

DIVERSIFICATION NOT DEPENDENCE

A MADE-IN-CANADA
CHINA STRATEGY

OCTOBER 2018





ABOUT PPF

Good Policy. Better Canada. The Public Policy Forum builds bridges among diverse participants in the policy-making process and gives them a platform to examine issues, offer new perspectives and feed fresh ideas into critical policy discussions. We believe good policy is essential to making a better Canada—a country that’s cohesive, prosperous and secure. We contribute by:

- Conducting research on key issues
- Convening candid dialogues on research subjects
- Recognizing exceptional policy leaders

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INTRODUCTION

By **Edward Greenspon and Kevin Lynch**, Co-chairs, PPF Consultative Forum on China



Over the past 18 months, the Public Policy Forum's Consultative Forum on China has collaborated with business executives, government officials, security experts, environmentalists, Sinologists, human rights proponents, labour leaders, Indigenous business representatives and former prime ministers and cabinet ministers, among others, to identify how to best represent Canada's national interests in relation to China. Co-chaired by the two of us, the Consultative Forum sought a course that would be economically beneficial, politically acceptable, and reflect the interests and values of a nation seeking new sources of growth and jobs amid a rocky relationship with our closest partner and a changing global environment.

After much discussion, we settled on a set of recommendations built off the foundation of sectoral agreements, rather than comprehensive free trade, as the best means for realizing quick and significant gains. A sectoral approach also provides the benefit of creating a pathway to a more diversified and growing trade

portfolio for Canada that does not run afoul of the virtual veto given to our North American trading partners in the new United States-Mexico-Canada Agreement (USMCA).

The members and guests of the Consultative Forum shared a steadfast belief that Canadians should never shy away from a genuine dialogue, wherever it may go. This has not always been the case when it comes to Canada's relations with China. There is often a chill in the air. The Consultative Forum sessions were characterized by tough and candid conversations as we worked our way toward solutions. On many points, we found convergence, while on several others—particularly our sectoral trade approach—a minority felt we were not being sufficiently ambitious. We were all struck by the bifurcated national conversation on China and the absence of progress on trade diversification with the fastest-growing region in the world.

The recommendations in this report are the responsibility of the Public Policy Forum (PPF) and are based in whole or in part on the input and insights offered by the participants in the Consultative Forum. We thank everyone for the extreme generosity of their time and their abiding com-

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mitment to the concept that good policy makes a better Canada. We particularly want to thank the PPF team that worked on what was a complex undertaking policy-wise and logistically: Jane Hooker, Director of Research; Zac DeLong, Policy Lead; Anna Jahn, Director of Membership and Partnership; research assistants Andrée Loucks and Gabrielle Feldmann; Director of Communications Carl Neustaedter and his team, Naushin Ahmed and Tomek Sysak; and our events planning and finance teams. We are also grateful to former diplomats Colin Robertson and PPF Fellow Drew Fagan for their input on the manuscript.

Edward Greenspon, President and CEO,
Public Policy Forum

Kevin Lynch, Vice Chairman of BMO Financial Group,
former Clerk of the Privy Council

CANADA AND CHINA: THE WAY FORWARD

In the summer of 2018, China’s middle-class parents rose up against the use of low-quality vaccines to inoculate their children against diphtheria, tetanus and whooping cough. They took to the social media platforms WeChat and Weibo and picketed government buildings to express their outrage over yet another Chinese health scandal. President Xi Jinping responded by agreeing the vaccine scare was “vile and shocking” and vowing to get to the bottom of it.¹ Authorities detained groups of executives amidst a criminal investigation and government inquiry.

There was a message in all this for Canada. The incident served as a reminder that China is home to hundreds of millions of newly minted members of the middle class who harbour heightened expectations for everything from safe products and livable cities to transparent financial markets and secure retirements. They have not hesitated to lay down demands, such as addressing air pollution in large cities. This middle class is unevenly distributed among geographically richer and poorer regions, raising issues familiar to Canadians concerning inter-regional transfers and equalization. Interestingly, at this point in its development, China needs more of what Canada knows: how to manage the demands of a middle-class, consumer-driven society increasingly attuned to quality of life issues. “China is at an historic juncture. After decades of high-speed growth, the government is now focusing on high-quality growth,” the International Monetary Fund (IMF) recently stated.¹ This plays to Canada’s strengths.

While China is Canada’s second largest export destination,² it still represents less than one-fifteenth of our exports to the U.S. market.³ Half of G20 countries sell more to China than Canada does, including South Africa, Brazil, Saudi Arabia and Indonesia. There is plenty of room for growth—and a need for it. Our people-to-people ties are in better shape. With 682,000 visits in 2017, China has displaced the United Kingdom from its perch as the second largest source of Canadian tourists. Family visits, business meetings and conferences now make up more and more of the total.⁴ About 30 percent of all international students studying at Canadian post-secondary institutions are from China,⁵ providing a critical financial boost that allows educational institutions to employ more faculty and build better facilities.

All Canadians benefit from these increased linkages and the money they pour into local economies across the country. Tourism in particular benefits



SHOPPERS IN CHENGDU, SICHUAN, CHINA

Using any measure, Asia can't be ignored. By 2030, it will account for half the world's population, more than 50 percent of the world's GDP and 65 percent of the global middle class, the Asia Pacific Foundation of Canada projects.

more remote regions of the country, where jobs are often hard to come by.

Using any measure, Asia can't be ignored. By 2030, it will account for half the world's population, more than 50 percent of the world's GDP and 65 percent of the global middle class, the Asia Pacific Foundation of Canada projects.⁶ If it continues on its current trajectory, Asia's per capita income will more than double by 2030 to stand at 60 percent of Europe's levels today, catapulting another 2.6 billion people into the middle class. With a total of 3.2 billion people, Asia's middle class will account for more than 40 percent of global middle-class consumption.⁷

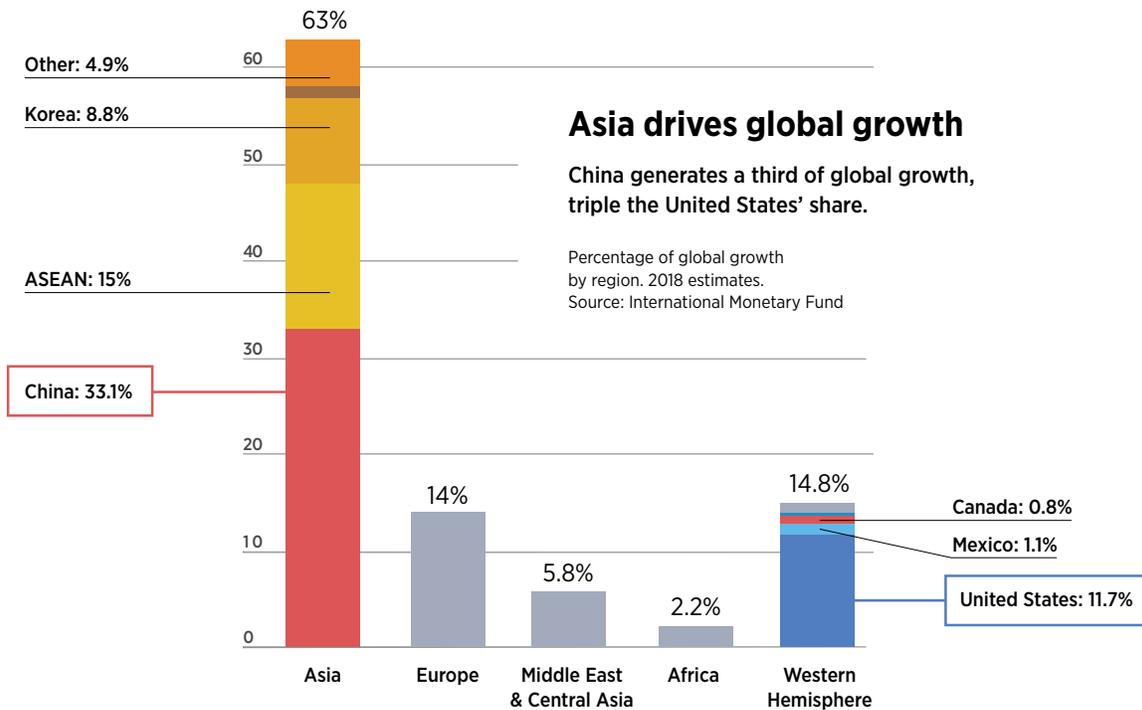
And within Asia, China can't be ignored. By 2030, China will be the world's biggest exporter of capital, goods and services; the largest emitter of greenhouse gases and producer of clean energy solutions; a technology superstar; a serious global military power; an aspiring Arctic player; and the world's top source of tourists and international students. China already vastly outspends the United States on state-of-the-art domestic infrastruc-

ture, and its economy is growing at least twice as fast as most Western nations.⁸

In 2000, China was responsible for a mere four percent of the global economy and the U.S. a dominant 31 percent.⁹ Today, China accounts for 15 percent and the U.S. 24 percent.¹⁰ Those numbers are forecast to converge in a decade or so, after which China will surpass the U.S. as the world's largest economy. According to the IMF, China alone accounted for 33 percent of global growth in 2017, outstripping all the rest of Asia (28.8 percent), as well as Europe (15.2 percent) and the Western Hemisphere countries (12.8 percent), including the U.S., combined.¹¹ Even with stronger U.S. growth this year, China's one-third share of world growth is holding steady.

China's extraordinary resurrection as a dominant power with global reach and ambition turns the presumptions of 20th-century international relations on their head and creates new risks and new opportunities for other nations. China blends elements of capitalism and authoritarianism in a manner never before seen. This presents unique chal-

The question is not whether countries like Canada need a China strategy; it is what such a strategy should look like.



allenges for policy-makers in liberal democracies to come up with responses that both serve their national interests and further the common cause of a peaceful, prosperous and predictable world.

The USMCA appears to render some options particularly risky with its provision that any two of the parties may terminate the agreement should one of them enter into a free trade agreement with a non-market economy. While this may well prove an unprecedented ceding of sovereignty, an immediate move to a free trade agreement with China was not what the Consultative Forum had in mind, in any case. For a variety of reasons explained below, including the probable provocation that negotiating a comprehensive free trade agreement

with China would cause to the United States, we opted for a more measured and attainable sectoral approach. We believe sectoral agreements do not offend the USMCA's new Clause 32.10, which appears directed at the kind of free trade agreement that in World Trade Organization (WTO) terminology would cover "substantially all trade."

Our traditional partners in the world are also trying to figure out how to balance the benefits of closer Chinese economic and diplomatic relations with growing concerns over state-owned and -directed enterprises, human rights, labour standards and the like. Arguably, Canada travels a more challenging road than most with the dual imperatives to diversify our global economic relations

and to preserve secure access to the American marketplace.

Despite recent tensions, China and the U.S. remain large trade and investment partners and, at the same time, growing strategic competitors. The rivalry between the dominant nation-state of the 20th century and the challenger to its throne in the 21st century poses perhaps the greatest geopolitical risk of our time. Harvard University political scientist Graham Allison has observed that of 16 major power shifts over the past 500 years, 12 have resulted in war. But three of the four exceptions—including the U.S. supplanting Great Britain as a Great Power and the Soviet challenge to U.S. dominance—occurred in the 20th century. “Despite moments when a violent clash seemed certain, a surge of strategic imagination helped both sides develop ways to compete without a catastrophic conflict,” he wrote in June 2017.¹² Engagement—often in the form of agreements on how to manage disagreements, such as the Cold War’s arms control treaties—is safer than isolation, Allison argued. In China’s case, this might involve negotiated limits on cyberattacks or surveillance operations, creating greater space for co-operation on common challenges like terrorism or climate change. According to Allison, “leaders should understand that survival depends on caution, communication, constraints, compromise, and cooperation.”¹³

By dint of geography, history, security, culture and economics, Canada’s relationship with the U.S. will remain its most important. But it is a relationship in flux and, both despite and because of the USMCA, where this relationship is headed in the long term is uncertain at best. The current U.S. administration treats allies and foes alike when it comes to its mercantilist trade instincts. Canada has an interest in its own welfare and, as in the Cold War, in doing what it can to contribute to open lines of communication between great powers.

This complexity means that Canada must factor U.S. realities into its calculations without becoming paralyzed by them. Pursuing our national interests demands a careful balancing act between sustaining access to the North American marketplace while developing a made-in-Canada strategy for trade diversification. This cannot succeed unless it includes China and the Asian region it leads. In the current ‘Make America Great Again’ climate, the long-held goal of diversifying our international portfolio of relationships has become even more vital as it has become more vexing. A North American trade agreement that gives away diversification flexibility for more assured access to our largest market speaks eloquently to the honey trap our dependence puts us in. Without a determined plan of diversification, Canada will stifle its growth and influence on the world, and perpetuate the



Canada's exports to China in 2017:

\$23.6 billion

4.3% of all exports

2nd largest
export destination

Percentage of total U.S.
exports that went to China
in 2017:

8.4%

very course that has led it to be so dependent on a single trading partner.

But there is still room to maneuver. In 2017, Canada exported \$546.6 billion worth of merchandise, with \$23.6 billion (4.3 percent of total exports) of those exports destined for China, its second largest export destination. As our largest trading partner accentuates its strategic rivalry with Chi-

na, there are indications that Canada has some breathing room when it comes to growing its trade. In 2017, 8.4 percent of U.S. goods exports went to China,¹⁴ almost double the proportion of Canadian goods exported to China.¹⁵ If Canada were simply to reach U.S. proportions of exports to China, that would translate to \$23.6 billion in new exports.¹⁶ Doubling Canada's current levels of exports to China would produce gains greater than



our current sales to Japan, India and South Korea combined,¹⁷ marking a good, yet hardly provocative, start down the diversification road.¹⁸

Canada has talked trade diversification for some time, but actual progress has been halting. Recently, we've made headway with the Comprehensive Economic and Trade Agreement (CETA) with the European Union (EU) and with the Comprehensive and Progressive Trans Pacific Partnership (CPTPP). But trade agreements are means, not ends. Both government and business need to focus on execution to deliver on the growth, jobs and higher incomes that flow from increased trade. While a step forward, the CPTPP suffers from the exclusion

of Asia's two biggest economies, China and India. Despite strong growth in absolute trade numbers with China since 2000, especially when compared with the U.S.,¹⁹ Canada's market share has fallen by about 25 percent since 1995.²⁰ This is a strong reminder that an absence of policy is not a safe harbour, but carries its own consequences.

