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Different Strokes:

Regionalism and Canada's Economic Diplomacy

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Canada

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DIFFERENT STROKES:

REGIONALISM AND CANADA'S ECONOMIC DIPLOMACY

Executive Summary

In the post Cold War era, economic diplomacy matters more than ever, especially for a middle-sized, open and trade-dependent economy such as Canada. This Staff Paper reviews Canada's economic relations with the major regions and attempts to identify critical emerging trends.

The Paper focuses on long-term changes in export market shares, investment (both direct and portfolio) patterns, research and development activity, and trade policy developments of interest to Canada. The strategic impact of the NAFTA on Canada's economic diplomacy is discussed, especially in light of the growing importance of the Pacific Rim and Latin America. The NAFTA can assist in achieving improved access to a number of regional markets. It should also be viewed as an important instrument for encouraging a negotiating dynamic over the medium to longer term that can address Canadian economic interests in Japan and the EC, as well as with regard to further securing access in the U.S.

Broadly stated, the Paper indicates that Canada's ties with Europe have loosened over the past generation, but that the financial and personnel resources that the federal government dedicates to trade and economic relations with Europe are still proportionally greater than merited when compared to the increasing importance of the Pacific Rim and Latin America for Canada's trade and trade policy agenda. Other elements of Canada's economic diplomacy (aid, environmental cooperation) should also take Latin America and the Pacific Rim into greater account. The Paper reaffirms that economic relations with the U.S. remain critical to Canada's well-being, although the level of resources dedicated to that task does not appear lacking. More emphasis on trade policy (as distinct from trade promotion) might be merited with regard to the U.S., given the heightened importance of trade rules embodied in the FTA and the NAFTA for the management of this special bilateral relationship.

Résumé

En cette époque de l'après-guerre froide, la diplomatie économique revêt de plus en plus d'importance, en particulier pour un pays de taille moyenne, ouvert et tributaire du commerce comme le Canada. Le présent document passe en revue les relations économiques du Canada avec les principales régions du monde et tente de définir les grands courants qui se dessinent.

Le document traite essentiellement des changements à long terme concernant les parts des marchés d'exportation, les types d'investissement (direct et de portefeuille), les activités de recherche et de développement ainsi que les nouveaux facteurs de la politique commerciale présentant un intérêt pour le Canada. Les répercussions stratégiques de l'ALENA sur la diplomatie économique du Canada y sont abordées, surtout en fonction de l'importance croissante des pays riverains du Pacifique et des pays de l'Amérique latine. L'ALENA peut faciliter l'accès à un certain nombre de marchés régionaux. Il devrait aussi être perçu comme un instrument privilégié pour encourager à moyen et à long terme des négociations où le Canada pourrait faire avancer ses intérêts économiques au Japon et dans la CE tout en renforçant son accès au marché américain.

En termes généraux, le document indique que les liens que le Canada entretient avec l'Europe se sont relâchés au cours de la dernière génération, mais que les ressources financières et humaines que le gouvernement fédéral consacre aux relations commerciales et économiques avec l'Europe demeurent disproportionnées par rapport à l'importance croissante des pays du Pacifique et de l'Amérique latine au chapitre des échanges et de la politique commerciale canadienne. Ces pays devraient en outre influer davantage sur d'autres éléments de la diplomatie économique canadienne, notamment l'aide et la coopération en matière d'environnement. Par ailleurs, le document réaffirme que les relations économiques avec les États-Unis demeurent un élément essentiel de la prospérité du Canada, et constate que les ressources qui y sont consacrées ne font pas défaut. En revanche, il serait justifié de renforcer la politique commerciale (qu'il faut distinguer de l'expansion du commerce) à l'égard des États-Unis, étant donné l'importance accrue des règlements commerciaux énoncés dans l'ALE et dans l'ALENA pour la gestion de ces relations bilatérales spéciales.

1. Introduction

The purpose of this Paper is to stimulate discussion about choices.

~~The end of the Cold War has~~ removed a major ideologi~~cal barrier to the~~ further integration of the world trade and payments system. The present sunsetting of central planning and the stark demythologizing of the workers' state have led to a consensus on the substantial merits of the market economy. The growing pains of transition reflected in the resurgence of very localized (and peripheral) nationalisms (as the glue of Soviet imperial totalitarianism has dissolved) do not seriously detract from the impact of this broad, new reality. Moreover, the growing acceptance of market forces has strengthened the trend toward deepening cross-border economic integration reflected in flows of goods, services, investment and technology that have increased at rates that have consistently outpaced growth in domestic economies over the past generation. In turn, increasing cross-border competition and integration continue to create further pressures for minimizing substantive differences between jurisdictions in many areas that most policy makers had considered quintessentially domestic and local in the past. In this context, economic diplomacy matters more than ever.[1]

Yet, perhaps we have become overly mesmerized with the stunning collapse of central planning and the seemingly inexorable logic of economic globalization. Neither of these shifts are necessarily permanent nor complete. Neither necessarily drives a middle-sized country such as Canada to be everywhere at the same time to the same degree. Neither conveniently releases us from the heavy, but critical task of making choices.

There is considerably more nuance behind "Going Global" than the phrase implies on the surface; or at least there should be. Most Canadian economic welfare is generated domestically, while much of the important growth created by cross-border trade and financing occurs sub-regionally and regionally within North America. On the other hand, we can identify valuable market niches elsewhere, while an open economy in Canada is essential to providing the competition needed to ensure that growth continues to be dynamic. This dynamism, in turn, is central to attracting quality investment and technology from whatever source. We have made and should seek further important marginal (in the economists' sense) gains in welfare through improved trade and economic relations with key countries in other regions.

[1] For further background, see Keith Christie, "Globalization and Public Policy in Canada: In Search of a Paradigm", Policy Planning Staff Paper 93/01, January 1993.

This paper deliberately does not focus on the multilateral trade negotiations (MTN). The successful conclusion of the MTN and the launching of a subsequent Round before the end of the decade must remain key Canadian objectives. Even a modest MTN package will bring useful market access gains for Canada, will contain improved disciplines on the use of trade rules (especially with regard to subsidy/countervailing duty practices) and, perhaps most importantly, will preserve a meaningful multilateral option to serve as a necessary backdrop to further regional integration. Nonetheless, much of the dynamism in international economic relations is now, and will continue to be found at a less "global" level. Regionalism matters and requires choices that are as forward-looking and dynamic as the economic changes that are occurring.

