

Free trade policies, such as the NAFTA, encourage Canadian affiliates of foreign MNEs to rationalize their behaviour, become more productive and streamline operations. They must seek out a niche market to justify their existence or they could become redundant within the strategy of the global MNE. This increased competitiveness can have positive long-run effects on productivity and Canada's international competitiveness.

Technology

R&D is an important determining factor in export and productivity performance. Because of this, the effects of FDI on R&D are of particular interest. Government policies can exploit the potential spillover benefits of R&D performed by MNEs both in the host and home countries. Certain key sectors in which the social rates of return to R&D are highest (and there is a high foreign-owned concentration) can be targeted to maximize program efficiency. The instruments used to accomplish this can be wide-ranging, such as R&D tax incentives, educational reform, etc..

Although the relationship is not as strong as might have been suspected, foreign R&D activities are found to be complementary to domestic R&D. Transmission of foreign R&D can occur through FDI, trade and joint research. Policies that encourage freer trade, reduce restrictions on FDI, and foster international and domestic information sharing should boost domestic R&D performance.

Although R&D may be becoming somewhat more internationalized in some industries, R&D performance still remains highly centralized. Therefore, FDI cannot be considered a cure-all for domestic under-investment in technology. The quality of R&D performed by MNE affiliates is also an issue. For example, routine product testing undertaken in order to fulfil host country product or safety standards does not have the same social or industrial benefits as core R&D performed at the home base.

R&D imported from foreign countries has a lower social return, i.e., fewer spillovers, for the domestic economy than R&D undertaken either by domestic firms or foreign affiliates. Canada, therefore, should not rely solely on R&D imported from abroad to boost performance. A competitive domestic scientific knowledge base, appropriate research centres and targeted academic research should continue to be encouraged so that domestic industries can more readily absorb foreign technological spillovers and pursue R&D independently. Direct encouragement of MNEs to undertake R&D in Canada, through coercion or financial inducements, should be avoided as this diverts resources away from the pursuit of longer-term, infrastructural solutions.