Meanwhile, despite the new USMCA, the extent of our reliance on a single market and the threats of more U.S. protectionist measures ratchets up the urgency to accomplish more, and soon. Our over-dependence on the U.S. is shown by a simple comparison of Canada's export profile to that of the United Kingdom. Three-quarters of

Canadian merchandise goods go to the U.S. and only 25 percent find their way to the rest of the world.²¹ In the U.K., just under 50 percent of merchandise goods go to the EU, which is roughly the same economic size as the U.S.²²

Canada's excessive reliance on a single market was something it could get away with when that market represented the great global engine of growth. For many decades, the U.S. soaked up our exports—from crude to cars—and accorded us special status. But our special status has been fading for several years. Even before the current U.S. administration's specious national security attacks on

coming to grips with a nation of 1.3 billion at the heart of the world's fastest-growing region.

It is also clear that while Canada is a trading nation, it is not a nation of traders. Our business structure tends toward enterprises that are either small and domestically focused or foreign-controlled and U.S.-oriented. Little more than 10 percent of Canadian small and medium-sized businesses (1-499 employees) export at all, and only 10-12 percent of those export to faster growing economies in Asia and Latin America.²³ Given that small and medium-sized enterprises (SMEs) account for the vast majority of Canadian business-

Given that small and medium-sized enterprises account for the vast majority of Canadian businesses, no export expansion strategy can succeed—economically or politically—without them.

our exports and roughhouse tactics over NAFTA, President Barack Obama rejected the Keystone pipeline and insisted Canada bear all the costs of a new border crossing at Windsor. Precisely where American foreign and trade policy is headed in the long term remains to be seen. What is clear now is that diversification must be a core element of Canadian policy going forward, and that there can be no meaningful diversification strategy without

es, no export expansion strategy can succeed—economically or politically—without them. Nor can any trade agreement aspire to being inclusive without including SMEs. The recent addition of the words “Export Promotion” to the federal government's Small Business portfolio must be followed up with concrete policies and programs.

Medium-sized enterprises (100-499 employees) may be the place to start, given that they already

export at nearly double the rate of their smaller cousins.²⁴ To some extent, the answers lie in ensuring they have the means and knowledge to sell abroad and that potential purchasers have an easier time finding them. Internet sales platforms such as Alibaba, which opened a Vancouver office in the summer of 2018, provide opportunities to reach foreign markets more easily. So would the creation of international sectoral marketing groups or the addition of more direct flights to additional Canadian destinations, as well as the streamlining of passenger movements through airports. Another part of the answer requires domestic action: for instance, internal trade barriers hobble the ability of SMEs to scale up domestically, a prerequisite to selling further afield. If the government acted on a goal of having SMEs increase their exports by 50 percent over five years, with special attention to fast-growing markets, that could mean an extra \$50 billion or so of export activity.²⁵

For that to happen requires not just liberalizing trade, but also investment. Close to half of Canadian trade with the U.S. occurs within companies, a reflection of the integrated supply chains that move goods back and forth in the manufacture of products. In advanced economies, trade is inextricably linked with investment, so two-way foreign direct investment, with transparent rules consistently applied and national security accounted for, must be an essential part of the Canada-China

trade equation.

After 18 months of study and debate, the Consultative Forum on China's clear determination is that the path to continued Canadian prosperity and influence in the world cannot be assured without deepening Canada's engagement with China through a more modern set of rules governing our relations. PPF initiated the Consultative Forum because of a sense the public dialogue in Canada, in contrast to many of our allies, had fallen into a simplistic dichotomy of human rights versus free trade. Both of these are critical factors, yet relations between nations exist on multiple levels among myriad players and demand to be drawn on a broad canvas of issues.

Even the most cautious members and guests of the Consultative Forum felt that, given how China is reshaping the world in the 21st century, a new made-in-Canada engagement strategy is necessary. The deliberations turned on the details, especially around security, human rights and the best way to expand trade substantively and rapidly given our real and present trade diversification imperative.

Three overriding principles in furthering Canadian interests stood out:

- Canada is always best served by systems of rules, both bilateral and multilateral, rather

than being subject to arbitrary or ad hoc measures. Rules matter most when we are the smaller party in a relationship.

- The U.S. is no longer the sole driver of the world economy nor is it the reliable partner it was. This necessitates an aggressive strategy of purposeful diversification, despite the USMCA. If we are going to continue to prosper, we simply need to sell more goods and services to more places, with more Canadian companies engaging actively in international trade. Canada must aspire to be not only a great trading nation, but a nation full of traders.
- Canada can only provide the rising incomes, rewarding jobs and expanding market opportunities familiar to past generations by trading more with economies that are growing faster than our own and are big enough to make a material economic impact. Trading with slow-growth economies will not do the trick. For the most part, fast-growing economies with scale are to be found in Asia, most particularly China.

Much has changed in the three short years since the Liberal government of Justin Trudeau came to power. China has defied its doubters by continuing its impressive economic growth while further centralizing political control in the hands of the Communist Party and its leader, Xi Jinping. It is shifting its economy from an export base to a consumer base and has opened more sectors to imports and investment. In the wake of scandals, it has also lowered non-tariff barriers on pharmaceuticals. It is spending heavily on education and advanced industries such as robotics, artificial intelligence and

data analytics, aerospace and electric vehicles.

It has also sharply turned its attention to improving environmental conditions at home and, in the wake of the Paris Climate Agreement, has become a champion of the transition toward a low-carbon future. In 2012, the Communist Party of China included the goal of achieving 'ecological civilization' in its constitution. With serious smog and water quality issues,²⁶ domestic political pressure to shift away from coal and significant investment in wind and solar power,²⁷ China is a natural partner for Canada in pursuing its global climate change and sustainability interests.

At the same time, the U.S. administration is redefining its relationship with the global, rules-based trading system it conceived. It has pulled out of the Paris Climate Agreement and the CPTPP and is sowing uncertainty with attacks on stalwart institutions such as the WTO, the IMF and the North Atlantic Treaty Organization (NATO). It is pushing hard for bilateral over multilateral trade arrangements, geared to manage free trade within a hub-and-spoke system centered on the U.S. This has led it to penalize such critical Canadian industries as softwood lumber, pulp and paper, steel, aluminum and potentially automobiles, despite their long-standing integration into the U.S. economy.

As a mid-sized geopolitical player, Canada worked tirelessly to make itself a major author of the

post-Second World War system of international institutions built on predictable rules and mutual interests. With the old order rapidly changing, the time has come again for us to shape our destiny by finally diversifying our economic and, by extension, political relations.

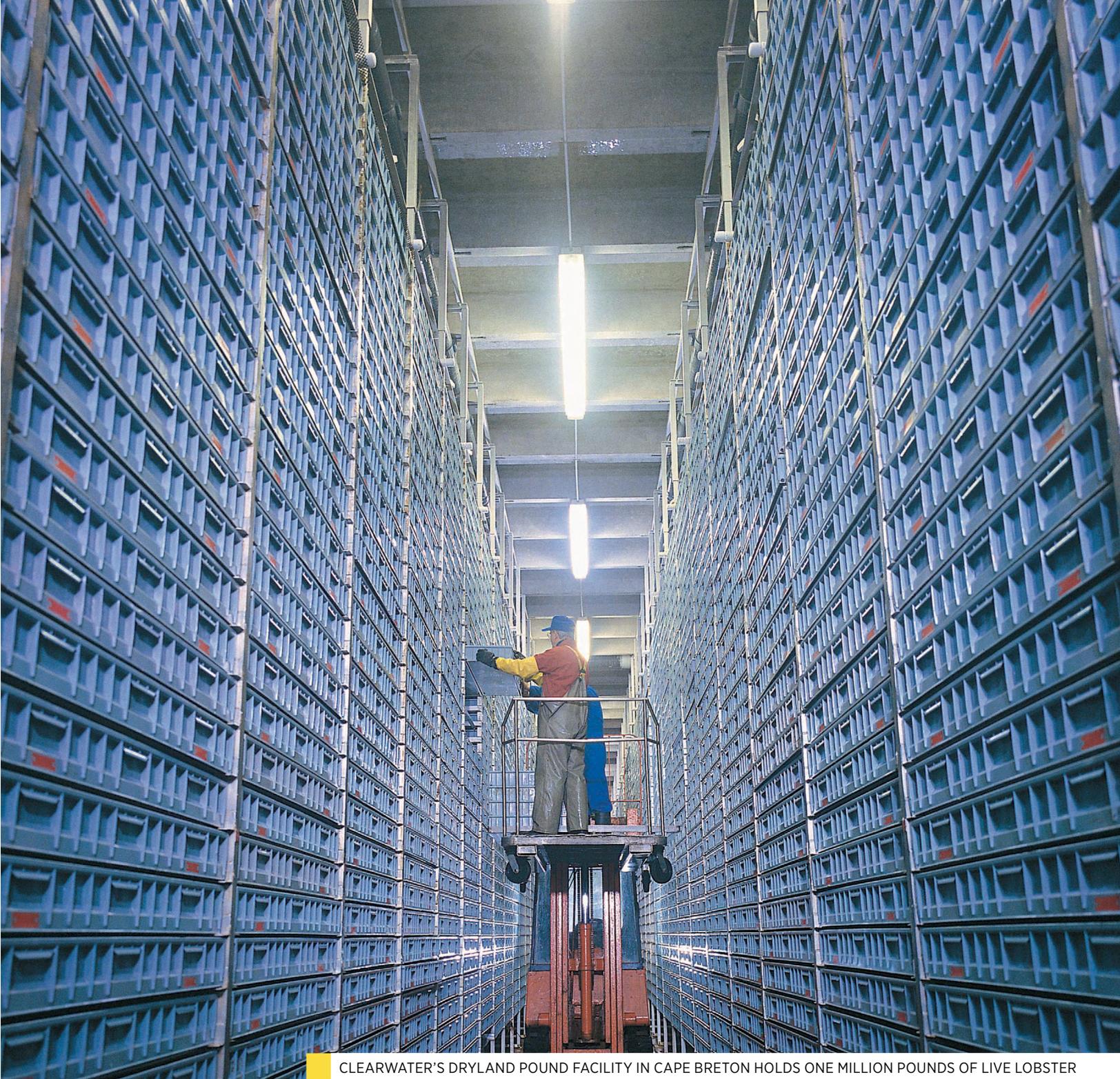
The choice is simple: chart a course through a clear, long-term Canadian strategy or be on the receiving end of others' ad hoc decisions.

As will be shown in the next section of this report, Canadian public opinion, though not fully formed, tends to be pragmatic on China. Canadians accept there are pluses and minuses to the relationship and seek balance over absolutes. Support for a free trade agreement has been rising steadily in the face of the dynamic Chinese economy and a less reliable U.S. There are misgivings, to be sure, especially when it comes to transgressions of human rights and the potential behaviours of Chinese state-owned and -directed enterprises in market economies. Conversely, support exists for international cooperation between Canada and China on issues such as the environment, reflecting a persistent belief that more engagement is better than less. In fact, Canadians view increased trade as the best driver of human rights improvements.

Agreeing with Canadians and Harvard's Prof. Allison, PPF's Consultative Forum on China felt en-

gagement, not retrenchment, was the preferred way forward for Canada-China relations. We have focused on what best serves Canada's interests rather than being overwhelmed by what China—or the U.S., for that matter—may or may not want. Before entering any negotiation, Canada must first decide what it wants and then pursue its objectives vigorously. We should resist the very Canadian notion that we couldn't possibly have anything of value to offer China. If that is so, let's leave it to the Chinese, not us, to say. Leaders in the public, private and other sectors must be prepared to engage in candid conversations with the Canadian public. That means business groups learning more about China and CEOs putting their capital—financial and political—where they believe their futures lie. From a government lens, unless China is on the cabinet priority list, in ministerial mandate letters, in the Speech from the Throne, on the federal-provincial-territorial agenda, in the speeches of the prime minister and premiers, and at party policy conferences and public town halls, we are not going to make real progress. It is time to put meat on the bones of the recent addition of 'Diversification' to the title 'Minister of International Trade Diversification.

Canada and China share concern over any regression of the global trade system. A window of opportunity exists to tackle some of the normal challenges of refreshing relations. This process is



CLEARWATER'S DRYLAND POUND FACILITY IN CAPE BRETON HOLDS ONE MILLION POUNDS OF LIVE LOBSTER

Clearwater Seafoods Inc. has created 509 direct jobs in Atlantic Canada. These would not exist without the Chinese market. The LNG plant in B.C. is expected to generate 20,000 jobs.

eased by the important complementarities between the two countries. China is highly attuned to ensuring security of supply through diversification of its import sources, just as Canada is increasingly focused on security of demand for its exports. Therein lies the potential for significant mutual benefit. In a recent example, China signaled concern about the security of its liquefied natural gas (LNG) imports from the U.S.,²⁸ while British Columbia is renewing efforts to develop its LNG potential with the recent announcement of a \$40 billion investment by Shell and partners.²⁹

None of this is esoteric. The LNG plant near Kitimat, B.C. and on the traditional territory of the Haisla Nation is expected to generate 20,000 jobs, as well as taxes and royalties for governments.³⁰ On the East Coast, the ability of Clearwater Seafoods Inc. to penetrate China's market is instructive; so far it has created 509 direct jobs in Atlantic Canada at its processing facilities, in its fishing fleet and at its head office, according to the company. These would not exist without the Chinese market. Elected officials should take note that a high share of new trade-related jobs, particularly in the resource and tourism industries, can be found in hard-pressed smaller centres and remote regions.

While we submit in this report that it's best for Canada to proceed confidently, we do so in the understanding of the need to, as has often been said, keep our eyes wide open, whether looking south or across the Pacific. We cannot afford to be blinkered to the ways in which the world is developing, nor be anything but clear-eyed that China is unlike other major countries with which we are accustomed to dealing. It is not a like-minded democracy, nor, as the 19th Party Congress in October 2017 demonstrated, does it aspire to be one. Moreover, the Communist Party's hand in the marketplace and within diaspora communities is all too visible, giving rise to concerns ranging from unfair competition to extra-territorial interference. And it is backsliding on human rights, particularly regarding minorities such as the Uyghurs. As an influential G7 and G20 nation, Canada will need to manage these issues through bilateral and multilateral means, and neither shy away from them nor succumb to the politics of the moment over the potential of the long term. In times of profound global change, the test of leadership often comes in the will and ability to chart new and sustained courses in a manner that the public recognizes as furthering its interests. Those times are upon us.

