

Another source of capital to developing countries is the issuance of equities in developed markets. Mexican firms, for example, have issued shares in U.S. stock exchanges. Shares in the Mexican telephone company -- Telefonos de Mexico SA -- were among the most actively traded on the New York exchange in 1992.

The expansion of capital markets in developing countries and the integration of developing country firms in developed markets could present Canadian firms with new trade and investment opportunities. With the availability of capital and participation in international markets comes an opportunity for developing country firms to grow. As Telefonos de Mexico grows, particularly with Canadian firms enjoying a degree of preferential access to the Mexican market under the NAFTA, we should expect an increase in telecommunications equipment trade.

4.2 The Role of the Exchange Rate

For an open economy such as Canada, the exchange rate is one of the key macroeconomic prices. The ability of Canadian enterprises to compete internationally depends on their production costs, which, in turn, depend on a number of other factors including interest rates and productivity levels, and the exchange rate. Low production costs accompanied by high levels of productivity can allow a firm to compete domestically, but without an appropriate exchange rate, the firm will not be able to compete internationally.

Two derived variations of the exchange rate that are often used to measure a country's competitive position are the effective exchange rate and the real effective exchange rate. The effective exchange rate is an index of the domestic currency price of a basket of foreign currencies, with each foreign currency weighted according to its trade share. It is a summary measure of the average cost of foreign exchange. The real effective exchange rate is an inflation-adjusted effective exchange rate. It takes into account the fact that nominal exchange rates move in response to inflation differentials between countries. Movements in the real effective exchange rate are thus often cited as indicators of change in a country's competitive position.