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THE CANADIAN PERSPECTIVE ON FOREIGN INVESTMENT AND ENERGY QUESTIONS

An address by the Honourable Mark MacGuigan, Secretary of State for External Affairs, to the Centre for Inter-American Relations, New York, September 30, 1981

...We all know that it [Canadian-U.S. relations are] vast and complex. Today we often hear that Canadian policies are vexing the relationship. Tonight, I will give you the background to some of those policies.

My reason for wanting to provide this context or framework is a belief that unless and until Americans, both inside and outside government, appreciate more fully the rationale for Canadian economic policies, the goal of managing the relationship effectively will prove elusive. We have to understand each other, or we risk talking right past each other.

Political facts of Canadian life

Let me begin with several political facts of Canadian life. First, all Canadians think of themselves as self-appointed experts about the United States. Second, all Canadians believe they know just what needs to be done to straighten out Canada-U.S. relations. Third, while Canada-U.S. relations tend to get buried on page 48 of the *New York Times,* it is big box-office in Canada. So, we have a usual situation of perceived general omniscience on one side and relative disinterest (albeit usually benign) on the other. These are aspects of the political environment which affect the way politicians in Canada have to deal with the topic.

Precisely because it is a potentially volatile topic, a succession of Canadian governments have placed great store in conducting relations with the U.S. on a business-like and case-by-case basis. The emphasis has been on dealing with most bilateral difficulties in a direct and low-key manner, and not through negotiations in the press. Over the years, the United States has welcomed this rational, problem-solving approach, and the state of the relationship reflected this. Beyond the obvious utility of these methods, the genuine respect and warmth existing between the two peoples made such a way of doing business natural. There have been difficulties. I think of 1971 when the U.S. took a number of national economic policy decisions directed toward trade, the so-called "Nixon shock", which were nothing short of traumatic for Canadian policy-makers at the time, and which subsequently reinforced Canadian determination to strengthen national control over our economy.

But it is with a general history of co-operation in mind that I turn to a set of American concerns, some of which have recently prompted U.S. officials to express public surprise at what they call Canada's nationalist and short-sighted policies. Perhaps in the next few minutes, I can help to alleviate this apparent state of shock.

Clearly, important elements of the U.S. private sector, Congress, and administration see a disturbing change in Canadian economic policies. In addition to the words "nationalist" and "short-sighted", the terms most often used to characterize this supposedly sudden shift in direction are "interventionist", "restrictive", and "discriminatory". In the view of some prominent Americans, at least, it is no longer possible to look northward and recognize the Canada they thought they knew.

Accompanying this generalized concern in some quarters is a more specific complaint, voiced mostly by corporate spokesmen, that the "rules of the game" have been abruptly changed in Canada, and that this amounts to unfair treatment. The companies involved have not hesitated to act on their convictions and seek support in this country, often from their friends in Congress.

Alarm unjustified

This level of alarm is unjustified, but to a degree it is understandable, since the commercial and economic stakes are high. Over 21 per cent of U.S. foreign direct investment world-wide is in Canada; according to the latest available figures, this amounted to more than $38 billion. So there is a strong degree of exposure involved. But be reassured that it is two way. In 1980, two-way trade between the two countries totalled some $90 billion, the largest trading relationship in the world between any two countries. The point is that neither side wishes to jeopardize economic links of such importance.

A key to ensuring that damage is not done is knowledge. I would like Americans to know more about Canadian realities. They would then recognize that these realities are not threatening to U.S. interests but reveal a country in the process of strengthening itself, not at the expense of others, and in a way which will in fact result in a more capable neighbour and ally for this country.

What is happening in Canada is for us an exciting process — the enhancement of our nationhood. Our domestic debates over the form of our government are well known to you and have their roots in the original bargaining which led to Confederation over a 100 years ago. Perhaps less well known is the on-going debate over economic development policy which has paralleled the political discussion.