RECOMMENDATIONS



'The Way Forward' formulation proposed by the Consultative Forum on China furnishes a fresh, measured and optimistic made-in-Canada strategy for future relations with the world's new mega-power. This is not a buffet table of policies, but a series of interrelated recommendations for achieving economic and geo-political gains for Canadians without sacrificing principle. To pick here and there would be to deny the necessary integration of measures that make for a strategy rather than merely a series of one-off actions. With that in mind, we recommend that Canada:

1. (a) Begin now with targeted sectoral agreements. The successful realization of several sectoral arrangements would allow both parties to benefit and build confidence, knowledge and momentum while acting to liberalize trade and smooth the movement of goods and services in areas of mutual interest. We note that before free trade with the U.S., there existed a long-standing auto pact, which proved a confidence builder. A sectoral formulation offers a

model for diversifying more rapidly, getting wins on the board, building capacity and avoiding the risk of attempting to leap before we can walk. WTO rules require broad trade agreements, covering "substantially all trade" before tariffs can be reduced on a bilateral basis. Even with the new USMCA constraints on the evolution of a free trade agreement, there are persuasive arguments from trade experts that a less sweeping economic partnership arrangement—covering

sectors, mutual recognition of certification, mechanisms to ward off or mediate disputes and identification of areas of international cooperation – would facilitate trade. In the meantime, China has been lowering a number of tariffs for supply chain reasons and opening new areas of the economy to foreign investment. Our sectoral approach is both in keeping with the recommendations of the Trudeau government’s Economic Growth Council and leans on work undertaken by the Harper government in identifying where Canada and China’s strengths and weaknesses are complementary. In time, it should serve as a precursor to a comprehensive free trade pact, but much may depend on the course of the new USMCA and, ultimately, whether the U.S. chooses to invoke Clause 32.10.

(b) Start with agri-food and natural

resources. Among the sectors meriting early consideration are agri-food (including fisheries), forestry, natural resources, insurance and wealth management, cleantech, life sciences, engineering services, tourism, education and research. Since sectoral agreements would have to be phased, we recommend starting with agri-food and natural resources, where complementarity is beyond doubt and quick gains can be recorded, followed closely by education and tourism services, before moving as rapidly as possible to the other sectors. We would also look for agreements around ‘enabling’ sectors, such as e-commerce and aviation.

This approach would:

- Create momentum through early and concrete progress, in contrast to a likely five- to 10-year free trade negotiation that would stretch over several governments and economic cycles, if such a comprehensive approach is even still feasible. (For instance, the CETA agreement

with the EU took eight years.) We believe an ‘all or nothing’ design would tilt toward failure, not success. For two nations that have both benefitted from the international trading system, a fast start on sectoral trade would also send a positive liberalizing message at a time of attacks on free trade principles.

- Forestall the highly sensitive issues of technology transfer and national security while Canada rethinks its regime. Selling lobsters, filling hotel rooms, shipping timber or oil and gas and reaching consumers via the internet don’t pose direct security threats to Canada or our allies.
- Build greater business support by having industry leaders from these initial sectors actively engaged in the strategy for further negotiations. In the 1980s Canada-United States Free Trade Agreement negotiations, the insights gained from the 1965 Canada-U.S. auto pact were instrumental in assuring others that a deal could work to Canada’s benefit.

2. Negotiate an international cooperation arrangement between Canada and China in areas of shared global interest, such as environmental protection, climate change, and the governance of international institutions.

China has responded to the environmental laxity of its early growth years by making ‘ecological civilization’ a constitutional principle.³¹ Polls show that Canadians strongly favour the two countries working more closely together on common global challenges, particularly environmental,³² creating a tangible series of non-business gains. A combined approach of sectoral agreements and cooperation on global issues could, in time, constitute a broad-

er economic partnership framework. It would also demonstrate tangible non-business gains through the international cooperation arrangement.

3. Establish clear dispute settlement mechanisms in the sectoral agreements. Sectoral agreements should include arbitration/mediation mechanisms and, where required, measures to address the protection of intellectual property rights. These processes could serve as building blocks to any eventual comprehensive trade agreement. It is important that both countries are confident in the rule of law governing these agreements, rather than arbitrary measures that may impair investment and trade. Both countries will benefit from the greater certainty of a mechanism authorized to apply those rules fairly.

4. Offer up Canada's long experience in designing social, consumer protection and transfer programs. China's new middle class and consumer society expect health and workplace safety, retirement security, livable cities and financial market regulation. There are great commercial, diplomatic and social policy opportunities for Canada to strengthen relations and gain economic advantage through the exchange by the public, private and higher education sectors of knowledge and experience gained over many decades.

5. Restore clarity and consistency to Canada's foreign investment regime for all foreign investors and enact more rigorous enforcement mechanisms to ensure foreign investors comply with undertakings made to Canada as part of investment approvals. Work with like-minded nations on criteria for national security reviews and information sharing. Special attention must be paid

to the relatively new category of national security reviews, which can be expected to periodically factor into the economic relationship. This is best addressed by a more transparent and better-informed system, perhaps along the lines of the Committee on Foreign Investment in the United States (CFIUS), that manages these situations rather than being buffeted by them.

We call for:

- Greater transparency and predictability around net benefit analysis, investor obligations and, critically, the conditions triggering a national security review;
- Coordination with like-minded countries on what constitutes a risk to national security. Many of our allies are reviewing their rules around investment in areas such as technology and critical infrastructure, and ownership thresholds, board governance and net employment benefits;
- Creation of a formal committee of economic departments, intelligence officials and independent security experts to assess and report publicly on security risks associated with investments in sensitive sectors within a set period.

Ultimately, final determinations rest with the elected government. There will always be grey areas, but these should emerge within the context of a coherent and explicable evidence-based process. This system of review can only work if we upgrade our understanding of investors, their connections to governments and other powerful players, the actual risks raised, and whether these risks can be mitigated. China maintains a list of sectors out of

bounds for investment or with special restrictions. For any agreement Canada would enter, we would expect a bilateral process aimed at winnowing the removal of protected sectors from the list as well as addressing conditions requiring foreign firms to enter into joint ventures or accept minority positions.

6. Draft an unambiguous Parliamentary declaration that Canada guards its sovereignty with the same conviction as other nations and will not tolerate external political interference in domestic politics or the affairs of residents of Canada, whether by Russia, China or any foreign country.

Canada has a head start over countries like Australia in countering foreign interference by virtue of our stricter election financing rules. We must be careful to draw a distinction between interference and influence, since Canada itself regularly organizes influence campaigns in the U.S. and other countries.

Parliamentarians and political parties need to conduct a robust and open discussion about Canada's national interests in the context of such issues as globalization, trade diversification, climate change and security partnerships if we are to develop a more durable consensus around our foreign policies among Canadians and their representatives.

7. Work more explicitly with like-minded countries within relevant international institutions to encourage China to abide by the international legal commitments it has made. Canada has a long tradition of human rights activism. The

first draft of the Universal Declaration of Human Rights was prepared by a Canadian. Both the Harper and Trudeau governments sought at various times to reflect Canadian values when it came to specific rights issues around the world.

Canada can make use of new bilateral mechanisms such as the Dialogue on National Security and Rule of Law and the Political and Security Consultations. Canadian human rights groups told us they are not against a trade agreement with China, but they want a) to do no harm (i.e. that China not backslide on existing obligations in the five core human rights treaties to which it is party); and b) Canada to use any talks to contribute to achieving greater protections on human rights. Polling shows that Canadians don't consider human rights and economic partnership as a binary choice; they view economic engagement as making Canada more effective on human rights.³³

Protection of human rights is part and parcel of a predictable regime of laws fairly applied and enforced by independent courts and tribunals. This means human rights issues should be mainstreamed. Businesses have their own stake in this for the sake of their employees in China, the protection of intellectual and physical property, and compliance with extra-territorial obligations that exist under Canadian law. We see a role for Canada not so much as an exporter of values but as an exemplar of values. What that means is ensuring trade agreements and domestic policies are inclusive—that a Canadian auto parts or insurance workplace in China looks and feels no

different than its counterpart in Canada in such matters as worker safety. Canada must walk our talk.

8. Adopt active adjustment policies with sufficient fiscal resources to allow for effective implementation, as was the case with the Canada-U.S. Free Trade Agreement. An example is the highly successful adjustment of the Canadian wine industry. Adjustment policies would be designed to assist the transition of Canadian firms and workers that may be adversely affected by new trade and investment rules, helping them to seize the opportunities for growth in the Chinese market.

9. Support Canadian enterprises, including SMEs, and women and Indigenous-led businesses, through a concomitant external adjustment effort to develop their China trade competencies and export potential. An effective and inclusive trade agenda starts at home with innovative programs to broaden participation, including the expansion of the trade commissioner service and a variety of other export promotion initiatives. Still, more needs to be done: we see internet selling platforms, such as Alibaba, as made-to-measure for many smaller Canadian firms seeking to export. We also favour expansion of the concept of sectoral selling groups and we would encourage China to establish purchasing centres in Canada to expedite the paperwork for SMEs seeking to ship goods. Canada also needs to work with Indigenous Peoples both to promote their exports and to educate foreign buyers and investors in the rights and prospects of Indigen-

ous Peoples and the critical importance of engaging them directly.

10. Radically raise Canada's game in understanding and interacting with China by all orders of government, the business community, financial sector, civil society and higher education. A long-term knowledge and relationships strategy would include serious support for more young Canadians to pursue study and work-integrated learning opportunities in China; encouragement for more Canadian business associations to become active in the region; and a concerted effort at using Canada's reputation for dependability and strong regulations for branding Canadian goods and services. Canadians need to both project Canada better within China and invest in understanding China and its people better in order to represent our interests effectively on commercial and political matters.

11. Strategically use infrastructure money, including financing from the new Canada Infrastructure Bank, for the next stage of the Pacific Gateway strategy. Canada is squandering export growth opportunities in such areas as agri-business, forestry and energy because of inadequate transport and logistics capacity and outmoded port facilities. With the imposition of tariffs on Canadian steel sold into the U.S., the timing of export infrastructure expansion couldn't be better.

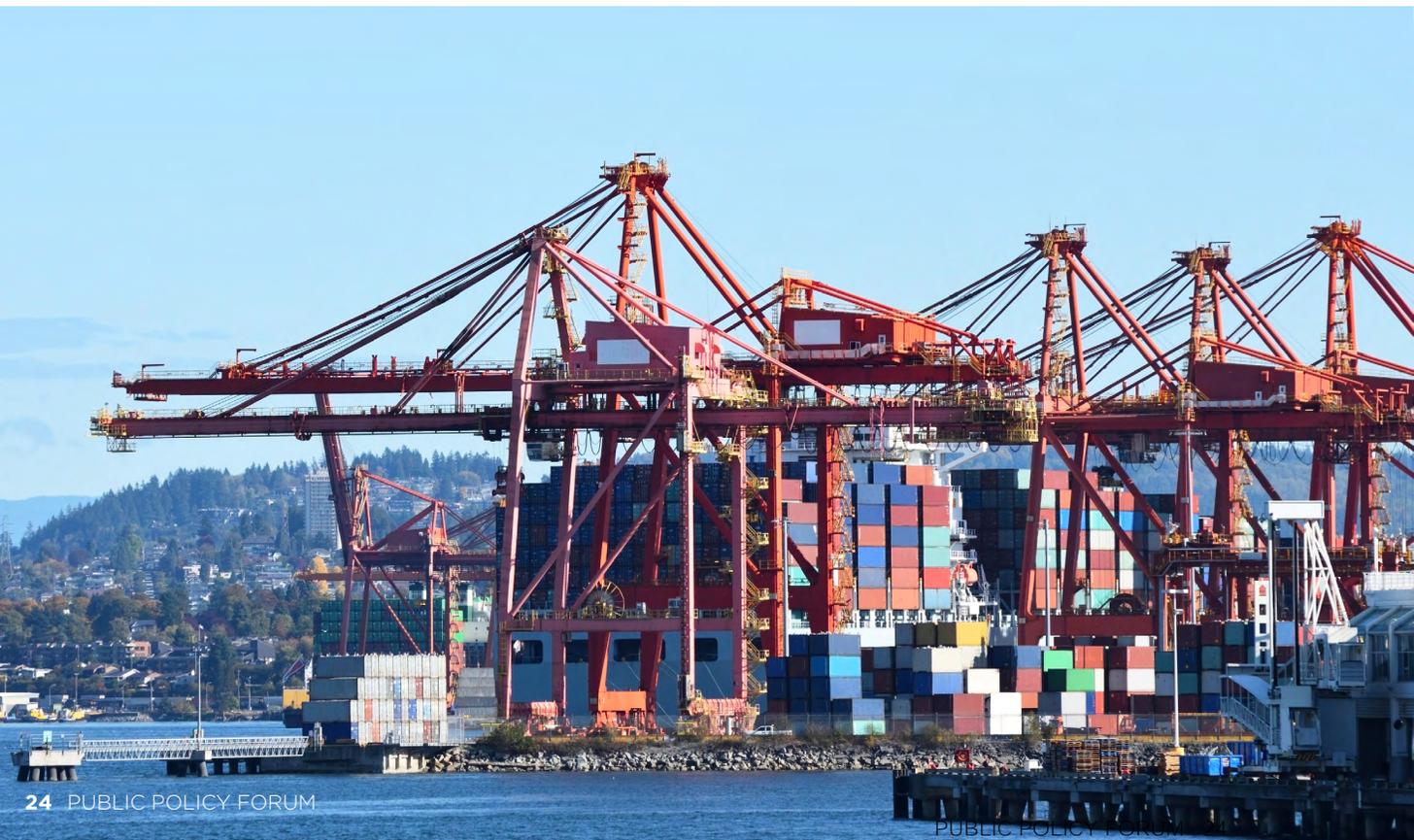
12. Participate in regional Asian forums and initiatives in keeping with Canada's levels of political and diplomatic activity in Europe,

the Americas and elsewhere. No relationship is purely economic, and the economic and political cannot be separated. If Canada is to achieve its goals as a Pacific nation and buttress efforts to strengthen rules-based behaviour and promote restraint and accommodation by great powers, it needs to tie these efforts together in a considered, coherent and concerted manner. China

is a global power and its actions affect the security of the world as well as Canada's national interests and values. That means, as with other countries and regions, having senior and stable representation at both economic and political tables. Canada has always believed that its contributions to diplomacy can make a difference.

