1. Introduction

One of the primary characteristics that have contributed to the globalization of the world economy has been the growth in the volume of world merchandise exports that has consistently outpaced the growth in world output (see Chart 1). As well, the growth in trade in services has also outpaced world output growth. However, since 1985 foreign direct investment (FDI) outflows has significantly outpaced both exports and output (see Chart 2). The purpose of this paper is examine the relationship and linkages between trade and investment flows and provide policy considerations based on Canada's roles as a country attracting FDI, as an outward investing country, and as a trading nation in world markets.

An initial discussion is provided on the importance and impact of trade on economic growth. This is followed by examining the trade and investment linkages, with particular emphasis on causality and the direct investment impacts on the balance of payments of host and investing countries. Further to the balance of payments impacts of direct investment, the analysis examines FDI-related trade and then recalculates traditional merchandise trade balances from a residence basis (trade flows based on country of origin) to an ownership basis (trade flows based on country of ownership).

An examination of the FDI boom in the late eighties and early nineties and a discussion of the major factors contributing to this strong growth is then presented. This is followed by an analysis of intra-firm trade flows, an important sub-component of global trade flows and a direct result of FDI. The analysis focuses on Canada-U.S. intra-firm trade and the factors influencing this trade.

The Canadian experience as a host for FDI is discussed, examining the growth of FDI in Canada, the sources of FDI and the trend in foreign control of corporate assets in Canada. As well, the growth and evolution of Canadian direct investment abroad is provided. In addition, information is provided on a Statistics Canada project which will create an extensive database that will link corporations with trade and investment data.

The paper concludes with a discussion of policy considerations for Canada based on its roles as a host country attracting FDI, as an outward investing country, and as a trading nation in world markets.