

Canadian Policy Towards East Asia
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I appreciate this opportunity to appear before you. The focus on Canada's relationships with the East Asian economies is a timely and essential one, especially in the light of the foreign policy review. The review serves as a catalyst for long overdue policy debate across the country. My approach to our relationships with East Asia is focused and strategic. I believe that one of the outcomes of the foreign policy review should be to focus Canada's foreign policy resources, including our political, aid, trade and investment resources, on a smaller number of strategic relationships and issues and on becoming more expert and far seeing within this focus. My remarks will touch on three topics: the drivers of global economic change; Canada's East Asian focus; and what we should do about it. I draw in the third section on our studies of Canada and East Asia at the Rotman School of Management.

I have been an active participant in international affairs for nearly 40 years, beginning with a CUSO assignment in India, through university and NGO connections, and as Associate Deputy Minister of Finance in charge of international financial diplomacy. During much of the past decade, I have conducted research on the East Asian region and have co-directed with my colleague, Professor A.E. Safarian, a 7-volume series *The Hongkong and Shanghai Bank Canada Series on East Asia*, published by the University of Toronto Press. In recent years I have observed a decline in Canada's international relevance. Canada used to play a special role as an enlightened Western democracy, and as a close friend and friendly critic of our American neighbour. While Canada still is seen to stand for certain values, we have spread our resources too thinly, achieving little of anything as a result. Periodically, our elected leaders have sought to play a specialized or leadership role in international affairs. Time and again, however, they have lost

credibility because the initiative died when they either left office or were forced to divert their energies into federal provincial relations, the “black hole” of Canadian policy.

The drivers of global economic change

I do not need to remind the members of this Subcommittee how much the global environment has changed in the past 30 years. Most of my remarks will focus on deepening economic interdependence because I see economic change as a major driver of foreign policy. Deeper interdependence has changed the role of the nation state, creating new opportunities for international cooperation at the same time that the scope for autonomous action has declined. The United States, Canada’s closest neighbour, has emerged as the world’s only super power. The tragic events of September 11, however, drove home the realization that the openness that generates interdependence is also its greatest source of vulnerability.

East Asians were among the world’s early and natural “globalizers”, allowing market forces through trade and FDI to link their economies ever closer to each other, but also tying them closely into the world economy. Since 1989, when the ending of the cold war erased the divisions between the world’s two major economic systems, hungry new competitors from the transition economies entered world markets. Even so, East Asia has been a leading beneficiary of this economic openness as the following stylized facts attest:

- Some of world’s most rapid economic growth rates over the past 30 years have been found in East Asia, driving major income gains, major learning and economic transformation in these economies. Beginning with Japan.
- While trade within East Asia has increased, most economies remain very dependent on markets in the rest of the world. Japan is the most dependent. More than half its exports in 1998 went outside the region. The average for the East Asia-12, including Australia and New Zealand, was less than half (44.5 percent).
- Japan and South Korea are examples of graduation to the OECD club. Others are close behind. The Asian Development Bank estimates that Malaysia’s per capita income could reach 70 percent of the US average by 2025 (measured at current

exchange rates). China's could reach 38 percent of the US average by then – which is what Korea had achieved by 1990.

- Nowhere is this dynamism more in evidence today than in China. Following its accession to the WTO, a stock adjustment is taking place in FDI, making China the world's top recipient of FDI in 2002.
- World Bank data show that the number of people in East Asia living on less than a dollar a day fell from 418 million in 1987 to less than 280 million in 1998, after the Asian crisis. China's rapid growth has lifted many people above that desperately low subsistence figure.

It is also worth noting that United Nations demographic projections estimate, under their medium variant that 50 years from now Asians will account for 58.5 percent of the world's population.

How should Canada position itself in relation to this dynamic region? Being an optimist, I look ahead and see some key opportunities for Canadians to play international roles that could make a difference, both in the world and for Canadians. But to do so, I believe we should focus our foreign policy and invest in this focus, particularly in our human capital that understands the rest of the world, is able to anticipate long run trends, and assists in preparing Canadians for these trends.

I believe two relationships will be of critical importance during the next twenty-five years:

Canada's relationships with the United States and China. There will, of course, be other priorities driven by geography (Latin America), history (Europe) and security concerns (South Asia and North Korea), but these two should always top the list.

Canada's focus in East Asia

Today I will focus on China. I have spent much of the past decade studying the economic integration of the East Asian economies in collaboration with intellectual counterparts

throughout the region and as a participant in four international policy and research networks. East Asia's economic emergence in the past thirty years has been dramatic. But China's and the ASEAN economies' decision to negotiate a free-trade agreement is a powerful signal of a new era -- an East Asian community is being born. Whether it will be a set of hub and spoke relationships around China or a collective community remains to be seen. There will be a painful transition and many adjustments on both sides, but East Asians outside of Japan are shifting their angle of vision in dramatic ways. Unless major economic and political changes occur in Japan in the near future, it will be China, not Japan, who will emerge as Asia's economic and political leader. Canada has a unique standing in China, a standing we have invested in consistently over many years. In the future, it is very much in our interest to understand China's expanding regional role and its eventual impact on world order.