NEXT STEPS

As we approach the 50th anniversary of Canada's recognition of China, we view these recommendations as the blueprint for beginning of a 50-year commitment to finally make Canada as engaged with its Pacific flank as it is with its Atlantic and American ones. In light of the risks and opportunities that exist in the world right now, we must move quickly. And we must go beyond small, tentative and ad hoc measures. Canada needs an ambitious, integrated strategy dedicated to furthering the interests and reflecting the values of Canadians.



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THE PUBLIC OPINION ENVIRONMENT

The Consultative Forum on China’s direction is very much in keeping with the direction of Canadian public opinion, which is highly nuanced, almost a principled pragmatism. No policy is created in a vacuum—so it is crucial to understand Canadian public opinion in addition to expert input.

Public opinion polling shows that Canadians hold several factors dear at the same time: a distaste for China’s record on human rights and democracy; an excitement about trade opportunities and economic growth; concerns of cyber-intrusions; suspicion around Chinese state-owned enterprise investments; and a belief that China cannot and should not be ignored. Certainly, support for free trade with China has been steadily rising, driven in part by anxiety

about access to the U.S. market and a general wariness about Canada’s partnership with our closest neighbour. It is difficult to discern the depth of any of these feelings, though those who have commissioned and conducted polls have told us they believe knowledge of China is light and public opinion is not deeply rooted. One analyst has described Canadian sentiment as ambivalent, anxious and opportunistic, all at the same time.

This presents complexity for policy-makers, but also underlines why we need to approach the China relationship strategically, with strong principles that will endure for the long run and cushion against events that will buffet public opinion. Concern about China and support for deeper relations can be reconciled, as this report

CANADIAN PUBLIC OPINION ON FREE TRADE THEN AND NOW

In 1985, when Canada entered free-trade negotiations with the United States, the country was deeply divided. The next two and a half years only sharpened those divides: most polls showed about one-quarter of Canadians were definitively in favour and one-quarter definitively opposed—the other half were up for grabs and eager for information. On the one hand, they were afraid of the potential impact on our sovereignty. On the other, they recognized economic benefits of preferred access to the biggest market in the world. Most premiers were against, and in the 1988 election, while Prime Minister Brian Mulroney won a majority on his free trade platform, it was with 43 percent of the vote and only three provinces—Alberta, Quebec and Manitoba (slightly)—supporting the Conservative agenda. Public opinion turned strongly in favour of free trade in the 1990s as exports soared and drove economic growth.

Support for free trade with China is higher today than it was for free trade with the U.S. from 1985-1988. But it has not been nearly as tested by public debate.

strives to do, but are subject to all manner of inputs. An example can be seen in local attitudes, especially in Vancouver, where Canadians' openness to deeper relations with China is in tension with concerns about rising house prices attributed to Chinese real estate purchases.

Generally, Canadian public opinion on China is more pragmatic than ideological, recognizing the pluses and minuses of a deeper relationship. Canadians are willing to seek balance rather than absolutes, just as they do with the U.S.

We looked at a plethora of recent and historic public opinion studies from such organizations as Nanos for The Globe and Mail,¹ Qualtrics for the University of British Columbia (UBC),² Ekos for the Asia Pacific Foundation (APF),³ and Abacus⁴.

Taken together, the major findings are as follows:

1. It's the economy, stupid! Canadians see deeper relations with China as favourable to prosperity and jobs.
2. There is a sense of opportunity, consistent with classic Canadian internationalism, in working with China on a range of economic and transnational issues, with climate change constituting a big part of this opportunity.
3. A new set of anxieties exist about how to project Canadian values and protect institutions at home.
4. Diminished confidence in the U.S. to be there for Canada is giving fresh impetus to thinking about the importance of China to Canada.

5. Distaste for China's system of government and human rights abuses (separate from calculations of what will benefit Canada and the world) exists alongside a belief that the best way to address China's human rights deficit is through deeper engagement.

The general message is not a warm embrace of China, but a pragmatism about options that go well beyond the "free trade versus human rights" framing so prominent in public discourse. From a broader public point of view, the degree to which human rights and democracy issues detract from support for free trade is nowhere near as significant as what greater international cooperation adds to the proposition.

These surveys seem to illustrate the Canadian outlook shifting from how to change China to how to live with China. The issue is not *whether* to deepen relations with China, but *how* to do so in a manner that leaves Canadians feeling their range of views reasonably reconciled.

While there are some conflicting results from different polls asking different questions at different times, the trend lines appear similar. Together they tell a compelling story.

CANADIAN VIEWS ON THE U.S. AND CHINA

The polls highlight the priorities Canadians want to guide any relationship with China and the expectations they have for the Canadian government. They also show the importance of encouraging respect for human rights and environmental concerns in China and how best to achieve that, as well as the need for more public information and discussion to better inform these opinions.

Several polls reported on Canadians' wariness toward deeper relations with China, especially regarding the intrusion of state-owned enterprises into the Canadian economy. However, in Qualtrics' estimation, these feelings are not so different from Canadians' views on the U.S. at the moment.⁵

In fact, in April 2017 Abacus compared Canadian attitudes on the two superpowers. The polling found that, as compared to the U.S., 61 percent felt China was doing more to maintain peace and avoid conflict, 57 percent felt China was setting a better example of what world leadership should look like and 56 percent felt China was doing more to grow the global economy.⁶

For its part, APF reported that 80 percent of respondents perceived Canada's relationship with the U.S. as worsening, while 71 percent of respondents perceived Canada's relationship with China as either improving or remaining the same.⁷

61%

Unfavourable or somewhat unfavourable views of China
(Qualtrics, 2017)

90%

Uncomfortable with Chinese state-owned enterprises
(Asia Pacific Foundation, 2018)

80%

of Canadians perceive Canada's relationship with the U.S. as worsening
(Asia Pacific Foundation, 2018)



Canadian Support for Free Trade with China

69%

(Qualtrics, 2017)

55%

(Asia Pacific Foundation, 2018)

54%

(Nanos, 2017)

Qualtrics highlighted a number of factors that may help explain the favourable or unfavourable views Canadians hold towards China. In particular, they found that China's system of government, human rights record, and environmental record fed unfavourable views of China.⁸ On the other hand, Qualtrics found that personal experience with Chinese people boosted Canadians' views on China.⁹

At the same time, APF reported that 74 percent of Canadians believe that immigration from Asia has a positive impact on the economy and 73 percent believe it has enriched Canadian culture.¹⁰ The APF's 2018 poll found that the majority of Canadians (82 percent) believe that Asian tourists are good for the Canadian economy.¹¹

Indeed, APF reported that Canadians increasingly feel they belong to the Asia Pacific region, and

that the rise of China is an opportunity rather than a threat (60 percent, up from 41 percent four years ago).¹²

If Canadians are wary but warming to the idea of deeper relations with China, this is most apparent in the changing attitudes towards free trade with China.

In each poll—Qualtrics, Ekos/APF, Nanos and Abacus—more than 50 percent of respondents supported the notion of a free trade agreement with China, with the levels increasing over time. Posing a slightly different question, Abacus found an even 50-50 split on public opinion concerning whether free trade would be good for the Canadian economy.

When discussing free trade with China, the protection of human rights was a recurring concern reflected in all four polls. Respondents in most polls saw a connection between free trade and human rights—some seeing free trade agreements as a tool for promoting human rights, others seeing human rights recognition as a condition for free trade. The polls make a compelling case that Canadians do not view human rights and free trade as mutually exclusive.

46%

of Canadians agree: “I could probably be persuaded to support a closer relationship with China if I knew more about what was involved and why it was in our interests.” (Abacus, 2016)

88%

of Canadians are uncomfortable with Chinese state-owned enterprises having new access to the Canadian economy, such as by buying high tech firms or investing in the oil sands (Nanos, 2017)

81%

of Canadians oppose allowing Chinese state-owned enterprises to take over Canadian firms without national security tests (Nanos, 2017)

Canadians increasingly see China as an opportunity rather than a threat

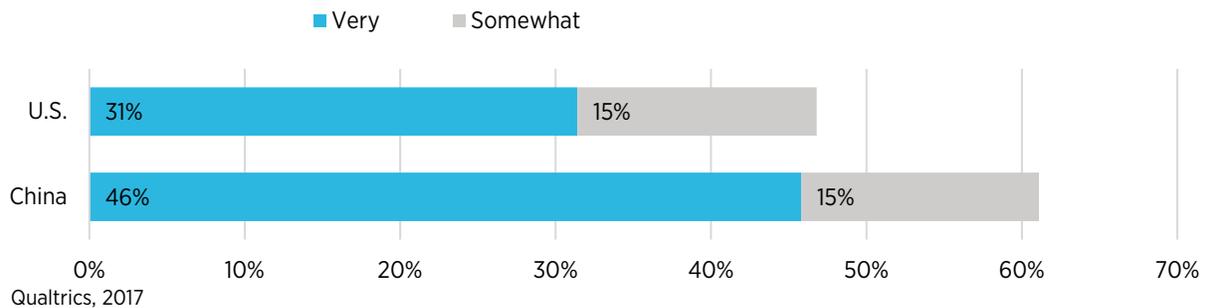
(Asia Pacific Foundation, 2018)

CANADIANS' RELATIONSHIP WITH CHINA IS COMPLICATED, AND CHANGING

Outside of the U.S., Canadians believe that China is the most important country to Canada's future

- 64%** of Canadians believe that China will be the largest economic power in the next decade (Qualtrics, 2017)
- 76%** of Canadians have negative or somewhat negative views of the Chinese government (Nanos, 2016)
- 53%** of Canadians worry that Canada will lag behind international competitors in Asian markets (Asia Pacific Foundation, 2018)

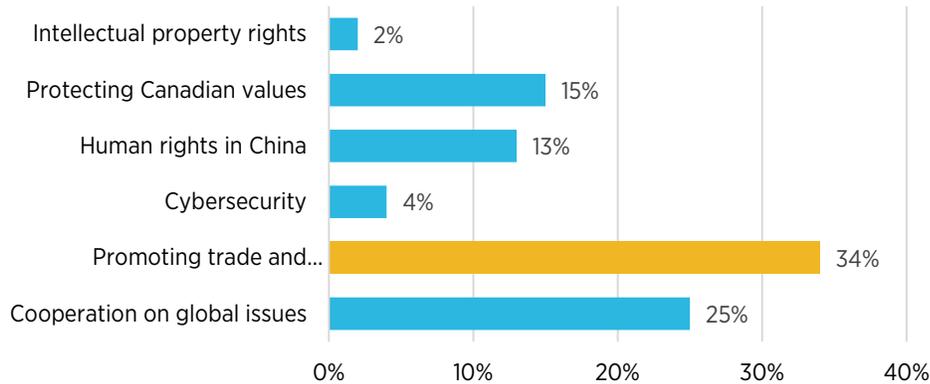
Canadians with unfavourable views of the U.S. and China



- 61%** of Canadians believe trade with China is important because of U.S. protectionism
- 62%** believe increased trade with China will give Canada a competitive edge
- 69%** believe increased trade with China will encourage investment in Canada (Qualtrics, 2017)
- 60%** perceive China as an opportunity, not a threat
- 51%** believe China holds great potential for Canadian economic interests
- 59%** believe trade with Asia will be more important than trade with the U.S. within a decade
- 59%** believe Canada would benefit from increased Asian investment (Asia Pacific Foundation, 2018)

TRADE AND HUMAN RIGHTS ARE BOTH IMPORTANT, AND ARE NOT MUTUALLY EXCLUSIVE

Canadians' top priority for a relationship with China



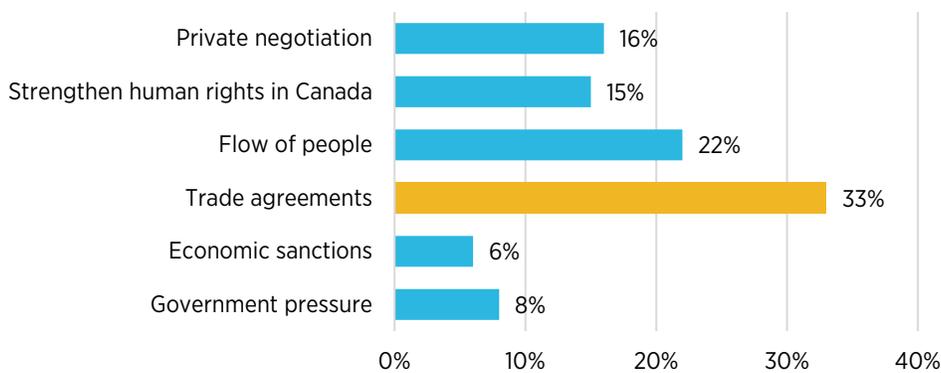
Qualtrics, 2017

69%

of Canadians support a free trade deal between Canada and China, with support trending upward over the past 5 years

(Qualtrics, 2017)

Canadian public opinion on how best to promote human rights in China



Qualtrics, 2017

91%

of Canadians believe that Chinese leaders should be pressured to respect international treaties on human rights

74%

of Canadians believe it is possible to expand economic relations with China while promoting human rights

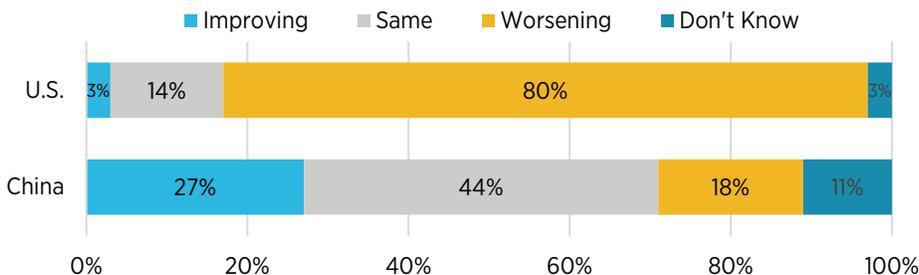
59%

of Canadians believe that human rights in China will improve as its economy opens,

(Qualtrics, 2017)

Canada's relationship with China improves while its relationship with the U.S. worsens

Perceived changes in Canada's relationships with superpowers



Asia Pacific Foundation, 2018

ENDNOTES

¹ Nanos survey dated February 2016, commissioned for The Globe and Mail. Methodology: “Nanos conducted an RDD dual frame (land- and cell-lines) hybrid telephone and online random survey of 1,000 Canadians, 18 years of age or older, between January 30th and February 1st, 2016 as part of an omnibus survey. The margin of error for a random survey of 1,000 Canadians is ± 3.1 percentage points, 19 times out of 20.” Scope: Canadian impressions of the Government of China and Canadian support for a trade deal with China. Nanos. (2016). [Canadians Divided on Free Trade With China](#). Nanos survey dated June 2017, commissioned for The Globe and Mail. Methodology: “Nanos conducted an RDD dual frame (land- and cell- lines) hybrid telephone and online random survey of 1,000 Canadians, 18 years of age or older, between June 24th and 27th, 2017. The margin of error for a random survey of 1,000 Canadians is ± 3.1 percentage points, 19 times out of 20.” Scope: Canadian perceptions of the China-Canada relationship and opinions on Canadian policy towards China. Nanos. (2017). [Impressions of Canadians on Canada’s relationship with China](#).

