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Challenges Facing a Deeper Canada-EU Economic Partnership

By Angelo Katsoras

Introduction

With great fanfare, the President of the European Commission, Ursula von der Leyen, proposed in September 2026 that Canada become the bloc's first "associate member." Though no one has explained what the term actually means, it is broadly understood that the aim of the proposed partnership is to strengthen cooperation between the EU and Canada in the areas of trade, technology, defence and energy.

This report assesses the viability and potential implications of this closer partnership by examining the following:

- Canada's current trade relationship with the EU vis-à-vis the United States
- What associate membership could—and could not—mean in practice
- The economic and political challenges facing the EU
- The impact of "Made in the EU" policies

Canada's current trade relationship with the EU

For starters, it is important to note that a free trade agreement already exists between Canada and the EU. The Comprehensive Economic and Trade Agreement (CETA), which has been provisionally applied since September 2017, eliminated tariffs on most goods and reduced many barriers affecting services.

Yet nearly a decade later, CETA has yet to be fully ratified. Ten of the 27 EU member states, including two G7 economies – France and Italy – have still not completed their national ratification processes. Opposition has focused particularly on the agreement's potential impact on agriculture and concerns that its investment provisions could restrict their national regulatory powers. Until such time as all 27 member states ratify the agreement, CETA's key investment protection provisions, including the Investment Court System, cannot come into effect.¹

This unfinished business raises a fundamental question: Should Canada and the EU secure full ratification of their current agreement before pursuing a new partnership short on details? More broadly, the difficulties encountered in ratifying CETA highlight the political challenges that any new and ambitious trade agreement would likely face.

Canada's Defence Procurement Agreement with the EU comes with conditions

In a related development, Canada recently became the first non-European country to participate in the EU's Security Action for Europe (SAFE), a €150-billion loan program that finances joint defence procurement by EU member states. Access is not free, however. Under the agreement, Canadian content can account for up to 80% of a procurement's value, compared with the usual 35% limit for third-party countries. But if content from the EU, Iceland, Liechtenstein, Norway and Ukraine makes up 65% or less of the contract's value, the Canadian firm must pay a fee equal to 15% of the value of the non-European content. While SAFE could create lucrative opportunities for Canadian firms, it provides conditional, fee-based access to defence contracts. It is not free trade.²

How big is the trade relationship with the EU?

In 2025, Canada's total two-way trade in goods and services with the EU was worth \$178.3 billion, up from \$116.9 billion in 2017—an increase of about 52%.

In comparison, the value of two-way trade between Canada and the United States increased by \$358.5 billion (38.6%) over the same period, rising from \$928.5 billion to \$1.287 trillion. Although Canada-EU trade grew faster in percentage terms, the increase in Canada-U.S. trade was much larger in dollar terms. In 2025, the United States accounted for around 62.5% of Canada's total international trade in goods and services, compared with 8.7% for the EU.³

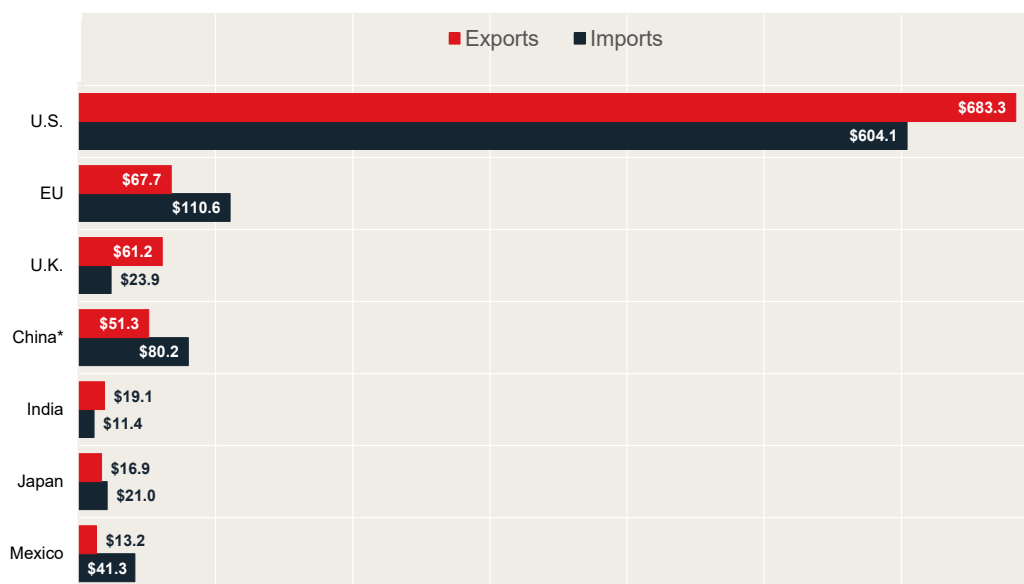
¹ "Stronger ties with the European Union aren't a lifeline for Canada," The Globe and Mail, September 18, 2026