In the end, the ultimate strategic goal for a middle-sized, open and trade-dependent economy must be global access and globalized rules of the game that reflect our needs and circumstances in order to underpin domestic economic growth. Yet Canada's strategy for making these gains is surely an empirical, practical matter, especially over the next decade or so during which severe fiscal restraints will continue to govern the use of scarce financial and human resources by governments in Canada.

How can we best use scarce resources abroad? How do we build on evident regional strengths to achieve further "marginal" gains more "globally"? What follows represents a preliminary attempt to identify at least part of the answer to these questions. The full answer will determine the shape and direction of Canadian economic diplomacy over the next decade, as we seek to underpin growth in Canada, to limit the dangers of inward-looking blocs, and to prepare for the ever more ambitious and intrusive trade and economic policy agenda that lies just around the corner.

2. Europe: The Loosening Ties

Our economic relations with Europe merit a hard, critical look. Despite Canada's deep European roots, both Europe and Canada have changed enormously over the past generation. These changes have affected considerably the global context within which Canadian economic diplomacy must function effectively.

The movement toward European economic and political consolidation is an important and positive process in terms of securing long-term peace and prosperity within the Old Continent. We should wish them well. Nonetheless, European consolidation on the economic and trade fronts will tend to be, by and large, an inwardly focussed process into the foreseeable future. Europeans are rightly preoccupied with the complex legal, economic, political and cultural dimensions of creating a common home that extends through eastern Europe and beyond to include closer links with Africa and the Middle East.

The ties of kith and kin across the Atlantic remain; but they are becoming noticeably more tenuous. In the 1960s, over 70% of immigrants to Canada came from Europe. The proportion has declined steadily ever since, dipping below 20% in 1992. In contrast, Asia provided less than one-tenth of our immigrant intake a generation ago, compared to more than half in recent years. The proportion of newcomers from Latin America and the Caribbean has also increased, from less than 5% to about 16% today.[2] Most of Canada's population still has European roots, but these now tend to be less immediate and directly felt on the personal level compared to the still fresh and quite different ties of those who have arrived more recently.

The full relocation to Canada of our NATO forces based in Europe, which brought few if any economic benefits to Canada in any event, closes an expensive yet increasingly symbolic chapter to Canada's trans-Atlantic connection. Redeployment to Canada is well underway and will be completed by early 1994. Canada's current peacekeeping presence in the Balkans may last longer than we hope. Nonetheless, it reflects more a continuation of a long-standing commitment to making the U.N. system work wherever needed, rather than of a "European" policy <u>per se</u>. In any event, peacekeeping within Croatia and Bosnia, while important in its own right, is qualitatively less than sharing the burden of front-line defence in mainstream Europe against Soviet expansionism.

Despite considerable effort and the many personal contacts, other trans-Atlantic links continue to weaken. Intra-European trading preferences and industrial rationalization, increasing integration within North America (led by private industry and strengthened by the FTA and NAFTA), and economic dynamism in east Asia have created important shifts in global trade and economic patterns. Canada has not escaped the consequences of these shifts. Europe took approximately 20% of Canada's merchandise exports 20 years ago and 17%-18% ten years later. The level has declined to approximately 10% since the mid 1980s. Moreover, the EC's share of Canadian exports of services also appears to have declined modestly from 17%-19% of such exports in the early 1980s to about 16% in the early 1990s. Europeans

[2] Statistics Canada, Catalogue 11-210.

are increasingly trading with themselves (intra-western European trade increased from 27% to more than 33% of world merchandise trade between 1980 and 1990).[3]

Moreover, the European economies have entered a relatively slow growth stage that will likely last to at least the end of this decade. Both DRI/McGraw-Hill and the WEFA Group forecast that Europe will be the slowest growing of North America's trading partners.[4]

On the trade policy front, the Europeans are not the only ones to indulge in trade protectionism nor are they solely responsible for the continuing impasse in the MTN. But the degree of their parochialism on several key issues is striking. The European Community's commitment to building a big, comprehensive MTN package has been considerably less than commensurate with its stake in global markets and growth. The EC's predatory agricultural policy is the most evident and disturbing reflection of this disconnect. There are other examples: a weak overall tariff-reduction offer in areas of major export interest for Canada; and an unwillingness to contemplate major reform of anti-dumping procedures.

The EC has also taken a restrictive stance vis-à-vis a number of bilateral trade irritants with Canada. These include Canadian newsprint quotas, access for our fisheries exports, over-fishing off the Grand Banks (until recently, when the crisis in fish stocks became so grave that even the unreasonable could not ignore it), fur labelling issues, phytosanitary concerns related to the pine nematode, compensation for impairment of Canadian trade arising from earlier EC enlargements, and a satisfactory resolution of Canada's long-term quality wheat access rights into the EC market (an irritant going as far back as 1962).

Canadian efforts to expand the level of western European investment in Canada has met with some success. Foreign direct investment (FDI) stock in Canada from that region more than doubled after 1985, exceeding $36 billion by 1991. More importantly, the European share of total FDI in Canada increased from 19% to 28% during the same period, accounting for the largest counterbalance to the decline in the

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[3] GATT, **International Trade 90-91**, Vol.II, p.9; André Sapir, "Regional Integration in Europe", in **The Economic Journal**, 102 (November 1992), 1491-1506; Norman S. Fieleke, "One Trade World, or Many: The Issue of Regional Trading Blocs", in **New England Economic Review** (May/June 1992), p. 13. Services trade data are from Cansim and should be treated with some caution given difficulties in recording such trade.

[4] According to recent DRI estimates, during the 1995-2000 period annual real growth in GDP will be 5.2% in both Asia and Latin America compared to 2.8% in Europe as a whole and the EC. The WEFA Group forecasts broadly similar results for 1992-97.

proportion held by the U.S. (76% to 64%). In the other direction, Western Europe became an increasingly attractive place for Canadian investors, accounting for 14% of total Canadian direct investment abroad in 1985, but over 22% in 1991.[5] Yet it is helpful to place this partial shift in context. The following factors are important:

- As in the past, a single country, the U.K., has remained by far the largest source of European FDI in Canada, with almost half that region's share in both 1985 and 1991. The U.K. was also the recipient of well over half of Canadian FDI stock in Europe.

