Department of Foreign Affairs and International Trade

Statement

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NOTES FOR AN ADDRESS BY

THE HONOURABLE ROY MACLAREN,

MINISTER FOR INTERNATIONAL TRADE,

TO THE ANNUAL GENERAL MEETING OF

THE CANADIAN BANKERS' ASSOCIATION

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Canada

One of the great economic triumphs of the last 50 years has been the liberalization of international trade under successive Rounds of the GATT [General Agreeement on Tariffs and Trade]. But there has been another process of liberalization which is at least as dramatic as the globalization of trade, and which has taken place largely outside the formal negotiations or international rule making — that is, the liberalization of global capital flows.

These two developments are not unrelated. The systematic reduction of trade barriers worldwide, combined with dramatic decreases in transport and communication costs, has paved the way for the emergence of a truly global system of production — one in which firms are increasingly free to assemble inputs from around the world and to service an equally global marketplace. This in turn has accelerated the globalization of investment, as firms learn that the best way to achieve a comparative advantage in production, in sourcing, and in technology is to establish a direct presence in foreign markets.

Where once trade was about the exchange of goods among national firms operating in national markets, today trade is much more about the movement of components, services and technology within global firms operating in global markets. Where once foreign investment was seen as a way of substituting for trade — a way of jumping over national barriers — it is now seen by many firms as a necessary precondition; to the point where trade and investment are virtually indistinguishable.

Production by foreign affiliates has now overtaken exports as the primary means for delivery of goods and services to foreign markets. Behind this dramatic growth in foreign investment is the so-called transnational corporation. In the 1990s, some 37 000 such corporations generated US$4.8 trillion in sales, accounting for one third of the combined outward investment of their countries of origin, and generated — directly or indirectly — some one third of world output. Taken together, roughly one third of all trade takes place among branches or affiliates of individual firms.

The implication of such numbers is clear. Global investment is becoming at least as important to Canada's economic future as is global trade. Or to put it another way, in order to advance the goals of greater employment and growth, Canada must be a home to firms with global operations and global aspirations.

Though such observations may seem axiomatic to businesses confronted daily with the strategic challenge of positioning themselves in a global economy for global competition, they represent nothing less than a sea change in the way Canadian governments have traditionally viewed foreign investment.

This sea change has given rise to two policy imperatives. First, we have come to the realization that the central problem facing Canada in the 1990s is not how to screen foreign investment, but how to compete for it. The fact is that investment is a finite pie. More and more nations want a slice.

Canada is facing mounting competitive pressures to attract foreign direct investment not simply because of a growing recognition worldwide of the jobs and technology that such investment can bring, but because dynamic economies in Asia, in Latin America and in Central and Eastern Europe have become such attractive magnates for investors. Although there will always be key sectors and key institutions that must remain in Canadian hands, it is clear that increasingly government's role is as a facilitator, rather than an impediment, to foreign capital.

It was largely in recognition of these changed circumstances that the more stringent review process for foreign investment under the Foreign Investment Review Act — or FIRA — was replaced by the Investment Canada Act in the mid-1980s. The objective now is to promote most types of foreign investment through an active program of marketing Canada as an attractive investment location — an increasingly critical activity when an estimated 9000 other jurisdictions worldwide are touting their own perceived attractions to international business.

More importantly, policy makers have become increasingly conscious of the need to get Canada's economic fundamentals right if we are to retain and expand foreign investment — messages quickly reinforced by the Moodies of this world, if not by the apocryphal 20-something bond trader in red suspenders. After all, firms do not decide to invest in a market simply because of favourable investment regimes. They decide to invest on the natural assumption that they will receive an adequate return on their investment.

Because of this, Canada needs to offer more than an attractive and stable regulatory environment, important though that is. We need to offer fiscal policies that complement our investment goals — and this means continuing to pursue the reduction of deficits and ultimately debt at all levels of government.

The second policy implication of globalized investment is the more radical: that Canada should be encouraging outward — as well as inward — investment if we want to build bridges to the emerging global economy. After all, the same logic that argues for a greater foreign presence in Canada also argues for a greater Canadian presence abroad. For many Canadian firms — particularly those in the service sector — the best way to access a foreign market is to establish an investment foothold in that market.

These firms also want the kind of access to capital and technology that only a direct market presence or more intensive business linkages can bring. And they want to establish production and distribution networks closer to their customers, either through direct investments in local facilities or through strategic alliances with existing firms. For many firms, foreign direct investment has become the critical linkage between Canada and the global economy of the 1990s — a calculation reflected in the fact that Canadian investment abroad has risen to about $125 billion in the last several years, and indeed has been growing faster than inward investment for two decades.

Despite the growing momentum for investment liberalization worldwide, Canadian businesses still face obstacles, especially in key developing markets. There are concerns about the transparency of regulations, about performance requirements, and about the procedures for purchasing existing enterprises. Problems are also encountered in the management and direction of foreign investments, as well as in the repatriation of funds. Rules on expropriation, including commitments for fair market value compensation, are also needed. And outside of NAFTA [North American Free Trade Agreement] countries, there is no legal forum or dispute settlement procedure for investment to match what we have already accomplished in trade. Finally, Canadian businesses want to compete on a level playing field with investors from other countries or with domestic suppliers — in trade policy language, they want most-favoured-nation [MFN] status and national treatment.