² Qualtrics survey date August 30 to September 12, 2017, commissioned for University of British Columbia School of Public Policy and Global Affairs and the Institute of Asian Research. Methodology: “Qualtrics panel survey of 1,519 Canadian adults (18+); adjusted to match the latest census data on age, gender, and region; in the field August 30 to September 12, 2017; margin of error $\pm 3\%$; median completion time of 15 minutes. The survey was conducted in English only. In total, 14 demographic questions (including party affiliations/support) and 60 on substantive matters and preferences.” Scope: Canadian public opinions on Chinese policy and on how Canada should engage with China. Qualtrics. (2017). [Canadian Public Attitudes on China & Canada-China Relations](#).

³ Ekos survey date February 28 to March 16, 2018, commissioned by the Asia Pacific Foundation. Methodology: The Asia Pacific Foundation of Canada commissioned EKOS Research Associates to conduct a survey of 3,561 Canadian adults (permanent residents and citizens 18 years and older). The survey was conducted from February 28 to March 16, 2018, using EKOS’s research panel, Probit. This panel offers coverage of the Canadian population accessible through Internet, phone or cellphone. A random stratified sample for this study was drawn from the panel database using random digit dialling. All data was collected online. The margin of error—which measures sampling variability—is $\pm 1.64\%$ for the entire sample. The average completion time for the survey was 19 minutes. The results have been statistically weighted by EKOS according to the current census data on age, gender, and region to ensure the representativeness of the sample. Discrepancies in or between totals are due to rounding.” Scope: “The NOP reviews some legacy questions from our past polls regarding Asia Pacific identity, warmth of feelings toward Asia, perceived importance of Asia, Canada-Asia relations, and support for free trade agreements. It tracks consistent trends as well as changes in Canadian views on Asia. The poll also poses some new questions that help uncover the

factors driving the Canadian public's feelings about particular countries; their attitudes toward a 'progressive' trade agenda; and, their views of what role Canada should play in the international arena." Asia Pacific Foundation. (2018). [National Opinion Poll 2018: Canadian Opinions on Asia](#).

⁴ Abacus survey dated January 20, 2016, commissioned by Teck Resources. Methodology: "The survey was conducted online with a total of 1,500 residents of Canada aged 18 years and older, between September 9th and 11th, 2015. A random sample of panelists was invited to complete the survey from a large representative panel of Canadians, recruited and managed by Research Now, one of the world's leading provider of online research samples. The Marketing Research and Intelligence Association policy limits statements about margins of sampling error for most online surveys. The margin of error for a comparable probability-based random sample of 2.1% 19 times out of 20. The data were weighted according to census data to ensure that the sample matched to population according to age, gender, educational attainment, and region. Totals may not add up to 100 due to rounding." Scope: Canadians' views of Canada's relationship with China, with an emphasis on trade, including their preferences for that relationship going forward. Abacus. (2016). [The Canada-China Relationship](#). Abacus survey dated April 27, 2017. Methodology: "Our survey was conducted online with 1,500 Canadians aged 18 and over from April 21 to 24, 2017. A random sample of panelists was invited to complete the survey from a large representative panel of over 500,000 Canadians. The Marketing Research and Intelligence Association policy limits statements about margins of sampling error for most online surveys. The margin of error for a comparable probability-based random sample of 1,500 is +/- 2.6%, 19 times out of 20. The data were weighted according to census data to ensure that the sample matched Canada's population according to age, gender, educational attainment, and region. Totals may not add up to 100 due to rounding." Scope: Opinion on Canadian response to hypothetical geopolitical situations, opinion on Canadian policy on China, opinion on China vs US. Abacus. (2017). [Tensions Rising: Canadian Views on Foreign Conflict, China, & Trudeau in an International Crisis](#).

⁵ Qualtrics. (2017). [Canadian Public Attitudes on China & Canada-China Relations](#), p. 4.

⁶ Abacus. (2017). [Tensions Rising: Canadian Views on Foreign Conflict, China, & Trudeau in an International Crisis](#).

⁷ Asia Pacific Foundation. (2018). [National Opinion Poll 2018: Canadian Views on Asia](#), p. 13.

⁸ Qualtrics. (2017). [Canadian Public Attitudes on China & Canada-China Relations](#), p. 26.

⁹ Ibid, p. 26.

¹⁰ Asia Pacific Foundation. (2018). [National Opinion Poll 2018: Canadian Opinions on Asia](#), p. 8.

¹¹ Ibid, p. 8.

¹² Ibid, p. 7.

WHAT WE HEARD

Over the course of 18 months, PPF organized five meetings of the Consultative Forum on China in three cities across Canada, numerous one-on-one and small group consultations and conducted research. In this section, we share the key issues raised during the Consultative Forum meetings, by other experts we consulted, and in our own research, which together informed the development of this report’s recommendations. We thank all the participants for their insights and share their perspectives in the pages that follow.

Engagement is better than non-engagement, but we must be strategic

The Consultative Forum heard that engagement is better than non-engagement when it comes to China. While there is no single overriding ‘Canadian’ view of China, there is wide recognition that China is a critically important relationship for Canada, both economically and politically, and these economic and political implications of engagement cannot be easily separated. China’s rise on the global stage, the mark it is leaving on a number of global challenges from climate change to international development, and the role it is playing in so many international institutions—both moving into the space vacated by the U.S. and establishing its own new institutions—mean that China cannot be ignored. Our relationship with China cannot be left to drift without a clear and concerted Canadian strategy.

In a paper prepared for the Consultative Forum called “A Mouse Sleeping Next to a Dragon: New Twitches and Grunts,” Carleton University Assistant Professor Stephanie Carvin writes, “The reality is that, as a middle power, Canada cannot afford to ignore a state with a sixth of the world’s population. Our prosperity depends on trade—but also a stable world order, including the rule of law.”¹ She was one of those who concluded that Canada needs to be strategic in every step it takes and keep its “eyes wide open.” In the face of this reality, participants speaking on behalf of the labour movement and steel industry, for example, recognized that Canada should engage China with a sophisticated, holistic and coordinated long-term strategy.

However, the Consultative Forum heard that Canada lacks an effective China strategy at the national level and the majority of Canadian businesses that operate internationally have expanded only to the U.S. We heard that what Canada needs is a united government and business strategy; a strategy that acknowledges—and coordinates—the roles of all levels of government and operates in alignment with Canadian businesses.

The Consultative Forum also heard that long-term planning is key: 20 years is a small slice of history. As the strategic plans produced by President Xi Jinping’s government show,

China is thinking long term, and so Canada needs to do the same. And while many Canadian businesses are eager to fast-track a more formalized trade relationship with China, we would be wise to remember that Australia's free trade agreement negotiations with China took close to 10 years and Canada's free trade agreement with Europe took eight years. (Most conversations took place before the new United States-Mexico-Canada Agreement, and its restrictions on free trade agreements, was concluded.)

China is a critically important market

During the 18-month period of consultations, a consistent message was that China should be a critically important market for Canada. According to the IMF, Asia accounts for more than 60 percent of global growth.² China is at the heart of Asia's rise, generating more than half of its gross domestic product. The continuing Chinese economic miracle has astonished the world and, so far, consistently proven the doubters of its sustainability wrong. Since it initiated market reforms under Deng Xiaoping in 1978, Chinese growth has averaged 10 percent annually.³



Although it has slowed recently, its current 6.6 percent growth rate is over twice that enjoyed by Canada (3 percent in a good year; 2.1 percent currently).⁴ This growth—the equivalent of adding a Canada sized-economy every two years—has lifted more than half a billion people out of poverty.⁵

China has become the undisputed second-largest global economy and in the coming decade or so is expected to surpass the U.S.⁶

Despite stresses—regional disparities, an aging population, declining heavy-industrial sectors, property bubbles, growth in debt levels, and continuing environmental degradation—China is on track to double its GDP between 2010 and 2020 and thus achieve its self-declared ambition to become a “moderately prosperous” country.⁷ Outbound investment through “China Inc.” continues with a focus on ‘Made in China 2025’ sectors, including Internet-enabled businesses, such as artificial intelligence (AI) and the Internet of Things.⁸

Under now-‘paramount leader’ Xi Jinping, the Communist Party Congress (2017) endorsed a national rejuvenation strategy. “Socialism with Chinese characteristics for a new era” aims to

make China a nation with leading, global influence by 2050.⁹ President Xi wants China to not only help write the rules of the game but to construct the playgrounds on which the games are played.

The flagship international, state-to-state collaboration program for building China-sponsored infrastructure around the world is its Belt and Road initiative, announced in 2013 by President Xi. It is enormous in its ambition, its scale and the sums of money involved (supported through the Asian Infrastructure Investment Bank, the Silk Road Fund and the New Development Bank). It is an expression of both hard and soft power. By comparison, the Marshall Plan that underwrote the regeneration of Europe after the Second World War was roughly one-tenth the size of what is contemplated in the Belt and Road initiative.¹⁰ This project is not without controversy and it has suffered setbacks in a number of nations where China has been building infrastructure.¹¹ While it presents an opportunity for Canada, we also heard we need to better think through, for example, our Arctic policy as northern shipping lanes within the Belt and Road conception become more navigable.

China is transitioning to a middle class and consumer society. McKinsey [estimates](#) that the Chinese middle class will include more than half of the country’s urban households by 2020, up from just [four percent](#) in 2000.¹²

This middle class, with more money and more ambition, has not been shy already to demand cleaner air¹³ and water¹⁴ and safer food¹⁵ and drugs.¹⁶ Its expectations will only grow. We heard that Canada has a lot to offer to a government

learning to respond to middle class demands because of our long experience with programs including pensions, insurance and wealth management, healthcare, food safety and workplace health and safety, well-regulated financial markets, the development of livable cities, management of national parks and waterways, promotion of recreational sports and consumer protection and taxation. Canada also has experience in offering its expertise to other countries in transition, as in Eastern Europe after the Cold War and in post-apartheid South Africa.

In terms of increasing our engagement, we heard about different sectors where engagement is already going on and sectors where there is a lot of potential. The Complementarities Study of the Harper Government identified seven sectors where the interests and requirements of one country were matched with a capacity to supply in the other country: agriculture and agri-food, clean technology and environmental goods and services, machinery and equipment, natural

resources and derived products, services, textiles and related goods, transportation infrastructure and aerospace.ⁱⁱⁱ The Advisory Council on Economic Growth recently laid out a strategy in its three reports for Canadian economic growth, including trade and investment with China and how to position Canada as a global trading hub.^{iv} The Advisory Council reports highlight which sectors Canada should focus on in order to grow its economy, including agri-food, advanced manufacturing, energy and renewables, and healthcare and life sciences.

Given the feeling among some in the Consultative Forum that China does not always adhere to the rules, clear dispute settlement mechanisms in any agreements made with China would help with our expansion in the Chinese market. As the smaller player in these relationships, Canada depends on a system of fairly adjudicated rules, whether through the WTO or regional and bilateral agreements. This is critical for Canada, as emphasized in the discussion this year around the importance of preserving Section 19 of NAFTA.

China consumes 35 percent of the world's seafood, and over the next decade, its rising middle class is expected to increase demand for seafood, causing China to account for an estimated 53 percent of global seafood consumption.

Global demand for seafood is outstripping wild caught supply, and China is becoming one of the biggest single markets for surf clams and lobsters. It has become Clearwater Seafood's second largest foreign market, surpassing the U.S. in 2015.

In 2016, Clearwater capitalized on rising Chinese demand by launching its first direct-to-consumer sales strategy with a flagship store on Alibaba, a Chinese e-commerce platform. It also opened a flagship store in China and is partnering with a Chinese grocery chain to offer its seafood directly to consumers in store, bringing the company into the retail space more prominently than ever before.

What this means for Atlantic Canada so far is 509 middle class jobs within Clearwater's Atlantic Canada operations.



60%

of Clearwater's surf clams business is linked to China

30%

of Clearwater's lobster business is linked to China

16%

of Clearwater's overall sales are in China, its largest market outside Canada

509

middle class jobs with Clearwater have been created in Atlantic Canada in response to Chinese seafood demand

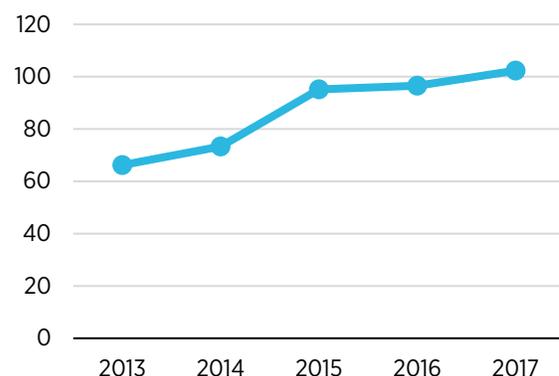
\$102 million

in Clearwater sales to Chinese markets in 2017.