- The other European majors (Germany, the Netherlands, Switzerland, France and Sweden) account for most of the balance of European FDI in Canada.[6]

- Policy makers predicate the hunt for quality foreign investment on the research, production and marketing efficiencies that such investment should bring. Yet not all FDI creates the <u>control</u> of an enterprise often necessary to ensure the adoption of the changes required to achieve the desired efficiency gains and, consequently, to have a major positive impact on the Canadian economy. When viewed from this perspective, the relative impact of European investment in Canada did not increase significantly during the 1980s. European investors controlled 5% of the assets of all non-financial corporations in Canada in the early 1980s, a level increasing to just 6% in 1988 (the last year available). Their share of revenues remained stable at about 5%.[7]

- With respect to non-direct foreign investments (i.e., portfolio instruments), the U.S. share sharply contracted during the 1980s (from 60% in 1983 to 38% in 1991). Portfolio investment from the European Community helped fill the gap, with the value of such holdings increasing from almost $30 billion to almost $80 billion during the same period. Yet the EC's <u>share</u> of foreign portfolio investments in Canada increased

[5] Statistics Canada, "Canada's International Investment Position", Catalogue No. 67-202 (1992), Table 9, pp. 67-72 and Table 29, pp. 101-06.

[6] Statistics Canada, Catalogue 67-202 (1992), Table 29, pp. 101-06.

[7] Statistics Canada, **CALURA 1988**, Table 1, pp.126-7, and Table 4, p. 139; **CALURA 1982**, Table 3, p.141. Since the early 1970s, Canadian-controlled corporations have accounted for a generally increasing share of assets and revenues of non-financial corporations, a trend reversed only modestly with respect to assets during the foreign mergers and acquisitions binge that peaked in 1988-89.

only modestly: from 18% to 22%. The stake of Japan grew much more rapidly: from 4% to 16%. The share from non-OECD sources increased from 6% to over 11%.[8]

The peak of the last mergers and acquisitions surge is now well behind us. Moreover, western European investment attention is increasingly focussed on facilitating German unification, the retooling required by the Europe 1992 integration process, and the enormous needs of Europe's eastern backyard. There is, consequently, little reason to believe that European investment will figure more prominently in Canada during the 1990s beyond the relative levels achieved during the past decade.

In general terms, moreover, there is little to indicate that Canada will figure more than occasionally and marginally in overall European economic planning and priorities into the foreseeable future. There is <u>no</u> special relationship in the economic sphere. This does not mean, however, that we have no European interests. Clearly we do. Trade has declined in relative terms, perhaps permanently, but it remains important. Fully manufactured end products comprise one-fifth of Canada's exports to Europe, much less than to the U.S., but considerably more than the meagre 5% of our exports to Japan. Put another way, Canada ships end products worth eight times more to Europe than to Japan and twice as much than to all of Asia, although the gap has narrowed somewhat since the 1970s.[9] Moreover, over 40% of Canada's exports to Europe comprise fabricated materials, including fully processed resource-based products which sustain many high quality Canadian jobs with high Canadian content.[10]

The European investment stake in Canada may be modest in terms of the Canadian economy as a whole and compared to the continuing substantial presence of U.S. investors. Nonetheless, it continues to make a useful contribution to Canadian prosperity and represents a commitment six times larger (in terms of assets controlled) than that made by the Japanese. Moreover, several western European countries are rich in innovative technologies in numerous sectors. In 1989, the EC as a whole accounted for 29% of total research and development expenditures within the OECD group, with the three leaders (Germany, France and the U.K.) responsible for just over

[8] Statistics Canada, Catalogue 67-202, 1981-84, Table 15, pp.48-9 and 1991, Table 2, pp.35-7.

[9] In 1990, 5.35% of total Canadian exports of end products were shipped to Europe; 0.67% to Japan; and 2.88% to Asia as a whole.

[10] On the job creation impact of Canadian exports, see Morley Martin, "Exports and Job Creation", Policy Planning Staff Paper 93\06, forthcoming.

22%.[11] The size of the EC financial commitment underlines the importance of pursuing research partnerships with European innovators, including through the participation of Canadian firms in EC-funded projects (negotiations are currently underway on a governmental level to establish a framework for such collaboration). Finally, four of the seven Summit countries are European, while the EC is one of the four Quadrilateral partners that meet regularly to review key trade policy issues. For these reasons alone, western Europe merits a vigorous and sustained Canadian presence in order to retain at least some influence on the fiscal, monetary, exchange rate and trade policies of the majors.

Nonetheless, the attention of Europeans is increasingly on Europe. The time-consuming task of managing the expanding and complex process of integration coupled with the end of the Cold War bonds that underpinned much trans-Atlantic cooperation imply that Canada, if it were to operate by itself without extra-European partners, would have difficulty preserving even its current modest influence in the overall European order of things to the benefit of Canada. If we work primarily alone, we may find ourselves expending scarce resources in no way commensurate with the trade, economic policy, or broadly political benefits derived therefrom. This rationale suggests the increasing importance of identifying and working with effective partners from other regions who broadly share our goal of influencing European economic and trade policies.

Much the same concern, although from a different angle, emerges from an analysis of resources currently dedicated to economic relations with Europe. As recently as 1991-92, Canadian activities in Europe received almost 40% of the trade development resources of the Department of External Affairs. Yet funding provided for one component, the popular Programme for Export Market Development (PEMD), generated no better than an average (eastern Europe) to low (western Europe) rate of return.[12] Moreover, almost 30% of our staff doing trade and economic relations work at Canada's bilateral missions abroad are located in Europe.[13] Amost 30% of official travel abroad (1988-92) by the Minister for International Trade and over 40%

[11] On a purchasing power parity basis, the EC accounted for 29.4%, the three EC leaders for 22.1%, Japan for 18.4%, the U.S. for 44.5% and Canada for 2.1%. See OECD, **Main Science and Technology Indicators**, No.2 (1992), p.16.

[12] Andrew Griffith, "From a Trading National to a Nation of Traders: Toward a Second Century of Canadian Trade Development", Policy Planning Staff Paper 92/5, pp. 32, 44, 101-2.

[13] EAITC/MCBA.

of the travel undertaken by the Secretary of State for External Affairs are to Europe.[14] All in all, these patterns seem to reflect traditional ties which, while still important, are nonetheless not as relevant as they once were.