² "Agreement between the European Union and Canada concerning participation under the SAFE Instrument," Government of Canada, 2025

³ Calculations based on Statistics Canada data reported in Global Affairs Canada, State of Trade 2026, Tables 1.4.1–1.4.3.

Canada: Top trading partners, 2025

Partners ranked by Canadian exports; goods and services (C\$ billions)



NBC Economics and Strategy (via Global Affairs Canada, State of Trade 2026, Tables 1.4.2 and 1.4.3).

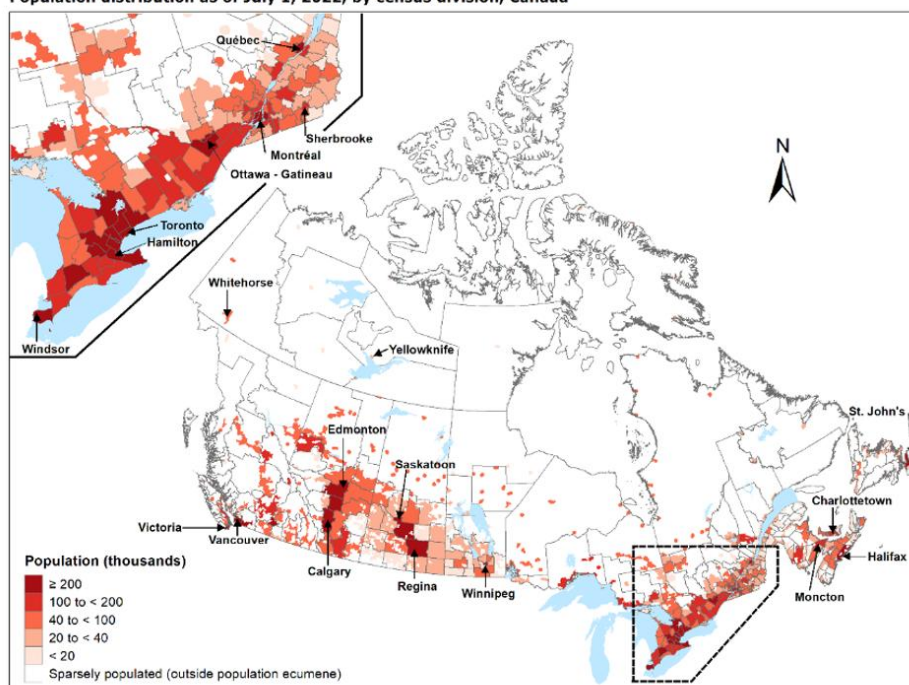
Despite that growth, Canada has recorded a trade deficit with the EU every year since CETA began to apply provisionally in 2017. In 2025, the deficit reached \$42.9 billion—\$35.5 billion in goods and \$7.4 billion in services—within a two-way trade relationship worth \$178.3 billion.⁴

The challenges of increasing trade with the EU

Geography is destiny

According to Statistics Canada: "In 2021, two out of three Canadians (66%) lived within 100 kilometres of the southern Canada-U.S. border."⁵ Geographic and population proximity to the world's largest market creates a natural pull toward economic integration. As a result, Canada's infrastructure and supply chains remain largely oriented toward north-south trade with the United States.

Population distribution as of July 1, 2022, by census division, Canada



Source: Statistics Canada, Centre for Demography.

⁴ Calculations based on Statistics Canada Tables 36-10-0023-01 and 12-10-0157-01.

