



Statements and Speeches

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CHALLENGES IN THE INTERNATIONAL ECONOMIC ENVIRONMENT

An Address by the Honourable Mark MacGuigan, Secretary of State for External Affairs, to the Rotary Club, Charlottetown, Prince Edward Island, July 5, 1982

...Within the last month, I've attended two summits, those at Versailles and Bonn, and a Pacific Rim meeting, where we struggled with the great problems of the world today — problems such as world recession and international inflation, the East-West division which encompasses so much of the world, and I think the most difficult problem of all, that of world poverty, the so-called North-South question.

The theme that I want to address today principally — and I might say briefly — can be stated as "Challenges for Canada in the Current World Economic Environment".

At the Versailles Summit last month, the Prime Minister referred to the crisis confronting the industrialized world. 'Crisis' — in my view — is not too strong a word to depict the gloomy world economic conditions which have prevailed since last autumn and which threaten to continue. In the past year virtually all industrialized countries have been experiencing low growth rates and an alarming incidence of business failure. Real interest rates are at very high levels in many countries. Unemployment, already high at the time of the Ottawa Summit last July, has grown by five million over the past year in the Organization for Economic Co-operation and Development (OECD) or industrialized countries alone, and will rise even more unless economic conditions can be improved sufficiently to provide jobs for the large numbers of young people coming on the labour market. Though progress has been made in reducing inflation in some industrialized countries, it remains at a worrying level in many others, including our own, and fears persist that it could again increase once economic recovery gets underway.

Beyond the circle of industrialized nations conditions are no better; in fact they're probably much worse. The economies of Eastern Europe are in difficulty, and several countries in that region have been having trouble servicing their debts. Third World nations, hit by reduced export earnings because of the recession in the West and by high interest rates, are also experiencing balance of payments difficulties in unprecedented proportions. With the collective deficit of the Third World this year estimated at between \$75 billion and \$100 billion the world payments system may face a serious challenge.

In looking for a viable way out of this situation, most observers have underlined the need for a reduction in the very high level of real interest rates in the United States. There is no question that this is a key factor for several reasons. Lower interest rates

Ominous
economic
conditions

Reduce
U.S. interest
rates

[would] hasten economic recovery in the U.S. thereby improving trade prospects for America's trading partners, particularly, of course, Canada. Lower U.S. interest rates would also allow other countries to reduce, at least somewhat, their own interest rates, which have been kept high in order to encourage investment and to protect currency values. In addition, lower American interest rates and a less-strong American dollar would greatly help the Third World in servicing its debt and paying for its oil. For these reasons the outcome of the U.S. budgetary process continues to be of crucial importance, not just of course for the United States, but for all of its economic partners.

An agreement has recently been arrived at between both Houses of Congress and accepted by the Administration but it is seriously flawed by the size of the deficit, which may well foster further lack of business confidence in the policies of the Reagan Administration. In case you're tempted to ask how a member of a government which just a week ago reported a larger-than-expected budgetary deficit can criticize the deficit in another country, let me point out that the growth of our Canadian budgetary deficit has occurred by reason of the operation of economic forces, of automatic stabilizers which reflect in government expenditures and government revenues what is happening in the economy. The larger American deficit, on the other hand, is deliberately chosen, in that it results from a conscious choice simultaneously to decrease taxes and greatly to increase military spending. Furthermore, in relation to the best criterion, which is the personal savings rate (12.4 per cent of disposable income in 1981, compared with 5.3 per cent in the U.S.), the Canadian budgetary deficit has very much less effect on private sector investment than that of the United States.

Returning to my main theme, I fear that the pressures from the prolonged recession are spilling over into trade relationships, generating demands for new — and indeed old — forms of protectionism. Manifestations of these protectionist demands include a call for reciprocity of fair trade from the U.S. Congress, and increasing use of restrictive measures outside the General Agreement on Tariffs and Trade (GATT) framework. In some cases, especially between the United States and the European Community, serious trade disputes have erupted which threaten to prejudice long-standing economic and political relations. In this particularly difficult situation it is crucial that the industrialized countries work together, not only to achieve recovery but also to defend an open multilateral trade and payments system which will allow the benefits of that recovery to be passed from one country to the other.

**Versailles
declaration**

At the Economic Summit in Versailles, the leaders of the seven Summit countries, with our Prime Minister playing an important role, clearly recognized the scope of the difficulties facing all our countries. They endorsed a declaration that stressed the need for a further reduction in inflation and a return to higher levels of growth and employment. They specified that these goals were attainable only if, in addition to the individual efforts of each country, Summit countries joined forces and were sensitive

to the effects of their policies on others.

The Versailles declaration also reaffirms the commitment of Summit countries to strengthen the open trading system and to resist protectionist pressures. These undertakings are not, of course, sufficient in themselves. They must also be translated into action. However, their reaffirmation at this critical stage serves to underline the common commitment of the world's leading industrial powers to work together and serves as a useful signal of support to other organizations, especially the GATT which is to meet at ministerial level in November.

The Versailles Summit was marked by several other achievements, especially a package of undertakings in the financial area which should help to promote a greater convergence of economic policy aims among Summit countries, but I should leave it to another occasion to develop this aspect of the situation.