These two strands are now coming together as the constitutional issue nears a decisive stage and as the over-all direction of economic development policy is clarified. The combined effect of this "coming of age" will be noticeable to a near neighbour, but if our lines of communication are kept open, one hopes not too unsettling.

Our Prime Minister summed it up as he introduced President Reagan in the House of Commons on March 11 this year. "In the years to come the United States will be looking at a dynamic neighbour to the north. By putting its own house in order, Canada will grow confident in itself. We will establish more clearly where our interests lie and we will pursue them with renewed vigour. One thing will remain unchanged, however: our deep friendship for the United States."

Clarifying Canadian interests

What we hope our American friends will realize is that, in economic terms, this clarifying of national interest is based on political traditions and economic structures different from their own. More than 200 years ago our paths diverged, although our goals remained much the same. The parting of the ways led to different political institutions and when compared with different geographic circumstances as well, even a different attitude towards the role of government.

A good example is the degree to which Canadian governments have historically felt the need to intervene in national life to knit together and develop a huge, underpopulated and, in some cases, forbidding land. Among the results are national television and radio networks, national airlines, the Canadian National Railway family of companies and a host of other government undertakings, meant to mobilize capital, technological, and human resources on a scale of effort and risk which some of the challenges of our national development call for. The need for and familiarity with government intervention in the Canadian economy remain to this day.

I should point out that government involvement of this sort represents a pragmatic Canadian response to a particular set of circumstances, and by no means reflects any philosophical discomfort with the role of private enterprise. The private sector has been and will remain the driving force behind Canada's economic development. We share with you the perception that one of the best guarantors of a free society is a free economy. But Canadian economic development needs to be as coherent as possible and as forward looking as possible in terms of over-all benefits to Canadian society. And for those reasons, Canadian governments, at the provincial as well as federal levels, are at ease with their responsibilities for judicious intervention in the development process.

In part, this is directly due to a second fundamental difference between the two countries, the structure of the two economies. Canada's economy is a tenth the size of yours, and is more heavily dependent on primary resource industries. The manufacturing base in Canada is narrower and is significantly foreign-controlled. Although in many respects general Canadian and U.S. economic interests are parallel, in some important specific ways they diverge. In the past 20 years, the public debate on the degree to which such a divergence was desirable or possible has centred on the question of foreign ownership.

Foreign investment

While Canadians acknowledge the benefits which foreign investment has brought them, it became clear by the beginning of the 1970s, after a decade of study, of the very high degree of foreign ownership and control and that there were very significant costs involved as well. These are well known; they relate to the negative effects on the performance of the economy of locating so many of its command centres outside Canada, on the social development of Canada, which needs more research and development for our engineers and scientists; or the effects of the branch-plant phenomenon on the Canadian potential for developing interesting trade prospects. And so on. And the events of 1971 left us feeling suddenly vulnerable.

Accordingly, in 1974, the government established a foreign investment review process whose task is to screen foreign investment for significant benefit to Canada. You will notice that I used the word "screen", not "block". As of August 1981, the Canadian government had an approval rate for applications by American investors of 90.5 per cent, hardly grounds for suggesting that they have been subjected to harsh treatment.

In view of the litany of complaints about the Foreign Investment Review Agency (FIRA), I would like to point out a few facts. Even now, after seven years of the FIRA regime, foreign ownership figures in Canada are at a level which I am sure you will agree would simply not be tolerated in the U.S. For example, according to latest available figures (1978), foreign investment in the United States accounted for 5 per cent of the mining industry and 3 per cent of the manufacturing sector. The comparable Canadian levels are 37 per cent and 47 per cent. The contrast is stark.

Furthermore, in 1978, non-residents controlled about 30 per cent of all non-financial industries in Canada; the comparable U.S. figure was about 2 per cent. Finally, while only two of the 50 largest firms in the United States are foreign-controlled, 19 of the 50 largest firms in Canada are foreign-controlled.