⁵ "Canada and the United States: The numbers on a unique relationship," Statistics Canada, March 2023

The EU's regulatory complexity

Although the EU single market has harmonized many rules, important differences remain between member states in areas such as taxation and regulation. Not only must Canadian exporters deal with this lack of uniformity, the EU's regulatory requirements tend to be different than those in North America, especially regarding food safety and product standards.

Exports of Canadian beef and pork illustrate the limitations of market access provisions when regulatory barriers remain in place. Under CETA, the European Union agreed to grant Canada tariff-rate quotas of 35,000 tonnes for beef and veal and of 80,000 tonnes for pork. However, restrictions on hormone-treated beef and other sanitary and production requirements have severely limited exports. According to data from the European Commission, Canadian producers used only about 3% of the beef and veal quota between 2021 and 2023 and just 1% of the pork quota in 2023.⁶

Foreign direct investment offers the greatest short-term opportunity

Foreign direct investment from the EU offers one of the most immediate opportunities for Canada to deepen its economic ties with Europe. The EU is already Canada's second-largest investor after the United States, and recent policy announcements could further enhance Canada's attractiveness as an investment destination.

These include measures to accelerate project approvals and the recently announced Productivity Mega Deduction, which would allow businesses to immediately expense a wide range of capital investments. According to the federal government, these measures will reduce Canada's marginal effective tax rate on most new business investment from around 13% to 6.4%—the lowest rate among the major economies and less than half that in the United States.

Canada's top foreign direct investors

Ultimate investor country, 2025 (C\$ billions)