3. Japan: The Limits of Bilateralism

The rise of Japan fascinates and frustrates at the same time. The sources of fascination are evident to all. The Japanese have emerged over the past 20 years as highly competitive exporters of goods, services and capital. Japan is a key G-7 player. Japan is one of the world's most industrially innovative countries, accounting for more than 18% of research and development expenditures within the OECD group, second only to the U.S.[15] Japanese motor vehicles have forced the Big Three to improve quality and manufacturing efficiency. Japanese producers have taken on the Americans and carved out a significant and, for most of the recent past, the leading role in the international market-place for semi-conductors. The Japanese share of world FDI stock has grown from a mere 1.3% in the late 1960s to 12.2% in 1990. Japan's contribution to global portfolio capital outflows increased from 20% in the late 1970s to 50% in the late 1980s.[16] Japanese per capita income has expanded impressively, doubling in the last ten years to US$ 19,100, creating a large, wealthy consumer market.[17] Japan has translated this stunning transformation into increasing influence in global economic and trade policy management. Regionally, Japan continues to solidify its economic position throughout the Pacific Rim by means of trade, aid, loans and investment in manufacturing and services industries.

Canada has reacted positively and with some ingenuity to the opportunities provided by the Japanese economic success story. The value of our merchandise exports to Japan increased more than five-fold during the 1970s and then almost doubled again in the 1980s. Exports peaked in 1989 at almost $9 billion.

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[14] The period 1988-1992 was reviewed. The percentages exclude visits to Europe that clearly were not Europe-focussed (e.g., OECD ministerial meetings or those related to the MTN). Anecdotal evidence suggests that this bias in travel also holds for other federal and provincial ministers.

[15] Calculated on a purchasing power parity basis, Japanese expenditures comprised 18.4% of the OECD total in 1989, compared to 44.5% for the U.S. and 22.1% for the three EC leaders: Germany, France and the U.K.. See OECD, **Main Science and Technology Indicators**, No.2 (1992), p.16.

[16] Before fading in 1990 and 1991 to 26%.

[17] Among the G-7, Canada edged Japan for third spot, behind Germany ($19,500) and the U.S. ($22,200). All numbers are for 1991 on a purchasing power parity basis.

Our share of the Japanese import market grew from 3.1% in 1981 to 4.4% in 1988. The stock of Japanese direct investment in Canada more than doubled after the mid 1980s, reaching $5.3 billion in 1991. The importance of Japanese holdings of Canadian portfolio investment instruments grew even more sharply: from $6.4 billion in 1983 to $58 billion in 1991, with the Japanese share of total foreign holdings quadrupling.

Nonetheless, the sources of frustration in Canada-Japan economic relations are also evident, clearly delineating the limits of bilateralism. Canada captured a mere 1% of outflows of Japanese direct investment abroad in 1985-90. The Japanese share of direct investment in Canada has increased only modestly and, at 4.1% of total FDI in 1991, remains far below potential and well off the levels of commitment and confidence in Canada shown by the European majors and the Americans (28% and 64% respectively). During the 1980s, Japanese-controlled assets in Canada increased from just 0.4% of total assets of non-financial corporations to a meagre 0.9%.

In recent years, the attractiveness of the Japanese market for Canadian exports has also peaked. Total exports declined in 1990 and 1991 by almost $2 billion before recovering modestly last year. The share of our total exports destined for the Japanese market has declined steadily since the late 1980s from over 6% to under 5%. And Canada has lost market share in Japan, dropping from 4.4% of Japanese imports in 1988 to 3.3% in 1991.

Perhaps most distressingly, the structure of Canada's exports to Japan remains heavily skewed towards crude materials and away from end products to a degree unknown in any other major Canadian export market. In 1980, inedible crude materials comprised 70% of Japanese imports globally and 45% of Canada's exports to that market. Ten years later, the relative importance of these same imported materials had declined substantially for Japan, comprising 41% of total imports (but still 42% of Canadian exports). During the 1980s, Japanese imports of semi-manufactures doubled from 7% to 14%-15% of total purchases off-shore, compared to a fairly stable one-third of Canadian exports destined for Japan (representative of continuing Canadian strengths in sectors relatively rich in good quality jobs such as forest products). The real disappointment for Canada lies in end products, dominated by machinery and equipment and a variety of consumer goods. The share of these products in global Japanese imports almost tripled during the 1980s to reach 30%. Yet in 1980, end products comprised only 2.4% of all Canada's exports to Japan. Ten years later, this proportion had increased to just 5% (one-tenth the proportion of our exports of end products into the U.S., and one-fourth the level into Europe).

Japan has not been a particularly friendly market for Canadian manufactures, including in the automotive sector.[18]

Ironically, Canadians also face considerable frustration when seeking Japanese commitments to remove restrictions that impede access for several more traditional Canadian exports where our competitiveness is not even remotely in question. Two examples should suffice, one a semi-manufacture, the second a basic foodstuff. Spruce, pine and fir lumber (SPF - largely supplied by Canada) faces an 8% import duty (which is unbound in the GATT) when entering Japan, compared to a zero tariff for another dressed lumber item for which the U.S. is the principal supplier, and mostly zero tariffs for tropical lumber. Although Canada also has supplied an important proportion of the second lumber item, the tariff differential is one reason why imports of SPF lumber (where we are the principal supplier) are considerably lower. Canadian efforts to redress this situation have gotten no-where beyond the possibility of some modest adjustment in the multilateral trade negotiations.

The second example is a case of apparent success covering a much larger problem. Japan applies a zero import duty on wheat. The U.S., Canada and Australia are major suppliers. But this tariff is unbound in the GATT, thus permitting the Japanese Food Agency to mark up significantly the price of imported wheat without violating Japan's GATT obligations. Mark-ups can range as high as 130%, thus making wheat-based products significantly more expensive than would otherwise be the case which in turn works to support domestic rice and grains producers. The binding of this tariff at zero and the consequent elimination of mark-ups would significantly lower the cost of and expand the demand for wheat-based products to the considerable benefit of internationally competitive Canadian producers. The Japanese have given no indication that they are likely to do so.

The Canada-Japan relationship is undeniably important and permanent. Bilateralism and multilateralism have both helped in developing this relationship and both will remain important. Yet both have also failed to capture significant potential benefits for Canada.

[18] Japanese import data from GATT, **International Trade 90-91**, Vol.II, Table A17, pp.108-9; Canadian export data from International Trade Division, Statistics Canada (May 1992). On the other hand, Canadian exports of end products do not generally appear to produce as many high quality jobs compared to exports of equal value of processed resource-based products. The former contain a higher proportion of imported inputs. This helps to explain why $1 billion in Canadian exports to Japan produce 50% more jobs in Canada than $1 billion in exports to the U.S. where over half of Canada's exports comprise end products. (See Martin, "Exports and Job Creation".)