(Clearwater Seafood)

These break down as: 180 fishing fleet positions, 304 processing facilities positions, and 25 head office support functional positions. And that's without counting the impact on places like Halifax's Stanfield Airport, where seafood is the primary air export shipping commodity.¹⁷

Clearwater Seafood Sales in China, 2013-2017 (millions)



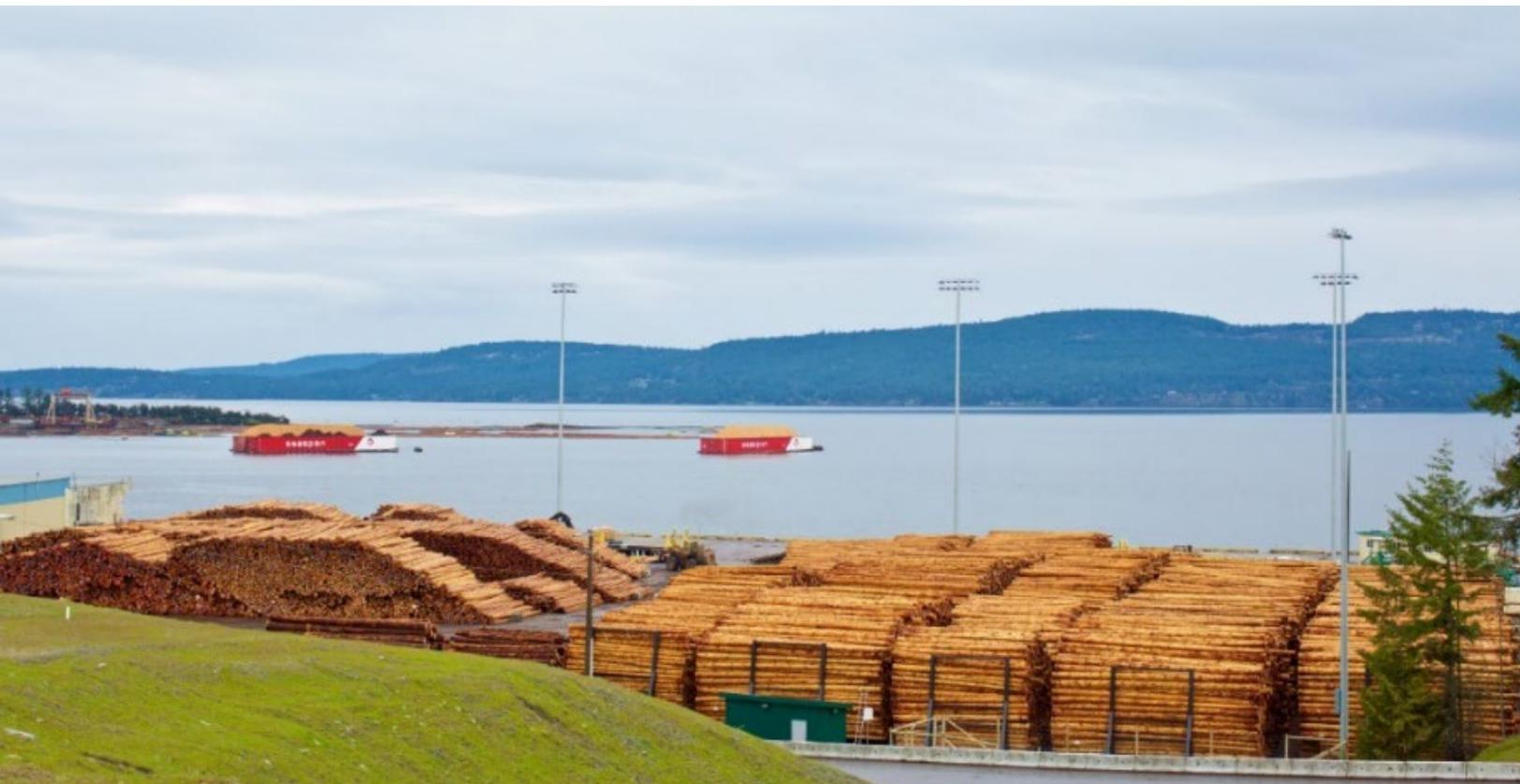
For TimberWest, a Canadian timberlands company, China has become the largest export market.

Logs that are deemed “surplus” to domestic demand are exportable from British Columbia. Within its export program, TimberWest has developed market opportunities in the Pacific Rim, of which China has become the largest.

China’s imports of hardwood and softwood logs rose by over 40 percent between 2012 and 2017 as a result of strong economic growth and increased demand. In recognition of this, China has eliminated most trade barriers to importing Canadian logs. Regulatory issues including

phytosanitary and measurement issues have been largely resolved.

Canada, however, maintains regulations restricting the export of logs, which represent a barrier to producers like TimberWest from entering into long-term supply commitments with foreign customers. In spite of this uncertainty, TimberWest continues to invest in its logistics facilities in Canada to facilitate trade with China and other export markets.¹⁸



Many who participated in the Consultative Forum, though not all, thought that developing a comprehensive free trade agreement now—while political parties lack alignment and international relations are uncertain—would be biting off more than Canada can chew. Turning to past experience, we heard that the Canada-U.S. Auto Pact, negotiated by the Pearson government with the Johnson administration in 1965, set rules for the most critical industry in the manufacturing sector, and its success built confidence on both sides of the border. This ultimately laid the foundations for a broader free trade agreement.¹⁹

By contrast, other members expressed concern that China would not take Canada seriously if it wasn't 'all in,' and that a broader arrangement would be required to have enough pieces to trade in the course of negotiations. Some participants also drew our attention to the WTO rules which allow for preferential tariffs as part of a free trade agreement only where the agreement covers "substantially all trade." However, we also heard from some companies that placing the initial focus on so-called 'behind the border' barriers and other areas to promote trade would secure them benefits. For example, this might be through greater cooperation and communication between customs officials, by easing the documentation processes exporters face, by mutual recognition of standards or certificates, or through establishing selling groups to help Canadian businesses, especially SMEs, to penetrate the Chinese market. Streamlining movement through our airports, huge engines of growth themselves, and ports for goods and people, would also produce economic benefits.

Getting goods to market and promoting the Canada brand

The Consultative Forum discussed the importance of being able to get goods to the Chinese market efficiently, with some raising the problem of choke points at our ports, both inland and coastal, inadequate capacity in our rail and road transportation systems, and our inadequate pipeline capacity. This impairs our ability to attract investment and grow trade with Asian nations, including China.

Our geography gives us certain advantages and we heard that we need to make the most of them: British Columbia ports are closer to Asian markets than any other ports on the west coast; ships from Asia can reach British Columbia up to three days faster than Los Angeles;²⁰ our rail system—from Prince Rupert or Vancouver—can get goods quickly to Chicago, the hub for American transport serving markets in the Midwest and the Northeast.²¹ With the Northwest passage becoming increasingly navigable and new ownership of the port of Churchill and the rail line leading there, another outlet to the world is opening up.

Both the Martin and Harper governments made significant investment in, respectively, the Pacific Gateway Strategy²² and the Asia-Pacific Gateway and Corridor Initiative,²³ measures that were also supported by western provincial governments. While these initiatives made significant progress, those plans were laid a decade ago and more needs to be done. Canada is effectively squandering export growth opportunities in such mainstay areas as agribusiness, forestry and energy, and therefore further suppressing rural

economies. We heard that we should look to federal and provincial government infrastructure money, as well as new Canada Infrastructure Bank financing, to renew and update the Pacific Gateway strategy. Such investments will generate long-term benefits by enhancing productivity, creating jobs and increasing export earnings as we look to diversify our markets and take up key trading opportunities.

We also heard about the additional efforts that Canada will need to make to promote its brand in the Chinese market. Our universities and firms aren't all going to be household names in China, but Canada should be known in China as a diverse and inclusive society, a safe place with stable institutions, a place of safe food and medicines, safe campuses and advanced teaching and research, a great place to travel, and somewhere to bring your talent. As Apple has shown, a good brand can command both respect for products and higher prices. Canada needs to do more to build a brand that has a halo effect.

Education

Education services is an area that has been an early mover in terms of Canada-China trade. China is the largest source of foreign students to Canadian schools and universities;²⁴ students from China accounted for roughly one-third of long-term international students.²⁵ It is estimated that on average each international student spends over \$30,000 a year in Canada and the total annual expenditures of all short- and long-term international students, including their visiting families and friends, contributed \$15.5 billion to economic activities in Canada in 2016.²⁶

But there are lessons to be learned from elsewhere. For example, Australia has significantly increased its number of international students from China over the past several years,²⁷ seeing a 12.3% increase in Chinese student commencements.²⁸ In comparison, Canada saw a 7% increase in the same year.²⁹ Canada could benefit from studying the factors behind Australia's recent success in order to further capitalize on the opportunity created by Chinese students looking to study abroad. The Consultative Forum also heard that a careful approach is needed to managing the downstream risks, including security risks associated with intellectual property generated through post-secondary research returning to China with Chinese students.

Canada is a popular destination for Chinese students, and the proportion of Chinese students in Canada is growing rapidly.

\$4.3 billion

is the estimated contribution to Canada's GDP by Chinese students in 2016, one-third of the \$12.8 billion contributed by international students overall

Federal government and university efforts to increase numbers of international students in Canada, paired with the rising middle classes in emerging economies, are key reasons for the significant rise in international students in Canada over the past decade.

This has been especially true for China; the number of Chinese students studying in Canada has skyrocketed over the past decade, as has the proportion of Chinese students among all international students in Canada.

Education in Canada is high quality, and though international students pay significantly higher tuition fees than Canadian students, tuition for international students costs significantly less in Canada than in other popular countries, such as the United States, Australia and the United Kingdom.

The federal government developed an International Education Strategy in 2011, which focused on international students from emerging economies, including China.

Chinese International Students: Opportunities

11%

of Canada's postsecondary student body are international students

32%

of international students studying in Canada in 2016 were from China

186,000

Chinese students studying in Canada in 2017

250%

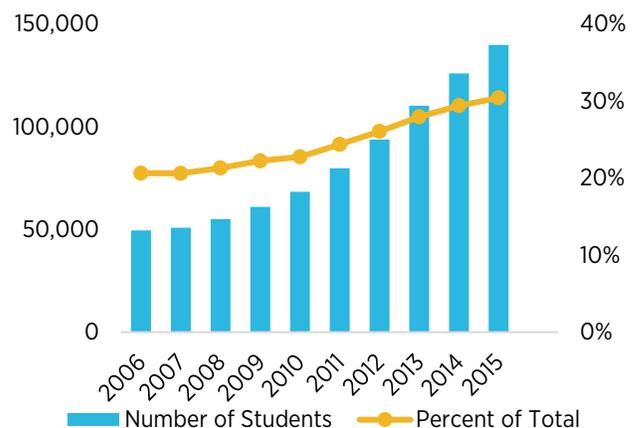
increase in the number of Chinese students in Canada between 2007 and 2017

(Universities Canada)

Post-secondary institutions have also increased recruiting efforts abroad, contributing to the influx of Chinese students.³⁰

Increase in Chinese Students

More Chinese students are choosing Canada, making up a higher percentage of Canada's total



Participants from the post-secondary education sector alerted us to the fact that some young Canadians are embracing the rise of China and embarking on China studies. For example, there is high demand for Chinese language training in Canada. However, students with this training reported little demand for it in the job market. Broader conversations about how to promote people-to-people ties with China through the education sector, and how to promote demand for these skills among Canadian businesses, are not taking place.

In the U.S., for example, there are specific initiatives to encourage students to study in China, such as the [100,000 Strong Campaign](#) that sets a target and date by which they aim to increase the numbers of university students going to China, and the [1 Million Strong Campaign](#) that aims to increase Mandarin proficiency within U.S. K-12 schools. Canada should look to adopt a similar program with similar goals. This would also be consistent with the recent Report of the Study Group on Global Education, which concluded that “Canada needs a more strategic and ambitious approach to global education,” as global education is an instrument for achieving

national priorities, including a dynamic work force, an inclusive and open society, and a country with global connections and influence.³¹

Tourism

Every year since 2015, more than 500,000 tourists from China make Canada their destination of choice.³² We heard that tourism is another sector that shows tremendous potential for Canadians to take advantage of a growing Chinese middle class. Chinese travel to Canada in 2017 was up 12 percent with 682,000 arrivals and China was Destination Canada’s second largest overseas market.³³ Chinese tourists spend almost \$2,400 per trip to Canada,³⁴ which is a significant boost to the economy and to those employed in the tourism sector, often small businesses and seasonal workers. We note that Chinese tourism is diversifying from visits to classic destinations like Banff and Niagara Falls to business conferences and, with Canada’s large immigration from mainland China, family visits. We also heard it is important that air services agreements with China are revisited in order to support increased tourism and economic growth.

Number of Visitors per Month from China to Canada, 2017-2018³⁵

Year	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
2017	44,916	31,338	28,904	40,305	55,074	79,616	104,840	101,218	80,688	53,642	29,985	44,017
2018	39,052	55,286	32,796	40,165	62,795	75,599	99,248					

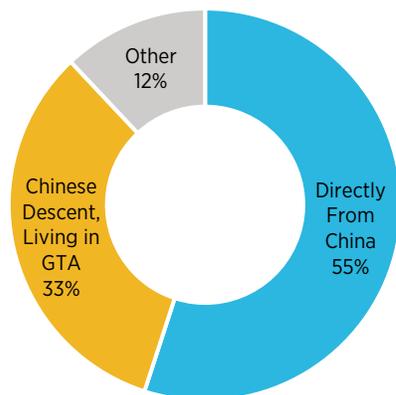
Gravenhurst, Ontario is a popular destination for Chinese tourists. Welcoming Chinese tourism continues to benefit the town's economy.

As the birthplace of Dr. Norman Bethune, Gravenhurst is an important destination in Canada for Chinese tourists. Bethune was a Canadian doctor who spent time in China in the late 1930s, teaching doctors and nurses and operating mobile clinics during the Second Sino-Japanese War. He performed emergency battlefield operations and created portable operating theatres that could be carried around the front. He died from an operation-related infection in 1938 and is extolled in China as a selfless hero. Many Chinese visitors are interested in paying homage to the doctor at his birthplace in Gravenhurst.

The town has capitalized on this interest by catering to Chinese tourists and developing Bethune-related attractions in partnership with Parks Canada, including Parks Canada's Bethune Memorial House historic site, the Victorian house where Norman Bethune was born.

Asian Visitors to Gravenhurst, ON since 2010

Approximately 130,000 visitors of Asian origin have visited Gravenhurst since 2010



Chinese Tourism Market: Opportunities

5,600

tourists visited Gravenhurst directly from China between 2014 and 2015

130,000

tourists of Asian origin have visited Gravenhurst since 2010

25%

of visitors to Gravenhurst from the GTA are of Chinese descent

90%

of visitors to the Bethune Memorial Centre are from China

\$572,000

has been spent by Asian tourists in Gravenhurst since 2010

(Town of Gravenhurst)

Town Wayfinding signs pointing tourists to the Memorial House include simplified Chinese.

In 2012, Parks Canada also opened the Norman Bethune Visitor's Centre. Businesses have made increased efforts to learn about and cater to Chinese visitors; the Gravenhurst Chamber of Commerce hosted a trip to China in 2017 for local business owners to learn more about Chinese culture and visitors. The town has even created a welcome sticker for every commercial business that includes both traditional and simplified Chinese translations.

