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Panel Remarks: Canada, United States and European Union – Out of Sync on Trade Agreements? Or Are We Sympatico?

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Panel Remarks: Canada, United States and European Union – Out of Sync on Trade Agreements? Or Are We Sympatico?

Erratum
article

PANEL REMARKS: CANADA, UNITED STATES, AND EUROPEAN UNION – OUT OF SYNC ON TRADE AGREEMENTS? OR ARE WE SYMPATICO?

Juscelino F. Colares[†]

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Thank you for being here and thank you to Steve Petras, Ted Parran, and Chios Carmody and Members of the Canada-United States Law Institute Board for helping us host such a great gathering.

Let me start by giving the audience a brief big picture of why this is a particularly perilous time for free trade. Then, I will transition to a few punctual trade issues where Canada and the United States can engage in cooperation to address current protectionist practices. Finally, I will conclude with a couple of comments about two very important trade issues in the bilateral relationship where we may not be as “trade sympatico”: the expiration of the Softwood Lumber Agreement (“SLA”) and the current status of the Trans-Pacific Partnership (“TPP”) in Congress.

I. ISSUE #1: THE BIG PICTURE – WHY ARE WE LIVING IN DANGEROUS TRADE TIMES?

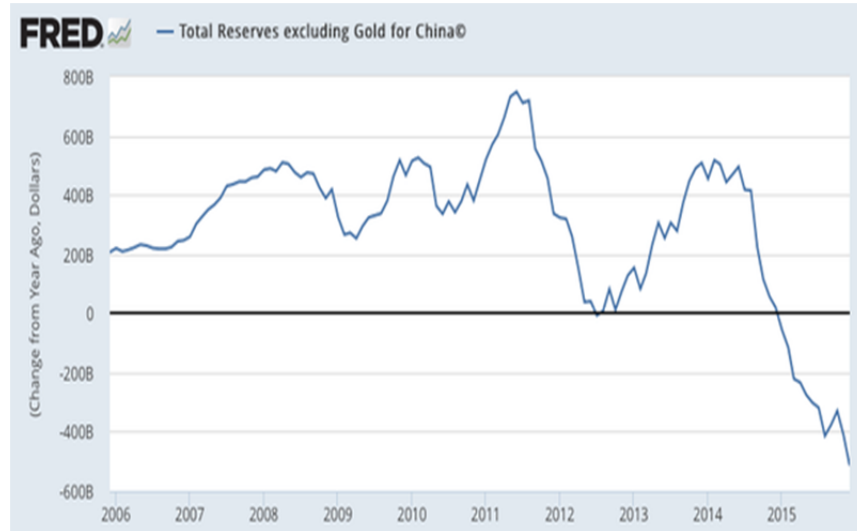
Since the economic slowdown that started in December, 2007 and the following Great Recession, the United States and its biggest trade partners (Canada, the European Union (“E.U.”), Japan, and China) have lived in a world awash with excess savings and inadequate demand. In this stagnant economic environment, interest rates in the Western world cannot fall any further to help boost investment and economic activity because rates are already near zero.

In other words, we are in a liquidity trap: without an increase in government spending, the private sector will keep on saving and waiting for a recovery in the *long* term, and the long term becomes longer as further economic retrenchment

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occurs. Thus, President Obama's first-term economic stimulus *helped* reduce the depth of the recession, but later budget sequesters and other forms of political budget brinkmanship damped the frail recovery. Abenomics, a mix of quantitative easing and massive spending in infrastructure, is having mixed results, getting Japan out of a two-decade long period of stagnation.