4. U.S.: The Inevitable Partner

This section need not detain us for long. The deeply embedded and multi-faceted relationship with the U.S. will continue to be fundamental to Canadian prosperity and the necessary centrepiece of Canada's economic diplomacy. The U.S. share of Canada's exports has increased over the past ten years from 67% to over 73% of all shipments abroad of Canadian goods and services. During the same period, the U.S. has accounted for a fairly steady share of almost 70% of the Canadian import market for goods and services.[19] The U.S. in 1990 was the recipient of almost 90% of Canada's exports of end products, up from 77% ten years earlier.[20]

The industries in the two economies are closely integrated operationally, with the U.S. by far the primary source of imported inputs within a context of increasing foreign sourcing by many Canadian firms. The motor vehicle industry is the prime example of this phenomenon, but it increasingly typifies Canada-U.S. production in other manufacturing industries.[21] The FTA and the NAFTA will accelerate this trend, just as the 1965 Auto Pact fostered such integration in a key sector with highly favourable results for Canada.

The U.S. share of the total stock of foreign direct investment in Canada declined somewhat in the 1980s. Nonetheless, in absolute terms it grew by almost $18 billion between 1985 and 1991 and still accounts for almost two-thirds of all FDI in Canada.[22] Looked at in terms of control of enterprises, U.S. investors controlled just over 17% of the assets of all non-financial corporations in Canada in the late 1980s, only slightly down from the 18% level recorded at the beginning of that decade. On the other side, the U.S. is the first port of call for Canadians investing

[19] All calculations from Statistics Canada on a balance-of-payments basis.

[20] Statistics Canada, International Trade Division, May 1992. It should be noted that end products (in part because of a greater level of imported inputs) do not create proportionally as many high quality jobs as fully processed resource-based exports. Nonetheless, the manufacturing of such end products involves high-tech processes which are important in ensuring the diffusion of leading edge technologies in Canada.

[21] OECD, "International Sourcing of Intermediate Inputs", DSTI/STII/IND(92)1, March 1992; see also, Canadian Manufacturers' Association, **The Aggressive Economy: Competing to Win** (June 1992), pp. 41-9.

[22] Statistics Canada, Catalogue No.67-202 (1992), Table 29, pp. 101-06.

abroad, and was the location of 58% (more than $54 billion) of Canadian FDI stock abroad in 1991, down from a 67-68% share in the early and mid 1980s.[23]

The U.S. share of foreign holdings of portfolio investment in Canada has significantly declined since the early 1980s, but nonetheless remains the single largest source of such capital, with 38% ($138 billion) of total 1991 holdings compared to $58 billion by Japan.[24] U.S. financing will remain of critical importance for managing Canadian fiscal deficits well into the foreseeable future. The U.S. is also a dynamic source of new technologies, accounting for close to half of all expenditures within the OECD group on research and development.[25] This underlines the importance of ensuring Canadian access on a non-discriminatory basis to innovative technology consortia in the U.S. at the "pre-competitive" stage.

Finally, and despite periodic and sometimes quite sharp trade disputes between Canada and the U.S., the fact remains that only the U.S. among the three major markets has been prepared to negotiate the elimination of most of the remaining barriers to Canadian exports and to secure this access through carefully crafted, binding rules subject to effective dispute settlement procedures - all of which goes beyond what has been achievable multilaterally. In at least partial contrast, the EC has preserved barriers (e.g., tariff preferences with EFTA countries, and a number of important non-tariff barriers related to agricultural and resource-related sectors which the EC has been reluctant to negotiate; the active use of a less than transparent anti-dumping regime to attract investment into member States). For its part, Japan has been reluctant to address resolutely trade issues of central concern to Canada.

Growth prospects for the rest of the decade in the U.S. appear modest compared to rates anticipated in the Pacific Rim and several Latin American economies. Yet, the U.S. has, at least, made a commitment to comprehensive change and integration. We must continue to exploit this policy bias to further Canadian economic interests: whether it be by pursuing additional liberalization related to government procurement practices, by seeking the replacement of anti-dumping procedures with competition policy within the free trade area, or simply by pursuing the on-going management of current disciplines by standing firm whenever the U.S., under pressure from domestic protectionists, occasionally tests the limits of the rules established in the FTA and now strengthened and clarified in the NAFTA. As explored

[23] Statistics Canada, Catalogue No. 67-202 (1992), Table 9, pp. 67-72.

[24] Statistics Canada, Catalogue No.67-202, various years.

[25] On a purchasing power parity basis.

further in subsequent sections, one key policy question for Canada is how to build on the NAFTA to ensure that it remains an instrument for promoting the elimination of remaining barriers to exports of Canadian goods and services within North America as well as elsewhere.

At present, just over one-quarter of Canada's trade and economic relations staff posted at bilateral missions abroad is located in the U.S.[26] Given the greater familiarity of Canadian exporters with the U.S. market and the high level of industry integration in several key sectors, a greater share is likely not needed, although the increasing "legalization" of trade relations generated by the FTA and NAFTA will require giving further attention to enhanced personnel training in trade policy, as distinct from trade promotion.

5. Redefining Our Backyard: Latin America and the Pacific Rim

Our relationship with the Triad economies of Japan, the EC and the U.S. is critical to Canadian economic growth prospects. Yet there are other attractive opportunities elsewhere. Attractive both in terms of access to markets <u>and</u> strategic cooperation with a view to managing more effectively our relations with the majors.

The Pacific Rim countries have managed their economies well over recent decades. They have, in most instances, implemented consistently responsible fiscal and monetary policies at home and pursued successful export-oriented trade development abroad (although not always opening their own markets at the same pace). Average annual real GDP growth rates of 8%-9% in the 1970s and 6%-8% in the 1980s were frequently the result, with even higher growth in some instances. Independent analysts predict modestly lower, but still impressive growth through the end of the decade.[27] Asian markets (less Japan but including the increasingly vibrant Chinese economy) accounted for 3% of Canada's merchandise exports in 1970, rising to 5% in 1990. Moreover, higher value-added fabricated materials, machinery, equipment and consumer manufactures increased from 48% to 60% of those exports over the same period, including a high proportion of processed resource-based products that sustain quality jobs in Canada. Moreover, several Pacific Rim

[26] EAITC/MCBA.