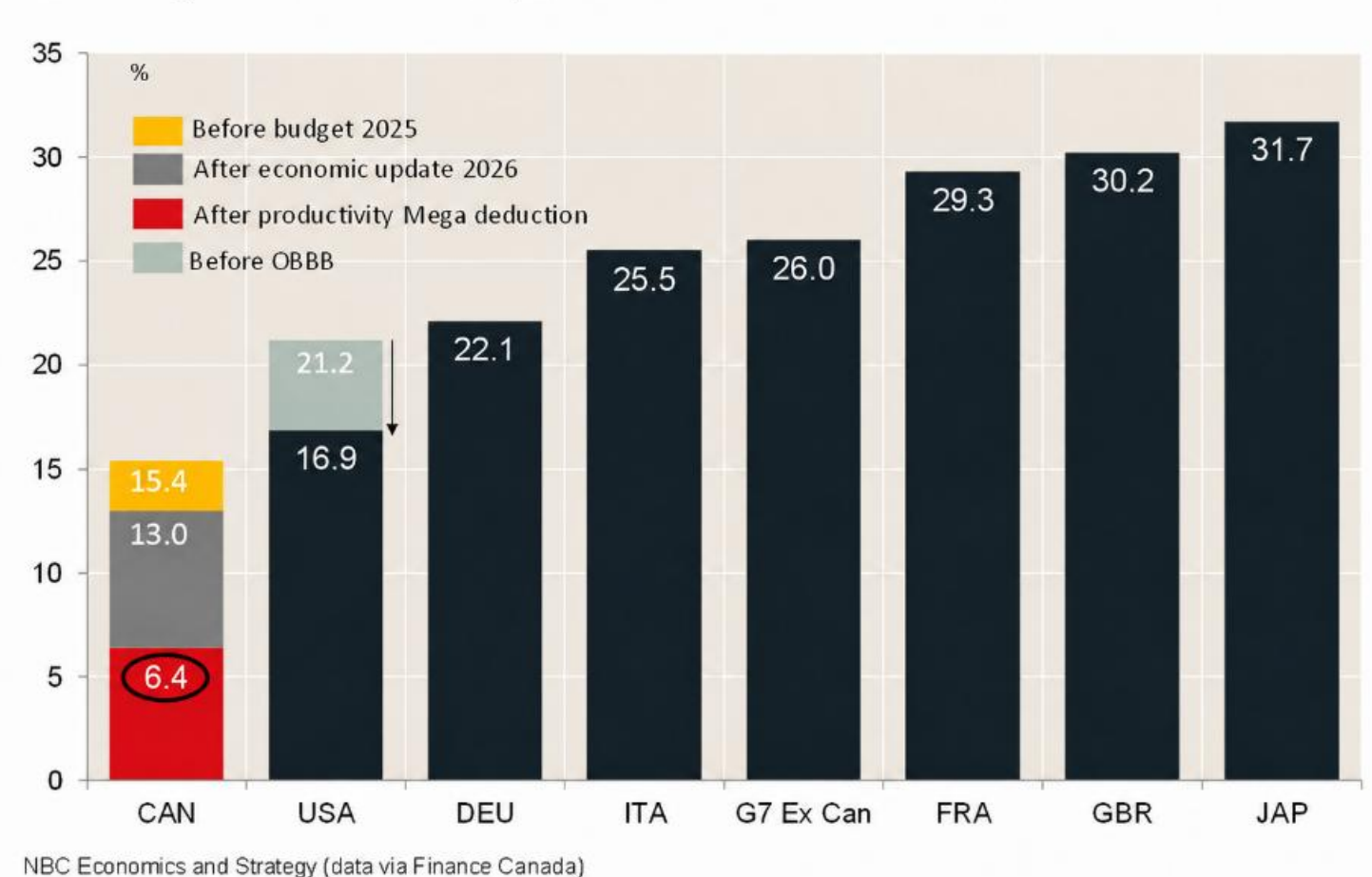


NBC Economics and Strategy (via Statistics Canada)

⁶ "Canada's bet on European trade faces plenty of hurdles," The Globe and Mail, September 21, 2026

Canada: A very attractive tax environment for investment

Effective marginal tax rate on investment, 2026



A more attractive investment climate in Canada, combined with the low tariff barriers that many countries apply to critical minerals, energy, and related industrial inputs because of their strategic importance, could help attract a greater amount of investment from the EU and other regions.

In contrast, the outlook for export-oriented manufacturing is less certain. Even with the proposed immediate expensing measure, firms may be reluctant to invest amid ongoing trade uncertainty and mounting protectionism in the United States and other countries.

What could associate membership mean?

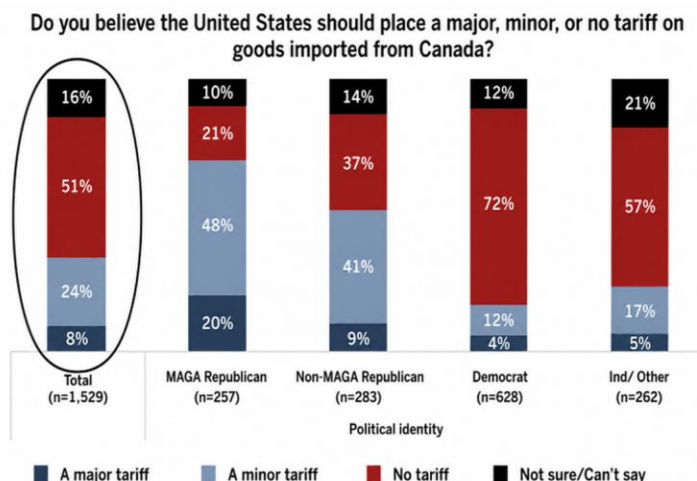
Canadian and European officials have emphasized that the proposed “associate membership” would not put Canada on a path to full EU membership. Indeed, under EU treaties, only European states may apply to join the bloc. Any arrangement with Canada would therefore have to take the form of a separate, tailored partnership. Although Ottawa has stated that it is not seeking to replicate the arrangements of countries such as Norway and Iceland, their experience provides a useful reference point.

Norway and Iceland participate in the EU single market via the European Economic Area, which facilitates the free movement of goods, services, people and capital. In return, these countries must comply with relevant EU legislation and contribute financially to certain EU programs despite not being EU members.

Such an arrangement makes sense for countries that are closely integrated with—and heavily dependent on—the EU market. Canada’s circumstances, however, are substantially different because of its geographic proximity to and deep economic integration with the United States. Moreover, a Norway-style arrangement requiring Canada to adopt EU rules without a formal vote on them would conflict with the Carney government’s emphasis on safeguarding Canadian sovereignty.

What could this mean for Canada-U.S. trade relations?