I regret bombarding you with these statistics, but I believe that the reason for Canadian action on foreign investment must be clearly understood. No country could allow these levels of foreign involvement to continue indefinitely. No country ever has. I do not have to remind this audience of the more recent reaction in this country to a degree of foreign penetration much, much lower than that occurring in Canada.

The essential point is that, having determined that the amount of foreign ownership and control was a concern, Canada chose to deal with the problem totally in accordance with our international undertakings. There has been no question of nationalization, confiscation or forced sale. Foreign investors have simply been told the conditions under which they would be welcome.

And I should emphasize the notion of welcome. Canada needs and wants foreign investment which will benefit all parties concerned. Foreign companies and individuals will continue to do business profitably in Canada. I do not believe that those who are complaining about our policies are in fact arguing that they have lost money on their investments. Certainly not. And by comparison with other countries, there are very few more secure places to invest money than Canada.

Energy issues

Let me now turn to the vexed question of energy. In the energy field, the cause of much recent anxiety has been Canada's National Energy Program (NEP). Within the context of the obviously special significance the energy sector has for Canadian economic development, that program is founded on three basic principles — security of supply and ultimate independence from the world oil market; opportunity for all Canadians to participate in the energy industry, particularly oil and gas, and to share in the benefits of its expansion; and fairness, with a pricing and revenue-sharing regime which recognizes the needs and rights of all Canadians, with respect to the development of all of Canada's regions.

From where I sit, one aspect of the NEP which has been much misunderstood is "Canadianization". The Canadianization objective is really very simple: it is to increase the share of the oil and gas industry owned and controlled by Canadians — to 50 per cent of the industry a decade from now. In the strategy adopted to achieve this utterly legitimate objective, the emphasis is on making room for Canadian oil and gas companies in the industry in Canada, not on forcing out foreign companies. There is no question that we intend to give Canadian companies the opportunity to grow more quickly. What we have not intended or done is to make the operations of large international oil firms unprofitable. For example, the net cost to U.S. firms exploring in Canada will remain lower than in the United States.

But we are dealing with an extraordinary situation. Throughout the 1950s and 1960s, non-residents owned nearly 80 per cent and controlled over 90 per cent of Canadian oil and gas assets. They also controlled nearly 100 per cent of the assets employed in refining and marketing operations. Canada did not have a single Canadian multinational oil company, not even a small one. We did not have a vertically integrated domestic company, until Petro-Canada acquired Pacific Petroleum in 1978.

Before the NEP, an unintended by-product of government policies was increased foreign ownership. New windfall profits due to increases in oil and gas prices favoured the firms already in the business with the largest production. Most of these were foreign-owned. These same foreign-owned firms were also the main beneficiaries of the earned depletion allowance, since this deduction from taxable resource income was available only to firms whose principal business was resources and who had existing resource income. The pre-NEP policy framework virtually guaranteed that the big (and the foreign-owned) would get bigger.

The Canadian predicament

No other developed country faced this predicament. Indeed, as I look around, it is a predicament tolerated by no country, period. By 1980, the 74 per cent foreign-owned and 81.5 per cent foreign-controlled Canadian oil and gas industry generated almost a third of all the non-financial sector profits in Canada. Without changes, enormous power and influence in Canada was destined to fall into a few foreign hands. We simply decided that we had to act and had to act now.

But, unlike some other countries, Canada has preferred the carrot to the stick. The operations of foreign firms in Canada are still very profitable and, to the extent that they increase Canadian ownership, they can now be even more so.

I want to dispel any impression that the NEP has suddenly made the role of foreign firms in the Canadian hydrocarbon industry uncertain and unpredictable. Certainly the rules of the game have changed from 10, 20 or 30 years ago. Perceptions change; needs change; situations change. Where do they not change? But the changed rules are clear. They can be ignored to the detriment of future balance sheets. Or they can be used advantageously by foreign-owned corporate citizens of Canada who are sensitive to the Canadian environment and to the opportunities there for profitable investment.