[27] For example, see the estimates of DRI/McGraw-Hill and The WEFA Group.

economies other than Japan have increased their direct investment stake in Canada in recent years, accounting for almost 3% of FDI stock in Canada in 1991, up from 0.3% ten years earlier.[28]

With respect to Latin America, several of the main economies grew at Asian rates in the 1970s (a fact sometimes forgotten), before the distortions of import substitution and the debt crisis led to the lost decade of the 1980s when the region fell sharply behind. Over the last several years, democratic institutions and practices have strengthened considerably. Latin America has also reversed its economic course, often quite remarkably. Although with varying degrees of commitment (strongest in Mexico and Chile, almost as impressively in Argentina, Colombia and Venezuela, still hesitantly in Brazil), Latin American governments have implemented increasingly coherent domestic economic reforms and have strikingly liberalized their trade and investment regimes. They have also demonstrated an important commitment to formalizing these changes in internationally binding obligations through accessions to the GATT, market opening proposals in the MTN, and a willingness to take concrete steps toward freer trade through additional sub-regional integration. Several are clearly committed to going even further by entering into a comprehensive economic relationship as equals with the U.S. and Canada through accession to the NAFTA.

Real growth in Latin America is expected to average about 5% annually through the year 2000. In 1980, Latin America was the destination of 5% of Canada's total merchandise exports, a level that plummeted to 2% during the troubled 1980s. Canadian exports are now expanding once again and could return to a 5% share by the end of the decade as a result of steadier growth in the region and increased integration through NAFTA.[29] The region is an excellent market for higher value-added Canadian products: in 1980 shipments of fabricated materials, machinery and equipment, and consumer manufactures accounted for over 60% of Canada's exports to Latin America.

[28] Statistics Canada, Catalogue No. 67-202 (1992), Table 29, pp. 101-06. Hong Kong leads the way in this regard.

[29] Canada's exports to Latin America and the Caribbean increased by 19% (on a customs basis) in 1992, while Mexico became our fifth largest source of imports. Statistics Canada estimates that Canadian exports to Mexico have been underestimated by at least one-third, due to the failure to record accurately shipments to U.S.-based intermediaries. This may also be the case for Canadian exports destined for other countries in the hemisphere which are transhipped through the U.S. This rectification implies that Canada's trade surplus with the U.S. is modestly lower then the formally recorded level.

The potential for closer economic relations with key Latin American and Pacific Rim countries goes much beyond the immediate and foreseeable export benefits. The even broader challenge is how to address the increasingly comprehensive and thus intrusive international economic agenda so that the system "works" for Canada, both through the establishment of clear economic rules that reflect Canadian interests and through the acceptance of these rules by the three majors.

The rule-making scope of the international trading system has expanded considerably over the past ten years. Issues such as cross-border trade in services, non-discriminatory investment rules, intellectual property rights and the nature of dispute settlement processes have moved far beyond the hesitant, tentative beginnings of reform of the early 1980s. Although the rule-making is far from complete multilaterally, this agenda now enjoys much broader acceptance. Yet, the 1990s promise to push this "trade" agenda much further.

In fact, trade negotiations are quickly becoming economic negotiations with profound impact on a wider range of policies long considered essentially domestic. The new agenda includes trade and the environment, competition (or "anti-trust") policy, and key issues related to industrial and innovation policies. As the scope of the work expands, as the rules of the game are made - and not just for the "new" issues, but also for important unfinished business such as trade in agriculture - we need to ask ourselves how we can ensure three key results:

- dynamic regionalism that will, over time, encourage broad multilateral liberalization in ways that serve Canada well;

- greater and more secure access to all three Triad markets,[30] including for processed resource and agricultural products in Japan and the EC, and government procurement and trade remedy reform in all three; and

- the effective management of the "new" issues, so that negotiated results reflect the needs and realities of small, open, trade-dependent economies such as Canada.[31]

[30] The U.S., the EC and Japan.

[31] I address this matter more fully in "Globalization", Policy Planning Staff Paper No.93/01 (e.g., vis-à-vis competition policy convergence on pp.46-50); see also Laura Tyson, "Managing Trade Conflict in High-Technology Industries", in Martha C. Harris and Gordon E. Moore. eds., **Linking Trade and Technology Policies** (Washington, D.C.: National Academy Press, 1992), pp.75-8.

If the international community, whether multilaterally or regionally, or (most likely) both, crafts new rules of the game for old and new issues alike, who will be our "friends in the game"? The important cooperative work done in the multilateral trade negotiations through the Cairns Group of medium-sized agricultural exporters provides a valuable lesson in this regard. A reasonably cohesive group of south-east Asian and Latin American exporters joined with Canada, Australia and New Zealand and ensured that the three majors heard another voice at the MTN table.

In fact, such Latin American and Pacific Rim players share many interests with Canada, including the hunt for improved and more secure access to Triad markets, the continuing importance of resource trade (including value-added processed products) for their economies (with Korea being the major exception in this regard), and a concern that emerging trade rules related to issues as diverse as competition policy, investment and the environment remain sensitive to the different structural characteristics of smaller, more trade-dependent economies. Moreover, these countries are also active players internationally and bring some leverage to the bargaining table in the form of dynamic markets of interest to exporters and investors from the Triad. Although the coalition building will inevitably vary with the specific issue under consideration, closer, more persistent and sustained cooperation with selected Pacific Rim and Latin American economies can only increase Canadian leverage both within the NAFTA and multilaterally, in pursuit of the ultimate goals of improving access to Triad markets and crafting balanced rules of the game that best reflect Canadian realities.

The logic of our new backyard also requires greater recognition with regard to the use of increasingly scarce financial and human resources. Asia Pacific has recently accounted for almost 30% of the trade development resources of the Department of External Affairs as well as 24% of the government's trade and economic relations staff at bilateral missions abroad. Given a better than average rate of return on PEMD funding, the dynamism of these markets, and the strategic requirements identified in this Paper, some increase in the share of resources available seems merited. But the greatest deficiency in the way we deploy our activities abroad is with regard to our presence in Latin America. With a very high PEMD rate of return, an economic dynamism beginning to match that in the Pacific Rim and an increasing willingness to forge closer trade and economic relations with North America, Latin America nonetheless received only 5-6% of the Department's trade development resources in the early 1990s and has just 12% of our trade and economic staff located at bilateral missions abroad.[32] Moreover, Asia Pacific and Latin America

[32] Griffith, "From a Trading Nation to a Nation of Traders", pp. 32, 44, 104-11; EAITC/MCBA.

combined have accounted for only one-fifth of the official travel abroad (1988-92) by the Secretary of State for External Affairs and the Minister for International Trade. This imbalance merits a close look.