At the same time, a not-inconsiderable group in the United States is determined to see China's emergence as a threat to U.S. hegemony, and the likely focus of a future war. Relationships between Washington and Beijing may well set the tone for war or peace in the coming decades. Thus Canadian foreign policy should seek to lead initiatives and "set some tables" that help to shape the future of the Chinese-US relationship. Canada should invest in assisting the necessary bridge building to ensure that the outcome is a peaceful one. We should work with the Chinese on regional issues, and on participation and leadership in the multilateral institutions. We should make an effort to ensure American participation in such processes. We are one of the few countries that can do this -- both because of our historical friendship with the Chinese and because of current demographics. I'm told that as much as 40 percent of Canada's annual immigration now originates from Beijing and Shanghai, with many Chinese Canadians having feet in both worlds.

What should we do about our East Asian strategy?

In the early 1990s, Pacific 2000 supported a Canadian foreign policy initiative in Asia. This focus collapsed when priorities shifted, renewing somewhat and temporarily in 1997

around Canada's hosting of the APEC Summit. Team Canada expeditions also focused on Asia for a time, reflecting the particular importance in Asia of state-to-state contacts. Anyone who has worked with Asians knows the fundamental importance, not only of developing relationships, but more importantly of maintaining them. Canada has observed this principle in China and to a lesser degree in Japan, but not with respect to the region as a whole. It is not an exaggeration to say that Canada is invisible in the region. We have minimal policy clout and little perceptible business presence to show for the Team Canada expenditures.

While it is not too late to try to restore Canadian profile, *we should not do so unless we are willing to make a permanent commitment of official resources*. If we are willing to make such a commitment, our strategy should have three pillars:

1. Build human capital

Financial support for the study of international economics and international relations has not been a centerpiece of foreign policy. It should be. The Association of Universities and Colleges of Canada has expressed concern about the lack of a coordinated national strategy for international studies. Under the status quo, our international aid program has become the major source of ongoing funding for international centers and universities, forcing them into narrow and shifting criteria and making unrealistically onerous administrative requirements upon them. Beyond that, ad hoc public investments, like gunshot, are made in a variety of institutions and foundations that serve passing political fancies. Do any of these institutions stand out as resources of leading international caliber, producing clear strategic analysis and advice that is influential within Canada and beyond?

I believe financial support should be re-focused and significantly increased to enable Canadians to invest in building deeper international relationships and expertise. Such a strategy is quite feasible, as other national examples attest. The Australian approach to research funding is one example. They obtain much better mileage, quality and policy relevance out of their government-academic connections than we do. In the United

States, Title VI of the US National Defense Act of 1958 has been the lifeline of international education in the United States for the past forty-five years. It finances 115 centers; its grants are matched by non-federal government funds and by foundations and corporations, thereby providing invaluable leverage to the best institutions. Thanks to Title VI, thousands of knowledgeable Americans have international expertise and contacts that they would not otherwise have.

I recommend serious consideration be given to restructuring funding mechanisms to create a competitive approach to funding university departments and interdisciplinary centers on the basis of periodic competitions in which proposals are evaluated in terms of the excellence (and relevance) of strategy, outputs and the efficiency of production and dissemination.

2. More focused business facilitation

I have suggested several initiatives over the years. Most recently, I proposed that Canada and Japan negotiate a free trade agreement. Repeatedly however, public servants and politicians have told me that public initiatives would be taken if there were “pressure from the private sector”. Based on my analysis of business ties with the region, this excuse is not a valid one because there is evidence of market failure, and therefore a case for a more proactive public sector role.

Between 1995 and 2002, the Institute for International Business led an intellectual enquiry into major aspects of Canada’s economic relationship with East Asia, sponsored by the Hongkong and Shanghai Bank Canada. At the outset, we commissioned Professors Head and Ries at UBC to bench mark our trade and investment ties and what to do about them. At the time there was much talk about Canada “missing the boat”. Miraculous growth rates implied higher potential returns than elsewhere. Canada’s relatively weak performance must be due to barriers to entry due to distance and lack of familiarity with the economies relative to the United States. Seven years later, we commissioned a followup study. The Canadian business presence is still small when bench marked against ten other OECD economies. But this time Head and Ries found that Canada’s export

performance in food, wood and metal products was better than the comparator group. They also found that Canadian businesses were most successful in Japan, China and Indonesia. But in all products and markets we were outstripped by the Australians.

Canada, as a latecomer to Asian markets, is unlikely to dramatically improve its performance in the future. My recommendation, therefore, is that we should build on our successes. We should focus over the long term on the three largest economies, where we have established sustainable relationships. Of these three, China has the best long run prospects and has our strongest beachhead because of our history.

3. Play a facilitating role

Canada as a middle power (and a shrinking one in relative terms) has a key role to play because of its geography and its history. I believe we should become more active in a focused way. Senior scholars and analysts of international economics and international relations in other major countries frequently comment to me about their hopes that Canada will return to its role (*which third countries cherish*) as an honest broker and an influential voice with Americans. This role is more important than ever given the newly assertive U.S. role in the world.

I recommend a “cluster” approach. We should invest in more focus geographically, in business facilitation, and in attaining greater depth in our human capital (language training, education in international economics, business and international relations, and centres of excellence in our universities). These investments in expertise in the major economies *and in the region overall* are essential if Canadians wish to play more influential roles in APEC and in major developments that will affect our interests, including the emerging regional trade and financial institutions and in promoting a positive-sum US-Chinese relationship, the overarching challenge of the next two decades.