

## 1. BACKGROUND AND TRENDS

### 1.1 The Canadian Automotive Sector

#### a) Overview

The Canadian automotive sector is characterized by a high degree of integration of its original equipment (OE) producers (both vehicle assemblers and parts producers) with that of the United States. Assembly has traditionally been dominated by U.S.-based vehicle manufacturers.

This integration was solidified by the signing of the Canada-United States Automotive Products Trade Agreement, commonly known as the Auto Pact, in 1965. The Auto Pact provided for duty-free trade in assembled vehicles and original equipment parts subject to certain conditions guaranteeing a minimum level of Canadian vehicle production and value-added.

Tariffs on aftermarket parts and accessories, however, were not affected by the Auto Pact. While production of original equipment has become largely rationalized on a continental basis, aftermarket production in Canada has remained to a considerable extent of a "branch-plant" nature (i.e., producing a broad range of product lines for the Canadian market only). This situation will likely change over the next several years as the Canada-U.S. Free Trade Agreement removes tariffs on aftermarket parts and accessories in five annual steps ending January 1, 1993.

#### b) Vehicle Assembly Subsector

The development of the Canadian motor vehicle manufacturing industry over the past two and one-half decades has been shaped by three principal developments:

The signing of the Auto Pact in 1965.  
The Auto Pact created an integrated

North American market for assembled vehicles and original equipment parts.

The Auto Pact paved the way for unprecedented prosperity in the Canadian motor vehicle industry. Total Canadian vehicle output, which stood at 846 000 in 1965, more than doubled to over 1.8 million by 1978 and reached a record of almost 2 million units in 1988. Employment in assembly plants grew from 34 000 in 1964 to over 50 000 by the late 1970s. Assembly employment has ranged between 42 000 and 50 000 jobs during the 1980s.

The Canadian share of North American vehicle production soared from 7 per cent in 1965 to 14 per cent in 1975, and reached 15 per cent in 1988. The Canadian share could reach 20 per cent by the mid-1990s, as a result of heavy investments by both the Big Three and Asian-based vehicle companies. Within the Auto Pact framework, Canada's favourable exchange rates, lower fringe benefit costs (due to its national health insurance system) and skilled and quality-conscious work force have helped attract a disproportionately high share of new automotive investment.

The growing market share of offshore imports. In both Canada and the U.S., the initial wave of imports was made up almost entirely of cars from Europe and the United Kingdom.

The 1970s saw the relative importance of the foreign nameplates decline until, in 1979, import penetration stood at 14 per cent, in Canada.

The most recent surge in import penetration began in 1980, triggered by rising fuel prices. By 1987, overseas-built cars accounted for 34.2 per cent of Canadian sales. This figure