6. NAFTA: Instrument of Choice

A critical question is the choice of trade policy instruments to develop the key relationships identified in the previous section. One option for reaching across the Pacific could be the Asia Pacific Economic Cooperation (APEC) forum established in the late 1980s and encompassing Japan, Korea, the three Chinas (PRC, Taipei, and Hong Kong), the ASEANs, Australia, New Zealand, the U.S. and Canada (Mexico and Chile are actively seeking membership). APEC is not yet a well-structured organization, apart from a recently established, but small Secretariat, and reasonably regular meetings of senior officials and ministers. It rather resembles a loosely knit consultative grouping also engaged in a limited number of useful, but modest economic and trade-related projects. Some have suggested, nonetheless, that member countries should now deploy considerable effort to transform APEC into a mechanism for trans-Pacific trade and investment liberalization. A number of Australians, Americans and occasional voices from the ASEANs have encouraged this approach.

The APEC has been helpful in ensuring greater dialogue on economic matters between North America and East Asia. Nonetheless, suggestions to transform APEC into a legally binding instrument covering trade in goods and services, government procurement, investment, intellectual property, dispute settlement, or any one of these individually imply a major dedication of scarce negotiating resources that we could justify only if the likely result were worth the effort, i.e., a result that would be both comprehensive and mutually beneficial. From this vantage point, the option of proposing APEC as a negotiating forum suffers from several critical flaws from a Canadian perspective.

First, it is not at all clear how many APEC members might be ready to enter into such an ambitious project. Australia, New Zealand, and Korea could well be. The first two are the beneficiaries of their own free trade agreement and have been active proponents of trade liberalization in the MTN. For its part, Korea has indicated a willingness to make substantial, legally binding commitments in the MTN and some influential policy makers have argued for even broader engagement. Yet, the record of the ASEANs is much more spotty despite their export orientation and their generally favourable approach to foreign investment. The ASEANs' own efforts at trade and economic integration have been painfully hesitant in practice. They have, moreover, played a disappointing role in the MTN, demonstrating as a group continuing reluctance to abandon special and differential treatment or to accept extensive disciplines in the area of investment. The PRC has made impressive economic gains in recent years, but formalizing trade and domestic economic liberalization in binding international agreements would demand a commitment that goes considerably further than what the Chinese leadership has accepted to date.[33] For its part, and as discussed in a previous section, Japan also does not appear ready to cross the threshold into a comprehensive arrangement in a truly reciprocal manner, including with regard to such sensitive sectors as agriculture and a commitment to explore meaningful reform of competition (anti-trust) policy.

Second, an APEC-based negotiation in the above areas would entail that which we have already done twice: negotiating a carefully crafted, broad-ranging legal framework governing our economic relationship with the U.S.. Canada already has an arduously developed, balanced framework to govern many of the multiple aspects of our relations with the U.S., including investment, intellectual property, and dispute settlement. That framework is the FTA as reworked in the NAFTA. To engage in the negotiation of an APEC-wide investment instrument, for example, would expose us once again to renegotiating our investment relations with the U.S., including those areas where Canada retains policy flexibility (e.g., the right to impose technology transfer performance requirements in cases of foreign takeovers; Canada's sectoral reservations to the non-discrimination obligations). If the U.S. were to decide to pursue seriously a detailed APEC negotiating option, and if others appeared ready to participate, then we would want to look very closely at joining the process. But there is no compelling reason for Canada to encourage such an approach.

Third, there are other, better options. With respect to investment, Canada has recently revised its model bilateral Foreign Investment Protection Agreement (FIPA) to reflect some of the higher quality disciplines found in the NAFTA. To the degree that Canadian investors in an Asian country seek greater security and the opportunity exists to prohibit certain trade-distorting practices in that country, then the negotiation of a FIPA would make sense.

But more importantly, we now have the NAFTA, scheduled to enter into force in January 1994. This agreement ranges far across the landscape of economic policy, including disciplines and comprehensive commitments on trade in goods and services, investment, intellectual property and various layers of carefully crafted dispute settlement procedures. It provides improved and more secure access for

[33] Not to mention continuing reluctance in the West with regard to forging significantly closer, more formal economic ties with the PRC as long as it adheres to political totalitarianism.

Canadian producers in the markets of the other two signatories and reinforces Canada's position as a favoured site for investment (both domestic and foreign). Furthermore, the NAFTA envisages additional negotiations (but without reopening that which the signatories have already achieved) in such areas as government procurement (accounting for perhaps one-sixth of North American production annually), cross-border trade in financial services and, in a very forward-looking agenda item for the 1990s, the relationship between competition law and trade, including the possible replacement of anti-dumping regimes within the free trade area.

The acceptance of the Canadian proposal for the inclusion of an accession clause in the NAFTA opens important, even exciting possibilities.[34] Accession opens the door to improved and more secure access for Canadian producers in other markets on a mutually beneficial basis without reopening the rules governing our relations with the U.S.. Accession means that other countries, in order to gain preferential access in the North American market, will have to accept the high quality generic disciplines of the NAFTA (subject to the possibility of limited reservations to be negotiated). In this regard, it would be best not to view NAFTA as the vehicle for full hemispheric economic integration in either the Americas or on a trans-Pacific basis. Over the next several years, some Latin American countries could make excellent partners as they should be prepared to negotiate in a broadly reciprocal manner (e.g., certainly Chile, perhaps Argentina, Colombia and Venezuela). Many others will likely require more time in the face of domestic economic policy confusion. Across the Pacific, surely the NAFTA dynamic could include Australia, New Zealand and perhaps Korea (historically uncomfortable with Japanese regional leadership and increasingly committed to open markets). The ASEANs and the PRC, on the other hand, do not yet appear ready for such sweeping, legally binding commitment.

Accession will further strengthen an outward-looking trading culture in Canada by encouraging Canadian entrepreneurs to seek market niches beyond the United States and by obliging Canadians, in a creative response to the pressures of globalization, to continue reshaping domestic policy in a measured and progressive

[34] NAFTA Article 2204 reads as follows:

"1. Any country or group of countries may accede to this Agreement subject to such terms and conditions as may be agreed between such country or countries and the Commission and following approval in accordance with the applicable legal procedures of each country.

