

Third Draft**Speech to the Canadian Club, Toronto, 11 March 1995⁶****HON. ROY MACLAREN, FORMER MINISTER OF INTERNATIONAL TRADE**

I had intended to begin this speech with the good news. But everything about Canadian exports today is good news. Canada is well on its way to becoming the greatest trading nation on earth in proportion to population. More than one-third of all the goods and services that we now produce is exported: 37% today compared with 24% only five years ago. We Canadians export three times as much per caput as Americans, twice as much as Japanese.

All that is good news -- and there is much else besides, such as the fact that a growing portion of our total trade is now in manufactured goods, services and value-added products. But the salient question is, how did we get here and where do we go from here?

Some would suggest that the relatively low level of the Canadian dollar has been a major factor in the recent record levels of our exports. No doubt that has been helpful. The fact is, however, that the Canadian dollar declined more against the Japanese yen and the German Mark than against the U.S. dollar but that did not result in a comparable increase in our exports.

Others say that our remarkable export performance is largely the result of a more buoyant U.S. economy. Again no doubt, that has been of great help. Almost 80% of our exports now go to that single market. But the growth in our exports to other markets have been accelerating at

phenomenal rates: last year there was an increase of about 20% in our exports to Latin America and 25% in our exports to Japan; 41% with each of the European Union, and Asia-Pacific and a quite staggering 47% with China.

How did we get there? Behind the myriad of variables contributing to our export success is the central fact that the Canadian economy -- and Canada in general -- has undergone a fundamental transformation, even revolution, in the way that we relate to the world. Today we are more competitive, more productive, and, perhaps most importantly, more outward-looking than at any point in our history. Canada has quite literally turned itself inside-out.

This transformation, moreover, is not merely economic, although productivity and export growth is perhaps the most tangible measure of these changes. The real revolution is psychological. Our collective mind-set is now increasingly open, our focus increasingly global. Almost uniquely among the industrialized world, Canadians have come to recognize that the challenge of globalization is not merely to manage technological and geopolitical change but to embrace it. While some in the United States talk of building a great wall against foreign competition, Canadians increasingly talk of building bridges.

Again there have been a number of forces driving this transformation -- our historic search for counterbalances overseas, our domestic reliance on communications and transport, our growing cultural and ethnic pluralism.

For these and other reasons, Canada is emerging as one of the great crossroads of a vast global community. But perhaps the main instrument of change in recent years has been our trade and economic policy: the original Free Trade Agreement with the United States, its expansion to include Mexico, the inauguration of the World Trade Organization, and now the expansive regional undertakings in Asia, Latin America, and across the Atlantic, in all of which Canada has been a leading proponent. By bringing down the walls with our largest trade partner and increasingly with the world as a whole, we are not only gaining global access for the products and skills of our society — we are fundamentally altering our society itself.

This was not always the case. At the time of Confederation and until the 1980s much of Canada's political and economic energy was devoted to building walls against global forces, especially forces from the south. The rapid industrialization of the United States, combined with the relative economic decline of Britain, saw Canada's economic relations shift increasingly in a north-south direction. Mineral, forestry, and manufacturing products moving to the United States soon gained greater prominence than agricultural staples travelling to Europe; annual U.S. capital flows into Canada surpassed those from Britain by the 1930s and grew precipitously thereafter. Yet in many ways this growing dependency on our much larger partner to the south only strengthened the resolve to preserve our national economic space.

Trade policy served as an important tool. First and most notably, there

was Macdonald's "National Policy". Protective tariffs for secondary industry and the development of transnational railways with subsidized freight rates, were purposely intended to strengthen economic links across Canada and encourage the development of a domestic manufacturing base. In the 1930s we participated in the Imperial Preference system, partly to strengthen overseas linkages and to reduce dependency on the United States. In the 1960s and 70s we limited foreign ownership and investment in strategic Canadian industries. Even Canada's post-war commitment to multilateralism in the GATT was in many ways a reflection of our long-standing concerns about sovereignty. By attempting to trade on a multitude of fronts, and by eschewing direct bilateral ties with the United States, Canada sought both to reduce its economic dependence on a single partner and to preserve, as much as possible for a small, export dependent country, its independence and self-sufficiency.

Against this background, the decision in the mid-1980s to pursue free trade with the United States -- based largely on the recommendations of the 1984 Macdonald Royal Commission -- marked a major shift in Canada's trade and foreign policy. Most obviously, it signalled a departure from our perennial concerns about bilateralism and continentalism. Against the historic concern that a Canada-US free trade agreement would bind our economies too closely together -- harmonizing the Canadian with the U.S. (certainly not harmonizing the U.S. with Canada) -- bilateralism was now justified as the only way to deal effectively with the complexity of our transborder relationship and to provide secure access to the critical U.S. market.

Perhaps more importantly, the government-of-the-day saw the Canada-U.S. Free Trade Agreement as symbolizing a new regional or "continental" approach to Canada's foreign policy, and by extension a pragmatic lowering of our sights from the lofty "internationalism" of men such as Lester Pearson. As Dulles' famously quipped, Canada was now to be cast in the role of a regional power without a region.