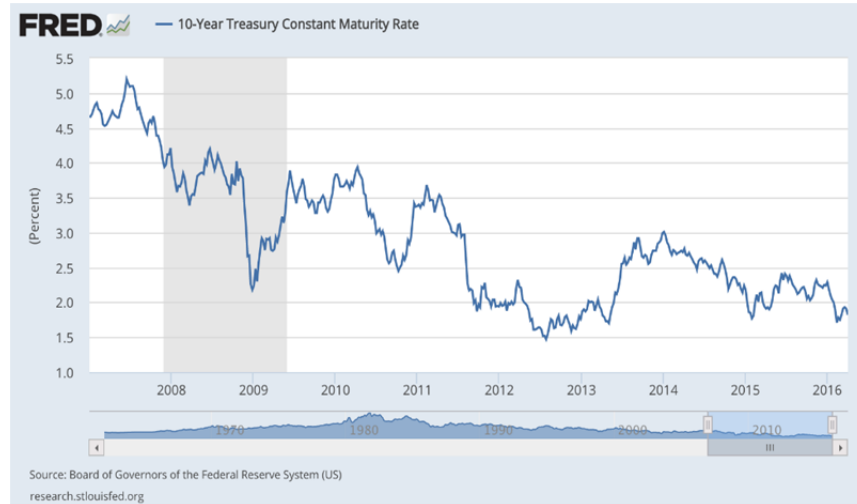
If you do not believe we are in a liquidity trap, remember the warnings about how the United States' "dependence on Chinese financing" through purchases of Treasury bonds would harm the United States once the Chinese stopped buying bonds? Well, the Chinese have been selling them for nearly a year and a half and not much has happened. Here is the annual rate of change in Chinese Foreign Reserves¹:



From the beginning of 2014 to the end of 2015, the Chinese Central Bank reduced total reserves (well over half of which are U.S. bonds) by about \$800 billion.² Yet, the sky is not falling:

¹ See *Total Reserves excluding Gold for China* © from 2006 onwards for the annual rate of change in Chinese foreign reserves, <https://fred.stlouisfed.org/series/TRESEGCNM052N>.

² See *10-Year Treasury Constant Maturity Rate* from 2008 onwards, <https://fred.stlouisfed.org/series/DGS10>.



U.S. interest rates on ten-year bonds are still below two percent,³ and it does not look like they are poised to rise anytime soon! But why am I pointing out this macroeconomic/finance data to you? I am a trade law professor. What do I know?

I am pointing this out, because, in a *normal* growth world, the negative employment effects of running a trade deficit tend to be offset, partially and, *possibly* totally, by greater capital inflows. Capital inflows reduce interest rates, which, as economists point out, boost economic activity and thus employment. Of course, a trade deficit can also eliminate some employment, but that impact is mostly distributional as other sectors benefit from cheaper availability of capital and investment and may hire more than otherwise.

Now, here is the big problem: this *balancing* effect of greater capital inflows that comes with trade deficits disappears when interest rates are already close to zero. As you recall, in such a world, rates can go no lower. So, in a *stagnant* macroeconomic environment, the following occurs: (i) trade deficits are bad for jobs because capital inflows provide little to zero relief; and (ii) every devaluation by traditionally export-growth-based countries is a hit on economic recovery. Specifically, most of the foreign capital that is coming into the United States does not get directly invested in the real economy. It is invested in government bonds and short-term deposits, investments that stay fallow if a government decides not to take advantage of near-zero interest rates. Arguably, this is because of an opposition-controlled Congress, hell-bent on fiscal austerity and/or willingness to sabotage economic recovery under President Obama.

³ *Id.*

Regardless, with continued capital inflows, the United States has seen its currency appreciate. Countries like China, Japan, and Brazil, all for different reasons, have had currency devaluations. So, in a world awash with liquidity and little investment, where capital inflows do not mitigate the loss of jobs through free trade, how can Canada and the United States ensure that they do not get taken advantage of? A partial answer can be found on my discussion of Issue #2, to which I now turn.