If trade and investment are two sides of the same coin, then ideally what we need is a set of rules providing a seamless web of protection for all global economic transactions, whether trade or investment. Unfortunately, the new World Trade Organization [WTO] falls short of this ideal. Some disciplines related to market presence are incorporated in the proposed services agreement or what is known as the GATS [General Agreement on Trade in Services]. A few disciplines on such issues as local content rules are included in the Trade Related Investment Measures — or TRIMs — agreement.

There continue to be efforts to gain greater access for our financial services and telecommunications sectors through ongoing negotiations in Geneva. However, this patchwork quilt is scarcely enough for today's world of increasingly integrated investment and trade activities, let alone for tomorrow's.

In the absence of a more universal regime, Canada has so far pursued a multi-track approach to rule making. The first "track" has been an extensive program of bilateral negotiations on Foreign Investment Promotion and Protection Agreements — or FIPAs. As you know so well, FIPAs help to promote foreign investment by lowering the non-commercial risk faced by Canadian companies investing in certain countries. Among other things, such agreements include legally binding obligations to protect against expropriation and restrictions on the transfer of funds, enforceable through a dispute settlement provision.

The focus of our negotiations has been on developing countries and economies in transition in Asia, in Latin America and in Central and Eastern Europe. These priorities are shaped by a combination of economic and political factors, including an analysis of the current and forecasted level of Canadian investment interest in a particular country and the attendant risks of investing there.

Canada has FIPAs in force with Russia and all the signatories of the Commonwealth of Independent States, with the Czech and Slovak Republics, and with Poland, Hungary and Argentina. New FIPAs were signed recently – and will soon be in force – with Ukraine and Latvia. FIPAs will likely be signed in the next several months with Trinidad and Tobago, Peru, Ecuador, and Venezuela.

Negotiations are also under way with China, India, Hong Kong, Colombia and Kazakhstan, and several are being planned with some seven other priority countries. We shall continue this program as long as it is needed – which means at least until developing countries choose to participate more fully in multilateral rule making on investment.

Another important track for Canada is the NAFTA, which already includes substantial disciplines on investment. Here the path to expansion lies with the accession process – a process soon to be tested with Chile. Chile is important not only because it represents a key destination for Canadian investment in its own right, but also because the Chilean market serves as a springboard into the rest of the continent.

For this reason, we are also working to ensure that investment disciplines become part of the discussions for an Americas Free Trade Area, which is attempting to develop free trade among countries in our hemisphere by the year 2005. And we are undertaking discussions on guiding principles for international investment with other countries from the Pacific Rim under the Asia-Pacific Economic Co-operation forum [APEC].

Finally, in Paris last month, ministers from the OECD [Organization for Economic Co-operation and Development] countries launched negotiations for a Multilateral Agreement on Investment – or a MAI. The key objective is to attain a high-standard investment agreement with respect to access, protection, and dispute settlement among all OECD countries – countries which, of course, are among Canada's major investment partners.

A number of new issues – issues not currently covered by any type of existing agreements – will be on the table. For instance, negotiators will likely address the potential abuse of national security-based exceptions to the principles of MFN and national treatment – especially when such exemptions can be used to restrict access to government-supported technology programs. This form of "technological protectionism" is of particular concern to Canada, given the vulnerability of our high-technology firms in the United States, Europe, and Japan.

Another subject of negotiations will be extraterritoriality – the ability of a country to reach beyond its borders to apply its laws and regulations to the international operations and affiliates of firms headquartered in its own territory.

More ambitiously, negotiators may look at the interface between foreign investment and private business practices – the way complex financial and commercial linkages among firms can often impede market entry through investment. It is difficult to exaggerate the complexity of this issue – an issue which goes to the heart of the way national economies, and indeed societies, are structured; yet it remains true that disciplines in this area would greatly facilitate access to key markets such as Japan and even Germany.

In the end, however, there is a major shortcoming in the OECD negotiations – the lack of participation of developing countries. After all, these same non-OECD countries last year accounted for over 40 per cent of all foreign direct investment – up from 18 per cent in 1985 – and this proportion can only grow.

More important, it is in many of these countries that investors have the greatest need for binding protection, ease of access, and transparency of regulations. There are consultative mechanisms that might be established for non-OECD countries as negotiations progress; we shall also need to ensure that the final architecture is kept open to eventual accessions. But if we are living in a world in which investment is truly global then any meaningful OECD investment agreement must eventually be anchored in the WTO – perhaps as the catalyst for the first WTO Round.

How does all of this affect Canada's financial sector? You too are service providers in an increasingly porous and competitive global marketplace. You represent an essential link in Canada's productivity chain. And you are not immune to the larger forces at work in today's global economy.

As you are all too well aware, the Minister of Finance and I rarely waste an opportunity to ask what role Canadian banks are playing in facilitating Canadian business performance internationally, particularly the performance of our small and medium-sized enterprises. But tonight I also want to express my interest in the global viability and competitiveness of the Canadian banks themselves. No one can afford any longer to be strictly domestic players, least of all institutions that play such an essential role as financial intermediaries.

Thank you.