

Brexit: Is the trade agreement between Canada and the European Union under threat? There could be a new agreement between Canada and the United Kingdom

The United Kingdom's exit from the European Union is raising many concerns. In Canada, the impact could be particularly felt in the current process to ratify the Comprehensive Economic and Trade Agreement (CETA). For one, the United Kingdom's withdrawal process could shift the attention of European countries, pushing other files to the back burner, which could delay ratification of CETA. For another, some fear that CETA will become less attractive once the United Kingdom, Canada's largest trade partner in Europe, is no longer a party to the agreement. Yet even if additional delays could arise, public decision makers seem determined to move forward with ratifying the agreement. In addition, CETA will retain several benefits for Canada and will facilitate better geographic diversification of its international trade.

On June 23, Britons voted to leave the European Union (EU)—commonly referred to as Brexit. Even though the withdrawal will not be effective for several months or even years, the official exit process should be launched by the start of 2017. There will obviously be numerous consequences in Europe and around the world. Furthermore, there is a question as to what will happen to the Comprehensive Economic and Trade Agreement (CETA) that was recently concluded between the EU and Canada.¹

The ratification process is still underway; the official agreement text was released on July 5 in 23 official languages. Canada and EU members must now go through their respective internal processes to ratify and implement CETA.

THE PROCESS IS UNDERWAY

It should, however, be noted that the negotiation and ratification process was, and continues to be, longer and more difficult than initially expected. It must be said that it is an ambitious agreement covering trade in goods and services as well as many other aspects of trade between Canada and the EU. In addition, the number of stakeholders

is high, with 28 EU members² and the ten Canadian provinces, which were also involved in the process.

Yet many analysts fear that the CETA ratification process will now be hampered by Brexit. There is no doubt that the United Kingdom's exit³ will be the crux of other EU member country concerns in the coming months, while also pushing other topics to the back burner, which could give rise to additional delays in ratifying CETA.

That said, those responsible for the file have been rather reassuring on this front, on both the Canadian and European side. Canada's Minister of International Trade, Chrystia Freeland, recently spoke with her counterparts from Germany, France, Italy, the Netherlands and the United Kingdom, and they all reaffirmed their support of CETA. Moreover, the United Kingdom, which will remain a full member of the EU until the exit process is completed, assured Canada that it would support a fairly quick ratification of CETA. Ratification of CETA could also have strategic importance in the context of the United Kingdom's

¹ For more details on CETA, see our *Economic Viewpoint* published on April 22, 2015, www.desjardins.com/ressources/pdf/pv150422-e.pdf?resVer=1429702137000.

² Number of members in 2016, including the United Kingdom.

³ Once Britons invoke Article 50 of The Lisbon Treaty, it could take about two years (perhaps longer according to some sources) before finalizing the United Kingdom's official exit from the European Union.

exit from the EU. The British minister responsible for Brexit, David Davis, in fact mentioned that CETA could serve as a model for future negotiations between the United Kingdom and the EU to establish a free trade agreement between the two zones.

In addition, it is possible that CETA will partially come into effect. This would make it possible to put forward a large part of CETA's clauses fairly quickly (probably in 2017) while pursuing negotiations on more sensitive components.

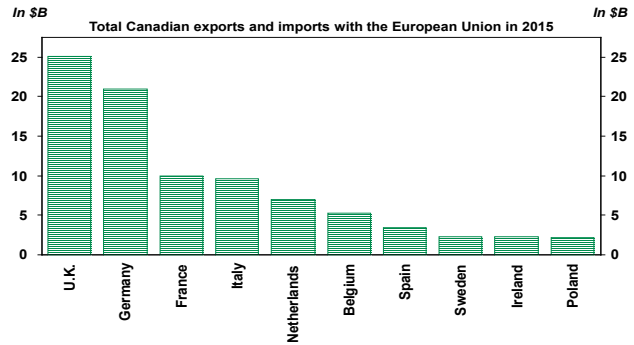
THE EU IS LESS ATTRACTIVE WITHOUT THE UNITED KINGDOM

Even though everything suggests that CETA should be ratified in a few months, there is a question as to whether this agreement is still beneficial for Canadians, considering that the United Kingdom will eventually be excluded from the agreement. The United Kingdom is Canada's largest trade partner in Europe, with a bilateral trade of goods totalling \$25.1B in 2015 (graph 1). On its own, the United Kingdom represents a little over 25% of all goods Canada trades with EU members. The United Kingdom is far ahead in terms of exports from Canada to the EU (graph 2), and is in second place in terms of Canadian imports from the EU (graph 3), just behind Germany.