II. ISSUE #2: AREAS OF CONVERGENCE, THEREFORE EASIER COOPERATION

I would say that the starting point for a joint agenda should be a coordinated approach to ensuring that export-surplus countries do not succeed in gaming the system. Let us start with the following low-hanging fruit:

- (1) Canada, the United States and the E.U. should join forces in dealing with issues of overcapacity in steel and other basic industrial goods. Excess capacity in Asia is threatening jobs in North America and Western Europe at a time when popular dissatisfaction with trade is at its highest;
- (2) Canada and the United States must adopt a common approach to pressuring China and other countries to reduce Internet controls. The Great Chinese Firewall is a significant trade barrier to the world-beating Internet companies on both sides of the 46th parallel. Chinese internet regulations and their ostensible focus on blocking politically objectionable material is a façade: Canadian and U.S. suppliers of consumer and capital goods are being arbitrarily blocked from selling their products in China and other Southeast Asian countries. A recent New York Times article stated that *services* offered by Google, Facebook, and Twitter are blocked so that the opportunity for further business through these media is also being taken away. Worse, Home Depot pages, famous for marking what must be politically sensitive home improvement wares (said with sarcasm, of course), are swept under the Firewall as well.
- (3) Another big, present question is how Canada and the United States respond to China's self-described *graduation* from Non-Market Economy ("NME") status. Do you see the problem here? While the World Trade Organization Appellate Body has been busy eviscerating importing Members' Anti-Dumping remedies, with the effective destruction of the more import agency-deferential standard under Anti-Dumping Agreement, Article 17.5⁴ no doubt giving a big boost to trade-managing economies, China now wants to further its mercantilist policies by demanding market economy treatment? This, from a country where domestic prices are administered. Thus, whether it is steel overcapacity, internet-based trade barriers, or NME, Canada and the United States have a lot of work to do together. Now, on to the less *sympatico* part.

⁴ Agreement on the Implementation of Article VI of the General Agreement on Tariffs and Trade 1994 (Anti-Dumping Agreement), 1868 U.N.T.S. 201, art. 17.5.

III. ISSUE #3: TWO VERY IMPORTANT ISSUES: LUMBER AND THE TRANS-PACIFIC PARTNERSHIP

With the expiration of the SLA, the trade litigation peace period ends in October, 2016. Complicating factors such as inter-provincial differences and the U.S. industry's ability to file a case under U.S. trade statutes (if it deems its interests are not observed) should encourage all parties to, again, look for a balanced deal.

On TPP, Canada and the United States have much convergence and, in some usually complicated areas, reached a balanced deal. For instance, in dairy products, Canada preserved its "supply management" system while conceding greater market access. More recent news suggests that this compromise might unravel, so one ought to be cautious.

Trade diplomats from both countries seemed satisfied at the conclusion of the negotiations but, U.S. congressional resistance to a vote during the "lame duck" session and concerns over the investor-state dispute settlement ("ISDS") mechanism—national security, tobacco, and art and culture carveouts, notwithstanding—make it hard to predict what will happen after the election. Also, this will make it difficult to predict how other TPP countries might react to the enacting bill or statement of administrative action coming late this summer from the Executive Office of the President.

From the U.S. perspective, I believe, the United States Trade Representative must be interested in how the Canadian-E.U. Comprehensive Economic Trade Agreement is finalized. The United States is not comfortable with the European permanent court approach, and Canada finds itself now in an interesting spot.

As an academic, I am much more concerned with ISDS in TPP than with any eventual agreement with the EU under the Transatlantic Trade and Investment Partnership. To be clear, my biggest concern lies with weakening regulatory standards more than ISDS (although, concerns with the operation of the latter are also very important). Clearly, most TPP members have lower standards. That tends not to be the case with Canada. Of course, I still have major concerns with how adjudicators review cases under either *ad hoc* or permanent tribunal setups. Do they effectively apply the standards of review that they are required to? My own misgivings aside, finalizing an ISDS deal with countries that have lower regulatory stringency is a much more serious consideration than doing the same with Canada or the E.U.

I am sure the panelists and participants in this conference will be scoping out and giving careful thought about these issues. Hopefully, these discussions will contribute to greater trade convergence and coordinated action.