Specific efforts to attract and cater to Chinese tourists can boost tourism and have a positive effect on the local economy, as Gravenhurst has seen over the past several years. ³⁶

Focusing on cities and the drive for technology

As China's economic center of gravity continues to move south, the Greater Bay Area, encompassing Guangzhou, Shenzhen, and Hong Kong (which contains one of the larger Canadian diasporas), will likely be the source of a disproportionate share of China's next wave of growth. With a population of 70 million and a GDP per capita of more than \$20,000³⁷ it has become the headquarters of many of China's most innovative start-ups and scale enterprises.

One approach for Canada would be to focus efforts on emerging Tier 1 cities, where opportunities are robust but competition not as stiff. In 2017 alone, 15 new Tier 1 cities were identified, each larger than Toronto.³⁸ China, says President Xi, "will not close, but will open wider and wider."³⁹ The 2015 'Made in China 2025' strategy designed to comprehensively upgrade Chinese industry is an integral piece of President Xi's reform agenda. It highlights 10 priority sectors, including new advanced information technology; automated machine tools & robotics; aerospace and aeronautical equipment; maritime equipment and high-tech shipping; modern rail transport equipment; and new-energy vehicles

and equipment.⁴⁰ The emphasis on technological advancement in these priority sectors is no accident. For instance, China is determined to make the country an "innovation centre for AI" by 2030.⁴¹

E-commerce is another area that begs for attention, especially given Canada's high proportion of SMEs.⁴² E-commerce platforms, such as Alibaba, reduce the time and cost of marketing Canadian products into a market like China. Thus this 'enabling' sector should also be included as part of greater engagement with China, and efforts need to be organized to help Canadian SMEs scale their production capabilities so they can deliver on the potentially larger orders that a market the size of China can generate. We were told that Alibaba has recently opened an office in Vancouver, which could help in building a portal into the Chinese market.

By 2020, China is projected to be the world's largest cross-border e-commerce market, worth \$9.4 trillion Canadian.

As part of the government's focus on growing domestic consumption, Beijing's most recent Five-Year Plan includes reforms to stimulate the services sector, provide better goods, and support online shopping.

Canadian firms are well positioned to take advantage of this boom in e-commerce-led growth. Chinese consumers are demanding foreign products of superior quality which are innovative and unique in design. Canadian products are a natural fit for this demand.

Much of the consumption growth fueled by upper middle-class and affluent Chinese consumers will be located beyond China's biggest metropolitan areas. This will expand the reach of brands and drive the need for increased distribution and logistics abilities.

Key challenges for Canadian firms when entering the Chinese market include:

Language barriers: such as those created by Chinese language-only platform management interfaces.

Import and logistics barriers: such as import requirements, taxes and duties, and transport costs. Slow customs processing times make delivery times unacceptably long for Chinese consumers.

Chinese e-Commerce Market: Opportunities

700 million

internet users

40%

of online Chinese consumers purchase goods from abroad

30%

annual growth of cross-border e-commerce in China

(Asia Pacific Foundation)

Five-Year Projection of Chinese Consumption Growth

81%

of consumption growth will come from upper middle-class and affluent households

65%

of the consumption increase will be driven by consumers under 35

42%

of total consumption growth will be driven by e-commerce

90%

of e-commerce growth will come from mobile e-commerce

(Asia Pacific Foundation)

Legal barriers: weak intellectual property protections that do not prevent the sale of counterfeit goods online.

An agreement that addresses these barriers will allow Canadian businesses to take full advantage of China's e-commerce market, which is expected to reach C\$9.4 trillion by 2020.⁴³

Intellectual Property

Though impressive, Chinese technological achievement is also intrusive and, when it suits China, exclusive. In its 2018 [assessment](#) of China's technology transfer and IP practices, the U.S. Trade Representative concluded that China actions undermine U.S. firms' ability to compete fairly in the global market by (1) requiring or pressuring U.S. companies to transfer technology to Chinese companies; (2) imposing restrictions on, and intervening in, U.S. firms' investments and activities, including through restrictions on technology licensing terms; (3) obtaining cutting-edge technology by directing and facilitating the investment and acquisition of U.S. companies by Chinese companies; and (4) conducting and supporting intrusions and theft from the computer networks of U.S. companies.⁴⁴

In our consultations, PPF was made aware that China's practices target Canadian companies using these same tactics. In this regard, some participants highlighted the need for the strong protection and enforcement of intellectual property rights. But as also noted by some participants, companies cannot afford to miss out on huge economic opportunities by delaying entry into the Chinese market, despite fears around intellectual property protection.

National security and defending our interests against political interference

Canada's national security is obviously central to our national interests. We need to be able to distinguish where China puts Canadian national interests at risk and where it does not, and manage risks accordingly. We need to be firm

and unambiguous in stating that Canada, like China, will defend its sovereignty by not tolerating interference in our domestic affairs, whether on Canadian campuses, within diaspora communities, or by businesses. While we should always strive to be pro-engagement and respectful in our relations, Canadians expect their government to take matters of sovereignty seriously.

As one speaker explained, there is a fundamental difference between foreign influence and foreign interference. The latter is an attempt by a state to advance its interests by covertly undermining legitimate rules and processes. All countries, including Canada, engage in foreign influence - advocacy with foreign governments or interests through diplomatic engagement or other means.

We heard that Chinese-sponsored political interference and cyber intrusion has been reported by the Canadian Security Intelligence Service (CSIS) on various occasions. Then-CSIS Director Richard Fadden accused China of foreign interference and spying in a speech in March 2010, saying that Chinese authorities were organizing demonstrations against the "five poisons" including Falun Gong, and apparently recruiting agents through the Confucius Institutes.⁴⁵ In 2010, cyberattacks that crippled the Department of Finance and the Treasury Board Secretariat computer systems were linked to efforts, likely originating in China, to gather data on the potential takeover of a Canadian potash company.⁴⁶ Earlier this year, Fadden and Ward Elcock, another former CSIS director, along with John Adams, former chief of the

Communications Security

Establishment, urged the federal government to heed the warnings of U.S. intelligence services and cut ties with Huawei, the Chinese smartphone and telecom equipment maker.⁴⁷ Canada and China did reach an agreement meant to curtail industrial espionage and enhance cyber-security in 2017.⁴⁸

The Consultative Forum's sessions included discussion about Chinese government interference in our democratic process and in their state-sponsored illicit cyber activities. The

presence of Confucius Institutes on 12 campuses was one of several issues raised. Generally, it was thought that it would be difficult to distinguish these from other soft diplomacy initiatives such as the Goethe-Institut Kanada and Alliance Française. Further, Canada also employs such institutes as a diplomacy tool. But if Canada invested more in understanding China, it would render the Confucius Institutes less relevant. Regardless, Canada has a responsibility to protect ethnic Chinese students and others from possible forms of harassment.

Confucius Institutes

China has doubled down on applying soft power through the development of an international media network and establishment of cultural study centres around the world. The first Confucius Institute opened in 2004 in Seoul, South Korea. There are now more than [500 institutes](#) around the world, including on 12 Canadian campuses. As [Xi Jinping observed in 2014](#), "We should increase China's soft power, give a good Chinese narrative, and better communicate China's message to the world."

Whether promoting China's traditions, values, language, and culture will win China friends and influence is still to be determined. Canada must ensure these institutes operate in a manner that does not place undue pressures on students on campus.

These matters also concern other Western countries, some of which have taken steps to address the potential for domestic political interference. Australia, for example, recently passed measures aimed at controlling behaviour that “falls short of espionage but is intended to harm Australia’s national security or influence Australia’s political or governmental processes.”⁴⁹ But these efforts to control ‘influence’ rather than ‘interference’ have also been widely criticized by rights groups as dangerous overreach.⁵⁰

Generally, Canada is better positioned than many other countries to deal with risks of foreign interference due to strict limits on political contributions, prohibitions on foreign election funds and lobbying registration requirements. That said, new responses may be necessary considering a new generation of interference tactics, such as the Russian ‘fake news’ attacks on a number of fellow democracies.

The Consultative Forum also heard that we can no longer treat the two aspects of trade and security separately. Canada needs to marry our strategic, economic and investment interests. As one participant noted, we need to look at the China puzzle and take forward the good ideas that are both economically viable and politically satisfactory. Canada needs a sound system for screening investments and exports that balances our traditional bias in favour of open investment, with protection of national security. This is similar to what several Western countries are doing in reviewing their investment screening regimes and making it tougher for outside investment where national security may be at risk.⁵¹

We heard that Canada’s foreign investment regime should be refreshed. The Canadian government has not only a right to say no to foreign investments that pose a national security risk or do not benefit Canada, but also a responsibility to do so. But that doesn’t mean the system should be opaque and discourage good investment. Investors reasonably expect to know the rules before getting on the field, and to be confident those rules will be fairly applied. With recent government decisions generating significant investor uncertainty (eg. Petronas, CNOOC, Aecon), it is time to re-think the system.

As noted in the previous section’s examination of public opinion, Canadians are anxious about Chinese state-owned enterprises investing in Canada. Warranted or not—and there is plenty of debate—they are not alone in these misgivings. Canada should, for example, make common cause with the EU/Japan/USA WTO initiative on forced technology transfers, an initiative also referenced in the recent G7 Charlevoix communique. Simultaneously, some said it is time to re-examine the criteria established in December 2012 by the Harper Government for state-owned enterprise investment. Not all state-owned enterprises are highly controlled by the government, and some non-state-owned enterprises are strongly directed by the state. In addition, whether an inbound investment is in the Canadian interest cannot be assessed solely by the scale of the investment. University of Toronto professor Wendy Dobson, a participant in the Consultative Forum, has recommended that Canada should place greater focus on investor behaviour rather than ownership in and of itself when considering

whether it is in Canada's national interest to allow an investment.⁵²

We heard that the U.S. has had a positive experience with an inter-agency committee, the Committee on Foreign Investment in the United States, which is authorized to review certain transactions involving foreign investment, in order to determine the effect of such transactions on the country's national security. The Committee is chaired by the Secretary of the Treasury, with members from nine different departments. During the review period, the Committee examines the transaction to identify and address any national security concerns that arise as a result of the transaction, and the members may request additional information from the parties.

Legislation specifies the criteria to be considered. In certain circumstances, CFIUS may also refer a transaction to the President for decision.⁵³

Several participants also pointed out that China's investment policies place significant restrictions or outright prohibitions in a number of sectors⁵⁴ (as does Canada). For example, while foreign investment is encouraged by China in high-end manufacturing, high technology, energy conservation and environmental protection and modern services, it is restricted or prohibited in most cultural, sports and entertainment services, oil, banking, power, heat, gas production and distribution facilities, medical and pharmaceutical manufacturing, and education.⁵⁵ Restricted industries are usually accessible to foreign investors only through joint venture structures with Chinese companies or are restricted through limits on foreign shareholding.⁵⁶

Environmental cooperation

As one member of the Consultative Forum observed, China takes seriously issues of ecological security, environmental safety and ecological civilization. In 2012, the Communist Party of China included the goal of achieving an 'ecological civilization' in its constitution.⁵⁷ In Canada's political culture, these terms are typically framed as issues of climate change, the changing Arctic, sustainable fishing and the 'blue economy.' Though the terminology may differ, the overlapping interests are clear. China's interest in and potential for influence on these issues is equally clear and China is a natural partner for Canada in pursuing its global climate change and sustainability interests.

Indeed, some partnerships have already begun. Canada and China are well positioned to work together on global climate resilience and sustainable development initiatives. The Canada-China Joint Statement on Climate Change and Clean Growth released during Prime Minister Trudeau's December 2017 visit to Beijing affirms that action on climate change is crucial.⁵⁸ Prime Minister Trudeau and Premier Li Keqiang agreed that intensified cooperation between Canada and China is vital to mitigating climate change and adapting to its effects around the world.⁵⁹ The commitment included concrete bilateral cooperation in the form of a Ministerial Dialogue on Climate Change and a Ministerial Dialogue on Clean Energy. The two countries also announced the renewal of the bilateral Memorandum of Understanding Concerning Environmental Cooperation and the first Ministerial Dialogue on the Environment.⁶⁰

Human rights

Despite its economic growth, China is not progressing as anticipated in terms of democratic values and human rights. While the degree of regression in democratic and human rights is sometimes subject to debate, the situation is not getting better. The jailing of human rights lawyers and the apparent creation of re-education camps for China's Muslim Uighur population are causes for concern for most Western countries.

Speaking on behalf of the Canadian Coalition for Human Rights in China, the question of whether a trade-driven approach had actually been effective in influencing human rights in China was raised. Despite these questions, the Canadian Coalition for Human Rights in China explained it is "not against" a free trade agreement between Canada and China per se if the process is in line with the following:

1. Do no harm: If pursued, a free trade agreement must respect human rights and not undermine current positions or further exacerbate shortcomings. Before beginning formal negotiations, a human rights impact assessment would be required.
2. Try to do good: Free trade agreement negotiations should be used as an opportunity to push for human rights outcomes, for example, to ratify the International Covenant on Civil and Political Rights. While success may be unlikely, the effort should be made.

China is party to five of the seven core international human rights treaties; Canada is party to six. It is important to have international commitments with which to hold signatory countries to account, human rights representatives told us. We also heard that Canadian business has its own stake in China's adherence to rights and rule of law, for example, in relation to employees they may have in China and their interest in the protection of intellectual and other property in China.

Treaty	Date of treaty	China's status	Canada's status
International Convention on the Elimination of All Forms of Racial Discrimination (ICERD)	1965	Accession by China in 1981, with reservations	Accession by Canada in 1970
International Covenant on Civil and Political Rights (ICCPR)	1966	Signed in 1998, but not ratified	Accession by Canada in 1976
International Covenant on Economic, Social and Cultural Rights (ICESCR)	1966	Ratified by China in 2001, with reservations	Ratified by Canada in 1976
Convention on the Elimination of All Forms of Discrimination against Women (CEDAW)	1979	Ratified by China in 1980, with reservations	Ratified by Canada in 1981
Convention against Torture and Other Cruel, Inhuman or Degrading Treatment or Punishment (CAT)	1984	Ratified by China in 1988, with reservations	Ratified by Canada in 1987
Convention on the Rights of the Child (CRC)	1989	Ratified by China in 1992, with reservations	Ratified by Canada in 1991, with reservations
International Convention on Protection of the Rights of All Migrant Workers and Members of Their Families (ICMRW)	1990	Not ratified	Not ratified ⁶¹

Adjustments and support will be required

If trade agreements have taught us anything, it is that adjustment assistance needs to be a part of the government's commitment to assist those harmed by a change in economic relations. This is part and parcel of making trade agreements inclusive. Adjustment policies in the past have included retraining programs to upgrade the skills of workers and incentives for industry to adapt to new circumstances. There is an obvious link here to the government's Advisory Council on Economic Growth, which made a series of recommendations to equip Canada's workforce with skills for the future, including the formation of a Canada Lifelong Learning Fund and the transformation of Canada's Employment centres.