But the Free Trade Agreement also transformed our trade policy in ways that were utterly unforeseen. Once Canada had decided to pursue free trade with the United States -- to open 80% of our economy to our largest competitor -- a policy of maintaining protection for the residual 20% suddenly made far less sense. Certainly the traditional role of border tariffs -- to provide protection for manufactures, to generate revenues, and to serve as "bargaining chips" in future negotiations -- was called into question. By 1998 Canada will have no tariffs on most imports from the United States -- some two-thirds of our total imports. Moreover, Canada's average MFN tariff will be reduced to around 6% when the Uruguay Round cuts are fully implemented -- 1999 for most manufactured goods and 2000 for most agricultural products.

At these low levels it is increasingly difficult to argue that border measures any longer provide either meaningful sources of revenue or protection -- excepting of course in the most sensitive domestic industries: dairy and poultry, textiles, apparel, and footwear. What's worse, these remaining tariffs can actually harm the interests of Canadian manufactures who source materials globally for export to NAFTA countries -- a growing

majority of our manufactures.

In 1994 the government embarked on a number of initiatives to reduce or eliminate tariffs unilaterally for these very reasons. We embarked upon the Tariff Simplification Exercise, the enrichment of preferential tariffs to developing economies, and, most important, the review of the adverse impact of tariffs on inputs of Canadian producers. In the past, Canada dealt with the issue of input costs on an ad hoc basis through duty drawbacks or remissions. However, the removal of drawbacks under NAFTA as of January 1 1996 called for a more systematic response. Just last year the government decided to reduce to zero the tariff on autoparts -- not only to increase their competitive edge of the so-called "transplant" automakers in the U.S. market but to ensure that Canada continued to remain an attractive location for addition investment and jobs. There are of course other sectors where duty drawback has been eliminated under NAFTA, and where tariffs might be unilaterally dropped to decrease input costs to Canadian manufacturers. But more generally we should be willing to look beyond these sectors and examine systematically our whole range of tariff and non-tariff barriers to see where inefficient domestic producers are being shielded to the detriment of our exporters.

For these same reasons, Canada now has more incentive -- and more freedom -- to pursue free trade with other partners. We have already incurred the adjustment "costs" involved in the transition to more open trade with the United States. Going the next logical step and opening our economy to other trading partners overseas would involve few additional

costs, but would place Canada in a better position to exploit to full advantage adjustments that we have made over the last seven years. Moreover, any increased efficiencies arising out of free trade overseas would serve to increase Canada's competitive edge in our principal market, the United States. Canada also has more to offer prospective partners: not just a market of 30 million, but a viable spring-board into a market of some 350 million -- a market that could very well become more restrictive to the outside world should protectionist sentiments continue to mount in the United States. Is it really too ambitious a goal to attempt to position Canada as a "hub" in a global network of free trade?

My central point is that NAFTA did not just provide for free trade with the United States; it provided an incentive to liberalize well beyond the continent -- to be "wide open" to the world. The restructuring of Canadian industry resulting from globalization and NAFTA, combined with our growing reliance upon world inputs, has fundamentally altered Canada's trade policy objectives. Canadian industries will be able to compete effectively in this new global order only if they have open access to both world markets and to world-priced inputs here at home. Economic theory has always taught that the removal of trade barriers, even if undertaken unilaterally, is preferable to protection. This is even more true in increasingly technological, knowledge-intensive economies where a society's innovation and creativity are directly linked to its openness and permeability. If a trade dependent economy such as Canada wants to attract world-class technology, investment and jobs, then there is an inherent logic in seeking to become the most open economy on the

continent.

Several years ago, I suggested that Canada should aim to become the first truly "global", outward-oriented economy in North America. By reducing our remaining trade barriers with overseas countries -- multilaterally, bilaterally, and even unilaterally -- we would increase our competitive position in the U.S. market as well as overseas -- in the same way that the restructuring arising out of the Free Trade Agreement has provided Canada with a springboard into the world market. Concurrently, the expansion of our trade overseas -- the further integration of Canada into the world economy - would serve to diminish Canada's relative dependency on the United States.

Look how far we have gone in five short years -- and look how much farther we can go. Canada's economic relationship with the United States remains the most complex and substantial among any two countries of the world. Managing this relationship -- and perhaps deepening the structures governing it -- must remain Canada's overriding economic policy priority. Although the overall bilateral relationship has been remarkably positive, careful management is required to ensure that Canadian interests are defended whenever U.S. regulators or special interests attempt to bend the rules of either the NAFTA or the World Trade Organization.

We must continue to seek resolution of various issues that currently strain bilateral relations. More importantly, we must pursue longer-term reforms to NAFTA that can close the holes in the existing structure and reduce the

scope for disputes — holes in such areas as trade remedy laws, agriculture, financial services, telecommunications, and government procurement.