2. This Agreement shall not apply as between any Party and any acceding country or group of countries if, at the time of accession, either does not consent to such application."

manner.[35] Accession will also draw in additional high quality economic partners who will provide further balance in an arrangement where the U.S. remains the dominant producer and trader. New committed members will create a dynamic in NAFTA that Canada could use to further the work that lies ahead in areas such as the liberalization of government procurement and trade in financial services, as well as the difficult but necessary challenges related to competition policy.[36] More members will help Canada do what it has always done best: use combinations of partnerships to move negotiating files forward in a creative and beneficial manner.

Finally, the use of NAFTA accession to build solid bridges across the Pacific potentially has two special benefits. First, this process would help deflect the prospect of the gradual emergence of an Asian trading bloc centred on Japan. The potential for the creation of a formal preferential trading zone in East Asia to reinforce the important but more informal trade and investment links already in place may not be great, but we should not be complacent. Second, accession to NAFTA by certain Latin American and Pacific Rim economies would not only reinforce growth prospects in Canada, but could also potentially revolutionize the world trading system to such a degree that we could create, by the end of the decade, sufficient critical mass to ensure a more fruitful negotiation with Europe and Japan than the current MTN has been able to deliver.

7. Economic Partnerships: The Logic of Our Choices

The preceding analysis provides a reasonable and forward-looking basis for making choices during a decade of scarce human and financial resources. The practical implications are several.

- First, the old shibboleth remains valid. We must continue to dedicate considerable resources to managing our relations with the U.S..
- Second, over the next several years proportionally greater attention must be paid to cultivating relations in this hemisphere and across the Pacific, both because the markets are promising, but also because selected

[35] Jagdish Bhagwati wisely advises that Parties to free trade agreements should remain wary of domestic interest groups who argue against expanding trade liberalization by espousing the following sentiments: "Our Market Is Large Enough" and "These Are Our Markets". This mind-set is inherently inward-looking and protectionist. See his "Regionalism versus Multilateralism", in **The World Economy**, Vol.15, No.5 (September 1992), 535-55.

[36] On the latter point, see Christie, "Globalization", pp.38-49.

countries in these two regions are prime candidates for accession to the NAFTA which in turn would create a dynamic amenable to pursuing Canadian economic interests within the free trade area and beyond.

- Third, this additional shift in focus requires, to be fully effective, greater coordination of the various instruments of Canadian economic diplomacy. NAFTA accession is part of this process. But other elements should come into play:

  a) Poverty alleviation in and economic cooperation with the Americas and the Pacific Rim require greater recognition in Canada's overseas development assistance (ODA) programmes (these regions currently account for about 35% of Canada's bilateral ODA disbursements), with Africa, the Middle East and south Asia receiving considerably less than their present disproportionate share of approximately 65%.[37]

  b) Canada should, moreover, actively pursue environmental partnerships with selected countries in Latin America and the Pacific Rim, both because such cooperation has considerable merit in its own terms (e.g., Brazil, with respect to forestry practices and global warming), and because it would reinforce trade and trade policy relationships that are becoming increasingly important to Canada's economic well-being.

  c) Trade development and economic relations resources (financing and staffing abroad) as well as the deployment of ministerial visits should more closely reflect the emerging importance of the Pacific Rim and Latin America, and the relative loosening of ties with Europe. We should assign any new or redeployable resources that may become available to regions <u>outside</u> Europe where there is more promising ground for coalition building in support of specific, increasingly economic Canadian objectives.

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[37] Bilateral assistance includes direct government-to-government assistance and Canada Fund. It does <u>not</u> include food aid, emergency relief, EDC section 31 financing, CIDA INC programmes, and cooperation delivered through non-governmental channels. These latter components would tend to increase the proportion of total ODA going to Africa in practice. Recent adjustments to reflect last autumn's Economic Statement do not affect this pattern appreciably.

- Fourth, we should resist the natural temptation to try to "do much more" in eastern Europe and the former Soviet Union (FSU) where economic adjustment will be long and painful, making it a less attractive export market in practice and even more peripheral overall to core Canadian economic interests.[38] Canada's stake in that region is largely geopolitical (i.e., concern over defence conversion and disarmament; facilitating the difficult transition to market economies), involving the exercise of our G-7 responsibilities through participation in international assistance efforts. However, our direct economic interests in eastern Europe and the FSU traditionally have been modest. Weakened economies will not provide, broadly speaking, good markets. Moreover, the EC and its member states will almost certainly retain the preponderant role as the area's reconstruction proceeds (including through accession to the EC further down the road). In light of these considerations and of the competing, more promising opportunities elsewhere, Canada should ensure that its participation in financial and other assistance to eastern Europe remains firmly in keeping with our relative G-7 status and no more.[39]

- Fifth, Canada should adjust somewhat the location of Canadian resources already in Europe to focus even more sharply on the EC Commission and EC-related advocacy and investment promotion in <u>key</u> member state capitals.

- Sixth, the more intrusive nature of international economic trends and the footloose nature of foreign investment and innovative technologies demand the highest degree of policy coherence within Canada if our country is to remain an attractive site for investment, both domestic and foreign. Whether the dynamic of economic growth is created regionally, sub-regionally, on a hemispheric basis, or truly globally, it is certainly more and more a cross-border phenomenon. To encourage investment, to attract and foster innovation, and to create jobs, the single-playing-field policy context demands, as never before, coherence in the choice and use of economic instruments. Policy makers (both federal and

[38] See OECD Forum for the Future, "Long-Term Prospects for the World Economy", OCDE/GD (92)68, p.9.

[39] Policy makers could, of course, make exceptions if, on normal commercial grounds, they can clearly identify real trade opportunities on a case-by-case basis that compare favourably with opportunities elsewhere.

provincial) responsible for domestic transportation, telecommunications, labour, environmental and taxation laws and regulations must review their bailiwicks with a wider, more competitive eye.

- Finally, External Affairs and International Trade, if the analysis developed in this paper is even half-way correct, must increasingly focus resources on training and retaining human resources (with the concomitant financial commitments) who understand the intricacies and inter-connections of the economic files and, in particular, their application to our relations in the Western Hemisphere and the Pacific Rim.

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