In today's strained climate, it is important to maintain a long-term perspective. President Trump's term ends in January 2029, and his successor could be more amenable to working with Canada, particularly since the majority of Americans oppose the high tariffs imposed on Canadian imports.



Two major U.S. unions call for return to 'stable' trade relationship with Canada

VANMALA SUBRAMANIAM > FUTURE OF WORK REPORTER
PUBLISHED JULY 29, 2026
UPDATED JULY 30, 2026



Sources: Angus Reid Institute, "Trump and Trade: Half of Americans Say There Should Be No Tariffs on Canada," March 10, 2026; The Globe and Mail, 2026

This presents a potential trade-off. The more closely Canada aligns its regulations and standards with those of the European Union, the more challenging it could be to maintain regulatory compatibility with the United States and negotiate the removal of certain existing tariffs under a future administration. This risk would be greatest in sectors where EU and North American standards already differ significantly.

As a recent Washington Post editorial put it: "Donald Trump is for now. A Brussels bureaucrat is forever." While this statement is deliberately provocative, it highlights a legitimate concern: How can Canada diversify its trade without adopting rules that could hinder long-term access to, and compatibility with, its largest trading partner?⁷

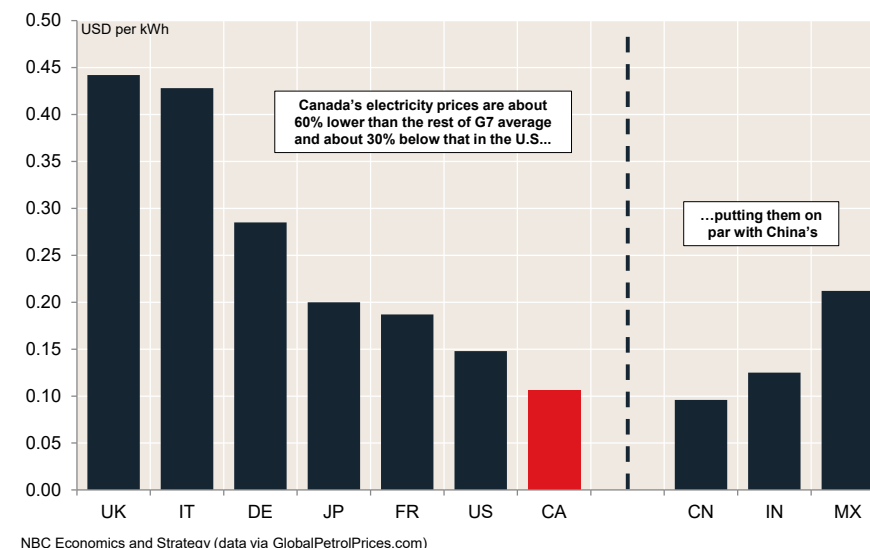
The EU's economic and political challenges

It is also important to recognize that the EU faces significant economic and political challenges that could constrain opportunities for Canadian firms.

The EU's industrial base is under pressure, particularly in energy-intensive sectors. European businesses continue to face much higher electricity prices than their counterparts in the United States and Canada. As production becomes increasingly automated and the adoption of AI expands, access to affordable, reliable electricity could become as important as labour costs in determining economic competitiveness in key sectors.

Canada: Lowest electricity prices in the G7

Electricity prices for businesses, 2023-2025 average (at market exchange rate)

