on the need for more inclusive growth, particularly in political discussions in advanced economies. These shifts mean that how trade impacts development is no longer a marginal issue or one that pertains only to the needs of developing countries; instead, it is an essential part of promoting global growth, reducing poverty and protecting the future of the international trading system. It is therefore increasingly important to Canadian trade policy.

In her analysis of the implications of these trends Biggs identifies strategic opportunities for Canadian leadership. She argues that "inclusive trade" — trade that is inclusive of developing and emerging countries and that advances shared prosperity within countries — is now central to the future of the international trading system and to any conception of a progressive trade agenda for Canada. She concludes that Canada is well positioned to find creative ways to integrate trade and development for the benefit of developing and advanced economies. Canada should become a global leader on trade and investment facilitation; work to reinvigorate the multilateral system; prioritize inclusive trade in its development efforts; promote two-way trade and investment with developing economies; and ensure that its social policy architecture is sufficiently robust to support an internationally integrated and inclusive economy.

How Gender Affects SMEs' Participation in International Trade

Arancha González

Arancha González examines the gender dimensions of international trade and proposes policy reforms to connect more women-owned small businesses to global markets. She argues that improving the trade and performance of these businesses would offer better economic and social opportunities for women, increase growth prospects and result in a more equitable distribution of income.

The author highlights the striking disparities between men's and women's participation in trade. For instance, a recent survey of 20 developing countries reveals that only one in five businesses that trade internationally are owned or managed by a woman. She says that is not a reflection of women's preferences but a result of the unique constraints and challenges that women entrepreneurs face. These challenges include explicit regulatory biases, procedural obstacles and cultural biases that limit the time that women entrepreneurs have to work and their access to resources like financing, land, information and business networks — all of which make it easier to identify and seize business opportunities.

González says that in order to establish a more enabling environment for inclusive trade, we must acknowledge that trade policies are not gender neutral, and then work to make the international trade system address the key challenges women face. For example, the conclusion of bilateral trade agreements with affected countries could be made conditional on removing legal discriminations against women's economic participation. Moreover, future trade agreements could include commitments that are crafted through a gender lens (as in the recent trade deal between Chile and Uruguay). The effect of trade and trade agreements on the advancement of women's economic empowerment should also be regularly examined, including in the WTO's Trade Policy Review Mechanism. Multilateral development assistance can also help build trade capacity and incorporate gender issues across its projects. González describes recent examples that include the SheTrades Initiative, which seeks to connect 1 million women entrepreneurs to global markets by 2020. Intergovernmental programs such as the United Nations' Sustainable Development Goals can help foster gender-related discussions and policy actions.

González says that now more than ever it is imperative that all actors work together to make equal economic opportunities a reality for men and for women. An equal and just society is a worthy goal; it is also smart economics. Removing the barriers that prevent women from fully participating in and benefiting from trade is in everyone's interests.

Appendix: Summary of the Authors' Policy Recommendations

Recommendations	Chapter references
1. Maintain preferred market access to the United States In the current context, prepare for a possible renegotiation of the North American Free Trade Agreement (NAFTA), including assessing what might be incorporated from the Trans-Pacific Partnership into a renegotiated NAFTA; improve North American regulatory cooperation.	Currie; Manley and Kingston; Moroz; van der Marel; Wolfe
2. Implement CETA Implement the Comprehensive Economic and Trade Agreement (CETA) with the European Union, with a postagreement framework to evaluate progress toward specified targets.	Currie; Hoekman; Manley and Kingston; van der Marel
3. Engage emerging markets Promote two-way trade and investment as well as learning by both sides by formally launching bilateral trade talks with China; conclude the Comprehensive Economic Partnership Agreement with India.	Biggs; Currie; Manley and Kingston; Wolfe
4. Promote inclusive trade and development Implement the World Trade Organization's (WTO's) Trade Facilitation Agreement and eventually expand these efforts to facilitate investment; help developing countries build their trade capacity; create a Canadian development finance institution of global scale and ambition; regularly examine the effects of trade and trade agreements on the advancement of women's economic empowerment (including in the WTO's Trade Policy Review Mechanism); include commitments crafted through a gender lens (gender chapters) in Canada's future trade agreements.	Beatty and Vidler; Biggs; Blanchard; González
5. Strengthen the multilateral trade and investment system Help develop a stronger multilateral trade system and new negotiating agenda at the WTO; remain active in plurilateral negotiations for the Trade in Services Agreement and the Environmental Goods Agreement; build upon CETA's updated investment chapter for Canada's future investment agreements, and promote a multilateral investment framework as a long-term goal to promote and protect foreign investment and resolve disputes.	Biggs; Blanchard; Hoekman; Newcombe; van der Marel; Vaughan; Wolfe
6. Improve Canada's trade infrastructure Make long-term investments in Canada's and North America's trade infrastructure, including transportation and communication networks; address domestic road congestion in major Canadian cities; increase container port competitiveness; improve rail and air cargo capacity; reduce high airport taxes and landing fees.	Roy; Van Assche
7. Address trade costs at the border Reduce or eliminate remaining import tariffs in sectors beyond manufacturing; assess the economic effects of Canadian border fees; review and attempt to consolidate remaining tariff classifications; provide clarity and consistency on customs procedures and costs.	Blanchard; Mallett; Moroz; Nott
8. Better align regulations across borders Create North American supply chain councils; continue the work of the Canada-US Regulatory Cooperation Council (including considering an "align or explain" default position for Canada on US regulations); establish a Canada-EU regulatory cooperation forum in CETA; seek not necessarily fewer rules and regulations, but rather clearer ones to facilitate business compliance.	Hoekman; Lapham; Mallett; Manley and Kingston; Moroz; Nott