Incentives for owners

I should add that the NEP gives foreign companies an incentive to acquire Canadian shareholders and partners. To the extent that they do, they can benefit from higher exploration grants just like firms which are already more than 50 per cent Canadian-owned. Let's not forget the many foreign-controlled companies who are quietly rearranging their affairs in Canada to take advantage of the NEP, and in so doing, to continue to grow and prosper in Canada.

Before leaving the subject of Canadian energy policy, let me deal with an assertion often made about another aspect of the NEP's impact. I have seen it claimed that the recent takeovers of foreign-controlled Canadian oil and gas subsidiaries by Canadians have been at "fire-sale" prices caused by the NEP.

In fact, the biggest single takeover since the NEP, the purchase of Hudson's Bay Oil and Gas from Conoco, was at a price that Conoco itself has termed fair and reasonable. The price included a premium of 52 per cent above the pre-NEP stock market price. The highest premium of all, 67 per cent, was won by St. Joe's Minerals for the alleged "forced" sale of Candel Oil Limited, in order to ward off a takeover attempt on St. Joe's itself. Not bad business for an alleged shotgun wedding. In comparison, the average premium in over 60 takeovers in Canada since 1978 was 35 per cent. Indeed, the government in Canada has consistently been criticized for Petro-Can purchases on the grounds that the premiums paid have been too high.

One last note — the takeover fever in Canada began long before the NEP. It has had involved Canadian as well as foreign firms and sectors beyond energy. I suggest that some recently interested observers of Canada step back a bit for a little perspective.

I have taken some time tonight to discuss Canadian investment and energy policies. I did so because these are areas of concern to many in the United States, and this seemed a good opportunity to explain the Canadian position before a largely American audience. I would not like to leave the impression, however, that these American concerns and our responses define the state of relations between us. The United States' own record on trade and investment is not unblemished. Measures have been taken, for example, to assist industrial sectors having difficulty meeting international competition. Buy-American preferences abound. There are sectors of the U.S. economy from which foreign investors are excluded. We are still awaiting action on shared environmental and fisheries issues. Raising these problems gives me no pleasure. It does, however, help to put the bilateral situation into better perspective.

Let me conclude these remarks by returning to a point I made earlier. For Canada, the state of relations with the United States is a crucial matter, full of political sensitivity. Energy and investment questions lie at the heart of the relationship between our two countries. The Canadian government has developed policies in these areas which command broad national support. The government has sought to take American concerns into account (we amended provisions of the NEP, for example), but the main lines of our policies are set. They are set because they correspond to the firm wish of the people of Canada. They are in the political mainstream, and also in the mainstream of a larger, wider current of Canadian economic and political history.

Long-term policies

Let us be clear about this. Contrary to a recent Atlantic Council report on the subject, the Canadian policies in investment and energy are not the product of short-term political expediency. The genesis of these policies can be traced back through at least two decades of spirited and intensive national debate. It would be a mistake to suppose that a Canadian government would be able or willing to resist the historical momentum of our country's growing determination to have the necessary amount of control over its own destiny.

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Recriminatory rhetoric will get us nowhere — except into a more excited and more nationalistic home environment.

It is the reality of the Canada-U.S. relationship that two different countries can grow separately in their own ways, yet retain bonds of friendship and respect through a common heritage of basic values — the sort we have protected together in two world wars, in Korea, in Iran, in the North Atlantic Treaty Organization (NATO) and the North American Aerospace Defence Command (NORAD). Those values find their ultimate expression in the countless personal links which are the fabric of our relations. In the long run, those values and those personal links define the quality of our relationship.

Canada and the United States have followed distinct paths from the beginning. Our challenge has always been to contain and channel our disagreements so that they did not impede the steady flow of friendship. We must continue to accept this responsibility.

But we must do more. We must visualize our relationship, including our problems, in a world perspective, in a world of general turbulence in which like-minded countries are few enough that we cannot afford to be distracted from achieving together our common goals of freedom, justice, democracy, and friendship among all peoples.

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