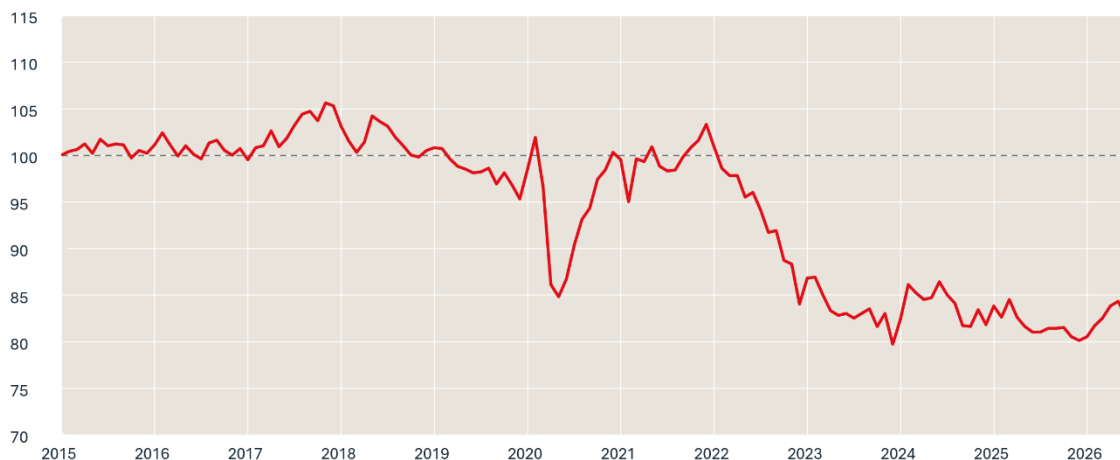


⁷ "Canada's great European misadventure," Washington Post, September 16, 2026

Germany, the EU's largest economy and a traditional manufacturing powerhouse, has been particularly hard hit by declining industrial production.

Production in Germany's energy-intensive industries has significantly declined

Production index (2021 = 100), through June 2026

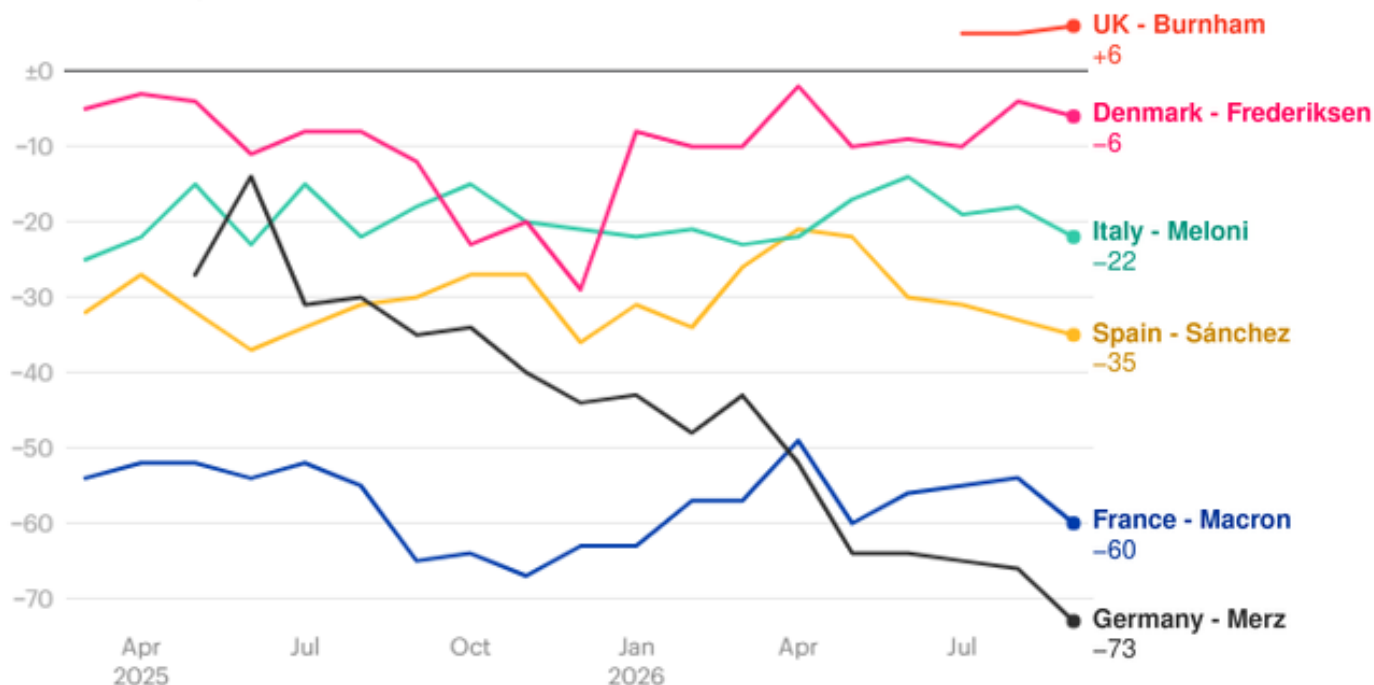


Source: NBC Economics and Strategy (Data via: German Federal Statistical Office: Destatis)