However, a good portion of the United Kingdom's leadership position is due to transactions of a financial nature. Canada's main export to the United Kingdom is gold, valued at \$9.4B in 2015, representing 59% of all goods exported from Canada to the United Kingdom (see annex on page 3). Gold also leads for imports into Canada from the United Kingdom, with a value of \$1.4B in 2015, or 15.7% of all Canadian imports of goods from the United Kingdom. This trade is mainly due to the importance of the London Metal Exchange for international precious metal transactions.

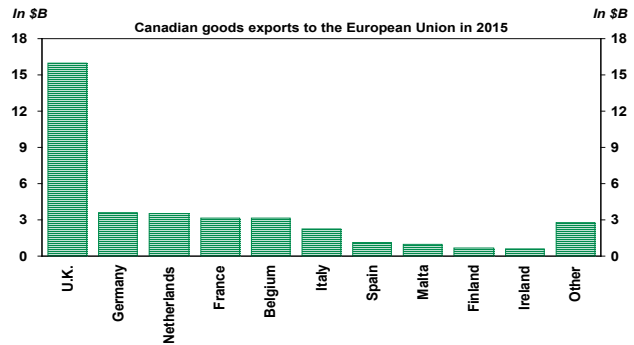
That said, several other European countries post a fairly high level of bilateral trade with Canada, including Germany, France, Italy, the Netherlands and Belgium. The presence of a trade agreement between Canada and the EU therefore remains completely beneficial in this context. In addition, even though trade with other EU countries is more modest, CETA will promote new trade opportunities with member countries. This could allow Canada to increase exchanges with other European countries and thereby improve the geographic diversification of its international trade. Under these conditions, even with Brexit, CETA remains beneficial. However, the extent of the economic benefits as estimated by the Canadian government and European authorities during preliminary discussions could be less given the exit of a major partner.

Graph 1 – The United Kingdom is Canada's principal trade partner in Europe



Sources: Industry Canada and Desjardins, Economic Studies

Graph 2 – The United Kingdom is the favourite destination for Canadian goods exports to the European Union



Sources: Industry Canada and Desjardins, Economic Studies

Graph 3 – The United Kingdom also has a big presence in Canadian imports from the European Union



Sources: Industry Canada and Desjardins, Economic Studies

TOWARD A NEW AGREEMENT BETWEEN CANADA AND THE UNITED KINGDOM?

It is also very likely that trade between Canada and the United Kingdom will continue at a sustained pace despite the latter's withdrawal from the EU and CETA. Trade relations between the two countries are well established, particularly in aeronautics. Under these conditions, it is even foreseeable that Canada and the United Kingdom will eventually negotiate a new bilateral trade agreement based on CETA fundamentals. It bears reminding that

relations between Canada and the United Kingdom already benefit from the presence of the Commonwealth, which promulgates cooperation within a framework founded on shared values and objectives.

Benoit P. Durocher
Senior Economist

ANNEX

Table 1 – The gold trade is a major factor in overall trade between Canada and the United Kingdom

Type of goods	Value in \$M	Relative size in %
Canada's main exports to the United Kingdom in 2015		
Gold (including gold plated with platinum) unwrought or in semi-manufactured forms, or in powder form	9,413	59.0
Nickel mattes, nickel oxide sinters/other products of nickel metallurgy	1,253	7.9
Waste and scrap of precious metal or of metal clad with precious metal	380	2.4
Radioactive chemical elements, radioactive isotopes or their compounds or residue	378	2.4
Petroleum oils and oils obtained from bituminous minerals	333	2.1
Aircraft, spacecraft/their launch vehicles	328	2.1
Parts of goods in the aeronautics sector	222	1.4
Fuel wood; wood chips; sawdust, scrap	191	1.2
Iron ores and concentrates	129	0.8
Wheat and meslin	124	0.8
Canada's main imports from the United Kingdom in 2015		
Gold (including gold plated with platinum) unwrought or in semi-manufactured forms, or in powder form	1,441	15.7
Parts of goods in the aeronautics sector	855	9.3
Motor cars/other motor vehicles for the transport of persons; racing cars	783	8.5
Turbo-jets, turbo-propellers and other gas turbines	546	5.9
Medicaments consisting of constituents which have been mixed together, not put up in measured doses	403	4.4
Petroleum oils and oils obtained from bituminous minerals	338	3.7
Undenatured ethyl alcohol (less than 80% vol); spirits, liqueurs and other spirituous beverages	222	2.4
Silver, unwrought or in semi-manufactured form, or in powder form	189	2.1
Human blood; prepared animal blood; serums, vaccines, toxins	169	1.8
Tractors	127	1.4

Sources: Industrie Canada and Desjardins, Economic Studies