Appendix (cont.)

Recommendations	Chapter references
9. Enhance competition in networked service sectors Reduce restrictions on inward foreign investment, particularly in services sectors that are key inputs to the rest of the economy, such as transportation, finance and telecoms; commit in international agreements to lock in the services trade openness of the de facto trading regime.	Miroudot; van der Marel
10. Encourage trade by small and medium-sized enterprises Design and promote government trade support programs with the needs of small and medium-sized enterprises (SMEs) in mind; help fill information gaps with a dedicated government website for SMEs and first-time traders that surveys foreign market conditions and helps potential exporters make well-informed decisions based on their circumstances; maintain effective trade commissioner services to act as troubleshooters that help to resolve problems facing Canadian traders.	Mallett; Nott; Sui and Tapp
11. Ensure that business taxation does not discourage growth Review and consider replacing federal and provincial tax rates and credits that unintentionally discourage the growth of SMEs.	Currie; Lapham; Stanford
12. Facilitate online and technology-enabled trade Raise Canada's low-value (*de minimis*) threshold exemption for duty-free imports; expand partnerships between customs agencies and online businesses to process goods faster at the border; better integrate small businesses into trusted trader programs; bring the postal system into mainstream trade policy discussions; develop a technologically neutral financial services policy to support the growth of digital payment systems; pursue international regulatory cooperation on consumer protection laws; improve broadband access across Canada, particularly in rural areas.	Ahmed and Melin; Mallett
13. Strengthen labour market support programs Strengthen Canada's employment insurance system as well as skills development and (re)training policies to better support those negatively affected by trade; facilitate the reallocation of resources to their most productive uses; generally support an internationally integrated and inclusive economy.	Biggs; De Backer and Miroudot
14. Improve the collection, coverage and timeliness of trade-related statistics Make more disaggregated firm-level data easily and freely accessible to researchers in a timely manner, and for longer historical periods, to allow for a better understanding of Canadian international trade and investment patterns; continue to improve sectoral, geographic and historic details for foreign affiliate trade statistics; match employee-employer data to improve understanding of how trade affects workers and different parts of the wage and income distribution; encourage Transport Canada to work with Statistics Canada to collect more data on the investment and maintenance needs and performance of Canada's ports, airports, bridges and other border entry points.	De Backer and Miroudot; Lapham; Koldyk, Quinn and Evans; Roy; Van Assche

Notes

1. The state of global trade negotiations evolved during our work on this project. Each chapter was individually pre-released in order to highlight its findings, and it reflects the trade context as it was at the time of its release.
2. This result is distinct from, but not necessarily inconsistent with, Baldwin and Yan's results ("Global Value Chain Participation"), which found larger productivity gains for Canadian firms linking with GVCs in other advanced economies. Sui and Tapp analyze the sales and profit growth of all Canadian SMEs in all sectors exporting to emerging markets versus other market destinations. In contrast, Baldwin and Yan look at the productivity effects (not sales and profits) for only Canadian manufacturing firms (not all sectors) that are of all firm sizes (not only SMEs) and that are exporter-importers (not only exporters) with higher-wage versus lower-wage economies.