In addition, Canada must continue to increase the number of our free trade partners and to improve market access for Canadian exporters. For instance, Canada is pushing at the frontiers of the Free Trade Agreement of the Americas, building on the commitments made at the Miami Summit in December 1994. One immediate proposal is to initiate discussions with the Mercosur common market countries with the goal of eventually bridging Mercosur and NAFTA.

Canada is also seeking further commitments with our partners in the Asia Pacific Economic Forum. In Osaka last year, Canada encouraged APEC members to push collectively for further liberalization at the first ministerial meeting of the World Trade Organization, while at the same time aggressively pursuing the 1994 commitment of APEC leaders to establish free trade in the region no later than by 2020.

Canada has also taken a leading role in proposing freer trade across the Atlantic, both to strengthen Canada's relations with Europe and to provide a stronger transatlantic foundation for the multilateral system. To this end, the government is examining how a transatlantic agreement might go beyond the results of the Uruguay Round in areas such as investment, technology cooperation, competition policy, and standards.

In addition to these several regional initiatives, Canada is pursuing bilateral

free trade options -- first with Israel and Chile. Although this latter initiative is designed as an interim "bridge" to Chile's full accession to NAFTA, one advantage of Canada's overture is that it will give us a greater foothold in that growing market -- and indeed in Latin America as a whole.

Finally, Canada is actively working to ensure a successful first ministerial conference of the World Trade Organization in Singapore in December. In November 1995, we hosted an informal trade meeting involving trade ministers from 14 WTO member countries. Canada is also pushing hard for the launch of discussion on investment and competition policy in the WTO, as for work on additional market access liberalization -- including the possibility of global tariff free trade by an agreed target date matching the commitments already made in APEC, in the FTAA, and perhaps transatlantically.

Canada's long-term economic interest lies above all in a strong multilateral system, just as multilateral trade and investment liberalization remains the world's first and best option. Yet over the past quarter of a century, it has become increasingly difficult to achieve swift and meaningful movement at the multilateral level, if only because of the sheer number and diversity of players. In the absence of significant momentum at the multilateral level, Canada cannot afford to stand idly by. By actively pursuing our own free trade policies -- regionally, bilaterally, and unilaterally -- we can steal the march on the global competition and help position ourselves for the barrier-free world of the coming century. With luck our initiatives might

even leverage the pace of multilateral liberalization worldwide.

My central point is that Canada's economic relations have entered a third, historic phase; one which goes beyond either the National Policy or Continentalism. The rapid industrialization of Japan and other countries of the Pacific Rim together with the resurrection of Europe has resulted in the relative decline of the importance of the U.S. economy. It would be naive to expect that there will ever be a time when Canada is not highly dependent on the U.S. economy. But it would be equally naive to ignore that the world has changed dramatically since the 1960s and 70s. Canada has greater means at its disposal now than at any point in its history to break-out its "continental" constraints and to become truly global actor.

Nor are the changes simply economic. The movement towards regional economic integration is, of course, itself part of the broader movement towards global integration. Developments in telecommunications and transport are diminishing geographic boundaries and constraints, thereby reducing the saliency of regions. This is especially true as regards trade in advanced technology industries and services. Increasingly, Canada finds itself part of a global, not merely a continental, economy. As barriers to trade and investment fall, Canada must be prepared to compete with the world's best, or risk watching our technological and productivity lead slip, and our living standards erode.

Trade policy is not the only key to this economic transformation.

Regulatory and tax policies that unnecessarily inhibit export sectors must

be revisited; regimes and restrictions that block constructive international investment -- both inward and outward -- must also be reexamined. As our economy becomes increasingly open, Canada will inevitably be exposed to greater and more fluid investment flows. We need to ensure that Canada can continue to attract the kind of high quality foreign investment that will allow us to take advantage of technology transfers, to acquire materials and skills from global markets, and to remain at the hub of international linkages and alliances.

The key to a competitive, productive economy lies in continuing to reduce government deficits and debts. Only through the kind of fiscal restraint consistently pursued by the Minister of Finance over the last several years can we ease the pressure on interest and exchange rates, eliminate the need for tax increases, and help to reinforce business and investor confidence. This can in turn allow an even less restrictive monetary policy, one that will make more accessible the capital needed for investment and help put unemployed Canadians back to work. If we are going to continue to aim for high-value, export-driven growth, then we need an economic policy that spends less on the present or the past -- using scarce resources to pay off domestic and foreign debts -- and more on investing in our future.

One observer recently suggested that Canada is rapidly evolving into a "state without walls". Indeed, there may be a peculiarly Canadian vocation in this drive for openness. As pride in our peacekeeping activities contributed to our sense of postwar achievement, today an active role in creating a world of open economic borders can underpin our national

unity. Canadians increasingly see the benefits of working together to achieve success in international markets. In doing so, they give tangible meaning to the Team Canada approach to international trade so successfully championed by the Prime Minister. It is when we in government, in industry, in all regions and in all walks of life, pull together that we demonstrate that Canada is greater than the sum of its parts. Instead of devising inward-looking policies intended to insulate ourselves from the wider world, Canada can be in the vanguard of those seeking a truly global economy -- and in so doing find an unifying national vocation.