On the political front, support for mainstream parties has declined in several European countries, while parties on both the far right and far left have gained support. As a result, the political landscape has become increasingly fragmented. France is an example of this trend: President Emmanuel Macron, a close ally of Prime Minister Carney, has seen his popularity plummet. While he cannot seek a third consecutive term, his centrist movement is at serious risk of a major defeat in the 2027 presidential election. In Germany, meanwhile, Chancellor Friedrich Merz's popularity, too, has plunged to record lows, casting doubt over his political future. **This political uncertainty could hinder Canada's efforts to strengthen economic ties with the EU, especially if future governments are less supportive of trade liberalization.**

How popular are European leaders in their own countries? September 2026

Do you have a favourable or unfavourable opinion of the following? [Leader of respondent country]
Net favourability results shown



Made in the EU

That uncertainty adds to the challenge Canada already faces in seeking closer economic ties with the EU just as the bloc, like many economies, is adopting a more protectionist approach. Over the past several years, the EU has introduced a range of measures designed to strengthen domestic industry, improve economic resilience, and reduce dependence on foreign suppliers. These include:

- Carbon Border Adjustment Mechanism (2023): Applies carbon charges to selected imports.
- European Chips Act (2023): Supports investment in European semiconductor production.
- Foreign Subsidies Regulation (2023): Restricts foreign-subsidized acquisitions and public-contract bids.
- Steel Import Measures (2026): Cut tariff-free import quotas by 47% and raised above-quota tariffs to 50%.

These measures have laid the groundwork for the more stringent provisions set out in the proposed Industrial Accelerator Act. This Act would impose conditions on foreign investments over €100 million in areas such as batteries, electric vehicles, and solar power. It would also introduce targeted “Made in the EU” preferences for public procurement.⁸ Its broader objective is to increase manufacturing’s share of EU GDP from 14.3% in 2024 to 20% by 2035.⁹

Before it can become law, the Act must be approved by both the European Parliament and the Council of the European Union. Given the widespread political support for strengthening industrial capacity and reducing strategic dependencies, the legislation is likely to be adopted in one form or another.

Although these measures are intended primarily to reduce the EU’s substantial trade deficit with China, they could have implications for Canada as well. Even with a trade agreement in place, Canadian firms seeking to access the EU market may have to establish production facilities within the EU rather than solely exporting from Canada. This would mirror the pressures Canadian companies increasingly face in the United States, where local production is increasingly necessary in order to secure market access in certain sectors.

Conclusion

While the EU offers some long-term growth potential for trade and investment, its ability to replace the much larger U.S. market will likely be limited by geography, regulatory barriers, economic challenges and protectionism. Also, new political leaders in Europe could be less amenable than their predecessors to deeper economic integration with Canada.

Consequently, Canada should take a targeted approach: work with EU member states to secure CETA’s full ratification while avoiding any regulatory commitments that could complicate trade negotiations with current or future U.S. administrations.

A more immediate opportunity is to attract European investment to Canada’s resources, energy, and advanced manufacturing sectors. This includes mobilizing much-needed capital to strengthen the ports and transport corridors that support overseas trade. The Port of Vancouver, Canada’s largest port, is one indication of the logistics challenge facing this country: it ranked 375th out of 400 container ports in the World Bank–S&P Global 2025 Container Port Performance Index based on the time container ships spend docked.¹⁰

Bottom line: Despite the current trade tensions between Canada and the United States, any new economic initiative with the EU should be put to a simple test: Does it diversify Canada’s economic opportunities and strengthen its resilience without further endangering long-term access to, or prospects for improved access to, the U.S., by far Canada’s most important export market? This test is particularly important given the uncertainty surrounding the impact of emerging “Made in Europe” policies and the very real prospect of changes in government in key European countries.

⁸ “Commission proposes Industrial Accelerator Act to strengthen industry and create jobs in Europe,” European Commission Press release, March 4, 2026

⁹ “EU proposes “Made in EU” rules for strategic sectors to limit China reliance,” Reuters, March 6, 2026

¹⁰ “The Container Port Performance Index 2025,” The World Bank & S&P Global, 2026



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