The most classic example of a successful adjustment program is the transition of the Canadian wine industry after the Canada-U.S. Free Trade Agreement. As reported by former International Trade Minister Pat Carney, the Canadian side believed free trade in wine would wipe out 70 percent of the industry in British Columbia's Okanagan Valley, with similar results for Ontario's wine industry.⁶² But federal and provincial adjustment programs allowed producers to pull out their low-quality vineyards and replant them with higher grade grapes.⁶³ Employment in Ontario and B.C.'s wine country actually tripled between 1990 and 1995 as product quality and wine tourism soared and the industry invested in marketing itself.⁶⁴

We also heard that Canadian businesses, particularly SMEs, need more support to develop their trade competencies and export potential. This is a domestic political and economic

exigency. By focusing in particular on SMEs (which account for the vast majority of businesses in Canada yet just 25% of all exports⁶⁵) and under-represented women and Indigenous-led businesses, the government would help to ensure that the gains of deeper engagement with China will be more widely distributed. With the populist backlash against free trade in several Western democracies, there is value in broadening participation in the benefits of enhanced trading arrangements. Such measures could include helping smaller Canadian firms get onto internet selling platforms, such as Alibaba, which offer extensive reach at minimal cost; expanding the concept of sectoral selling and marketing groups, allowing companies within a sector to band together to make selling abroad more efficient and effective; specialized trade missions led by ministers, such as the first Indigenous trade mission, which traveled to New Zealand; reverse trade fairs bringing Chinese importers to Canada and exposing them to SMEs; and establishing "beyond the border" purchasing centres in Canada to reduce the paper burden for SMES seeking to ship goods.

Engagement by Indigenous communities and rural communities

Some participants noted that Indigenous communities and rural communities have the potential to benefit from further engagement with China, such as with the recent announcement of an LNG plant in Kitimat, B.C. Canada should make it a priority to share knowledge and perspectives with indigenous communities about engagement with China. We

heard that First Nations groups in B.C., for example, have been at the forefront of engagement with China. In 2011, First Nations groups throughout B.C. were receiving unprecedented inquiries from Chinese companies to develop projects on their territories. As a result, the B.C. First Nations Leadership Council presented to the federal government a seven-point action plan to seize those opportunities.⁶⁶ That strategy included promoting trade missions, expanding market opportunities and setting up a China trade desk to help First Nations respond to business opportunities.⁶⁷ Indigenous business representatives told us that First Nations communities throughout B.C. have had China strategies in place for some time, as well as their own relationships with Chinese state-owned enterprises. We also heard that some suspect China is using direct engagement with Indigenous communities as an attempt to by-pass or influence the federal government in its decision-making.

Beyond project development, there are significant opportunities for Indigenous communities and rural communities throughout Canada to benefit from Chinese tourism if empowered to do so. In addition, we heard that Indigenous communities have an important role to play in Canada's partnerships with China on environmental stewardship, including with respect to promoting sustainable growth, clean energy, sustainable fishing and the protection of the Arctic.

Canada's China capabilities need improvement

Canada needs to make major investments in capacity building to radically raise our game in terms of interacting with and understanding China. Otherwise, we engage at a disadvantage. Now is the time to act to equip future generations of Canadians to engage knowledgeably and confidently with China. It will require a concerted, long-term and inclusive effort involving all sectors of Canadian society. Suggestions included making it a priority across all government departments to upskill the public service. For example, the federal and provincial government, and indeed individual departments, should set targets for numbers of Chinese speakers in their ranks by 2025.

Although some progress was made in the federal government's 2018 budget, Canada also needs to go further in expanding our network of diplomatic and trade posts in China (and the rest of Asia). It is necessary to set up shop where we can best gain competitive advantage, which may well be in emerging Tier 1 cities.⁶⁸ The government could also consider establishing a specialized and integrated China capacity within federal and provincial governments, in the same fashion as that around relations with the U.S. This would include, for example, a section in Cabinet memoranda that discusses the implications of a policy decision on the relationship with China. Such prompting devices will eventually result in China considerations becoming ingrained in policy development discussions.

Similarly, businesses need help to understand the intricacies of how to operate in China. This could be done through greater utilization of the Chinese Canadian community, which is estimated to be four percent of the Canadian population.⁶⁹ We heard about the opportunities for the highly successful Chinese Canadian business community to mentor SMEs on doing business in China. Global Affairs Canada, in collaboration with its provincial counterparts, could also establish a regular dialogue that analyzes and draws the best practices of SME experience in the Chinese market. Whatever the specific methods, Canada needs to quickly build this knowledge; it cannot afford to be poorly informed about one of the two biggest and most influential countries in the world.

People-to-people links

There is a growing appreciation of the importance and reality of our people-to-people ties created through immigration, education, tourism and, increasingly, research. These ties will only grow, giving Canada, with its large Chinese diaspora community, an advantage over other nations. But are we leveraging these ties adequately? Chinese Canadians are a varied group. Some among the Consultative Forum believe the Chinese diaspora in Canada sees a deeper Canada-China relationship as an opportunity to do something for their chosen country of Canada and to play a positive role in deepening the Canada-China relationship. However, other members of the diaspora feel pressure from China while yet another group, particularly within business communities trading with counterparts in China, are bemused and intimidated by anti-

China sentiment. They feel unfairly stigmatized. There have also been media reports suggesting that Chinese law enforcement officials have come to Canada to covertly track down suspects accused of corruption.⁷⁰ Canadian officials have sent clear messages that policing must be conducted through the appropriate diplomatic and law enforcement channels.⁷¹

As one participant urged, we need to look at how we can best connect to the domestic Chinese Canadian community, which is young and engaged and provides a unique window of understanding and connection. At the same time, it is incumbent on the Canadian government to protect members of this community should they feel harassed or threatened while in Canada.

Bipartisan support for bilateral relations

In 1961, over the objections of the U.S., John Diefenbaker's Conservative government passed legislation to allow the sale of Canadian wheat to China, which was still under embargo by most Western countries. In 1970, Pierre Trudeau's Liberal government became one of the first to recognize Mao's People's Republic, still in the midst of the Cultural Revolution. Canadians were highly supportive, even proud, of the decision. As Paul Evans recounts in *Engaging China*, Canada's independence from, but closeness to, the U.S. were attractive to the Chinese.⁷² Six years later, Trudeau refused to permit Taiwan to participate in the Montreal Olympics when it refused to give up the name 'Republic of China.' Canadian governments later sold Canada Deuterium Uranium nuclear reactors to China and assisted in the construction of the Three Gorges Dam, with Jean Chretien a proponent of closer ties.

After initial antagonism toward China and a heavy emphasis on human rights over economic opportunity, the Conservative government of Stephen Harper ultimately came to regard China as a critical player in the global economy and an integral market for Canadian resources. The high water mark in relations probably occurred during Harper's 2012 visit to China, in the wake of concerns about President Obama stalling on approval of the Keystone pipelines: "we want to sell our energy to people who want to buy our energy," the then-prime minister said.⁷³ Canada and China signed the Foreign Investment Protection Agreement during the Harper government, which was the precursor to today's discussions of a free trade agreement, but the government also leaned against Chinese investment in the oil sands.

The current Trudeau government came to office with big ambitions and less ambivalence around Canada-China relations. But it has not made the progress it might have hoped. On a visit to China in December 2017, widely expected to serve as a launch of formal free trade negotiations, Chinese officials expressed bewilderment and dissatisfaction with Prime Minister Trudeau's insistence on prioritizing a so-called progressive trade agreement.⁷⁴ More recently, there have been indications, including the absence of the term "progressive trade" in the August 2018 mandate letter of International Trade Diversification Minister Jim Carr, that the Trudeau government is recalibrating its approach to the question.⁷⁵

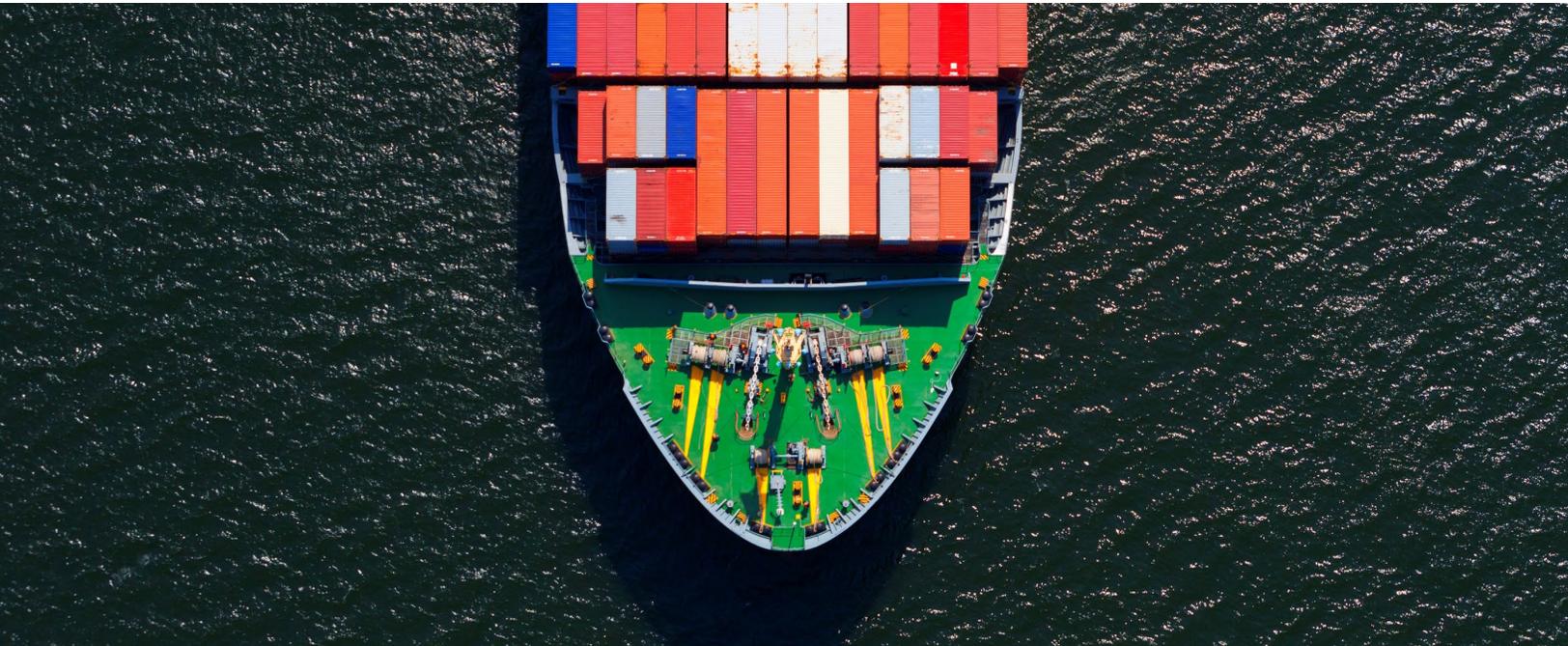
The sharp divide between the Trudeau Liberals and Opposition Conservatives over China is a

critical issue. Under leader Andrew Scheer, today's Conservatives echo many of the arguments of the early Harper era, concluding that closer economic relations with China are not in Canada's interest. As Scheer wrote in *The Globe and Mail* in 2017, "Conservatives [do not want to see](#) further concessions by the Trudeau Liberal government to conclude with a deal that gives benefits to the Chinese government, and makes Canadian workers and businesses pay the price." A lack of inter-party consensus on controversial issues make it more difficult for governments to move ahead, especially when they involve fundamental questions of national interests that will transcend the life of the governing party.

In our sessions, there was some discussion of ways to gain, at the very least, a more common appreciation of the facts and options for dealing with China. While a party has the right to adopt the policies it considers best for the country, some suggested that Canadians would be better served if designated members of the Official Opposition or perhaps members of a special Parliamentary committee were granted clearances to receive national security briefings. Whatever course they might ultimately choose once governing, they would at least arrive in office better prepared, reducing the learning curve that most governments experience on matters of state.

Arctic interests

China self-identifies as a "Near-Arctic State."⁷⁶ It casts China's interests in the Arctic into two categories: Beijing is "closely involved" in activities in the area, such as scientific research,



resource exploration and exploitation, shipping and security.⁷⁷ At the same time, climate change and its potential consequences on the region are expected to affect much of the world including China. Since May 2013, China has held observer status on the Arctic Council, an intergovernmental forum promoting cooperation, coordination and interaction among the Arctic states, Arctic Indigenous communities and other Arctic inhabitants on common Arctic issues, particularly

issues of sustainable development and environmental protection.⁷⁸ Canada voted in favour of China's application for observer status. By accepting observer status, China confirmed it will not challenge the land claims of the five Arctic coastal states (Norway, Russia, Canada, US and Denmark).⁷⁹ As China becomes more and more engaged in the Arctic, Canada will need to increase its engagement with China on this important topic.

The importance of Asian regional architecture

Some participants made the point that Canada needs to lift its game not only in respect of its bilateral relationship with China, but also turn greater—and sustained—attention to regional Asian forums and initiatives. Canada is a member of the Asia-Pacific Economic Cooperation, a dialogue partner of the Association of Southeast Asian Nations and we have now signed on to the Asian Infrastructure Investment Bank.⁸⁰ Canada has sought but to date not achieved membership in the East Asia Summit.⁸¹

Experts have told us that Asian countries tend to see Canada as either a peripatetic or indifferent partner, and this is part of the reason why we have not achieved membership in the East Asia Summit. Canada needs to demonstrate it is truly committed to the region to realise its potential as a Pacific nation—and it needs to do so with senior-level participation. Showing up is not enough. We need to be present with credibility and roll up our sleeves. That means allocating time and resources to ensure meaningful participation in the on-going conversations of the region's existing and emerging institutions. As China and Asia play a leading role on the international stage, middle-power Canada needs to have a seat—and use it—at the Asia table.

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