Export credit
subsidies

However, I do want to refer briefly to some other issues which are currently disturbing us. The first such issue is competition over export credit subsidies. I don't need to emphasize to a group such as this the importance of government support for Canadian exporters in the highly competitive international business world. But the cost has become very high. An arrangement among OECD countries to regulate and limit the trade distorting aspects of competition on export credits has come under growing strain in the last two or three years and increases in market interest rates have far out-paced negotiated rate increases in the arrangements. It is estimated that by 1981 arrangement participants were spending between \$5 and \$6 billion a year to subsidize their exports through below-market credits and assets — not a very healthy situation.

Some progress has recently been made in tightening discipline on export credits through a package of measures which reclassifies borrowers according to objective criteria and which increases the general level of interest rates.

Canada has been pressing for greater progress towards market levels so as to reduce the burden of costly subsidies. Yet difficult as it is to support this burden, the choice is a stark one. Either we provide financing to match the competition on large capital goods exports or risk losing business and jobs to our competitors. A widely publicized case in point was the recent tender to supply subway cars to New York City. Canada's official credits agency, the Export Development Corporation, had to provide a competitive package to meet an offer from France, at well below market rates, to allow the Bombardier company to compete on an equal footing for a contract for the export of 825 subway cars to New York's Transit Authority. I can assure you that providing big cash subsidies for the sale of Canadian products to a foreign utility gives us no joy whatsoever, but neither would the loss of a contract of \$1 billion — the largest contract in the history of this country — on which so many jobs depend. We very much want to see arrangement rules tightened so as to prevent such self-defeating competition in future.

Another issue which has dramatically moved to the forefront of the economic agenda is that of East-West economic relations, following setbacks to *détente* and the deterioration in the prospects for economic co-operation.

At the Ottawa Summit last year, it was agreed that consultations, and where appropriate co-ordination, were necessary to ensure that the economic relations of Summit countries with the East were compatible with Western political and security objectives. Since then the United States has sought to improve the system of controls on trade and strategic goods and to minimize what it sees as potential Western European vulnerability created by dependence on trade with the East, especially in the energy field. You've heard, I'm sure, of the proposed Siberian natural gas pipeline.

**More agreement
needed in West**

At the time martial law was imposed in Poland, Canada and other Western countries applied certain sanctions to Poland and the U.S.S.R. More recently, in the light of the continuing Polish situation, the U.S. has sought to limit export credits to the Soviet Union. Discussions over the past twelve months have, however, revealed differences in the approaches and interests of the Western countries. Prospects for East-West trade have also been clouded by the evident and growing economic difficulties facing some of the Eastern European countries and the growing level of their debt. What's plainly needed is more agreement among Western countries on what our political and economic aims should be, with regard to the East, taking account of the interests of all Western countries.

Some progress towards this aim was made at the Versailles and Bonn North Atlantic Treaty Organization (NATO) Summits, where participating countries agreed to pursue a careful and diversified economic approach to the U.S.S.R. and Eastern Europe, and particularly to observe commercial prudence in extending export credits. Despite this consensus, which seemed to bring Western countries closer together, President Reagan on June 18 extended American sanctions against the U.S.S.R. by restricting the export of oil and gas equipment to that country by U.S. owned or controlled foreign firms, including foreign holders of U.S. licences. This action has raised again the issue of the extraterritorial application of U.S. law, the attempt by the United States to make its laws apply outside the territory of the United States.

Canada, for its part, has long believed that trading relations between East and West can be mutually beneficial and a stabilizing factor in international relations. However, we also believe a prudent approach to economic relations with Eastern European countries is justified at this stage on commercial grounds alone. As well, we support a common agreement to eliminate the subsidy element of export credit to the U.S.S.R. as part of the broader agreement on export credit to which I referred earlier.

Third, let me flag a further issue that has gained increasing recognition in the past decades and will remain a vital issue for years to come. This is the urgent need to promote the economic viability of Third World countries and to work for their

integration into the international economic systems. The particularly difficult economic situation facing these countries, as a result of the present recession, makes it all the more imperative that we keep this issue in focus and continue our efforts to create a more just world. The Versailles Summit declaration clearly recognizes this need, and in these difficult times we must resist the temptation to ignore it.

From the foregoing, it is clear that the international economic system is facing perhaps its most serious challenge since the Second World War. It is clearly not within Canada's grasp alone to provide a solution to the world's crisis. However, it is within our negative potentiality to worsen the international economic crisis as it applies to us, and it is to the avoidance of this possibility that I want to turn for a final moment. To ensure objectivity in approaching this subject, let's turn for a basic analysis to the OECD.

**Wage restraints
necessary**

In a report prepared before last week's budget in Canada, the OECD warned that Canada's productivity growth remains the second lowest of the 16 OECD countries. The report spoke of "the moderation in wages in all of the seven largest OECD countries, except Canada," and added "we've very concerned because of the growing difference between U.S. inflationary performance and Canadian inflationary performance". The report's conclusion was that Canadians will have to exercise severe wage restraint in order to improve our country's competitive position.

Very similar words were used, and an appropriate solution recommended, a week ago by the Minister of Finance, the Honourable Allan MacEachen. Price inflation can be brought down, he said, by accepting for the time being income increases that are lower than the current rate of inflation. This strategy will lead in the short run to a lowering of income but it will soon slow the process that is eroding our pay cheque. It will check the rise of unemployment and it will establish a firm basis for resumption of real income growth throughout the economy. It will also, of course, increase our international competitiveness. This is the six per cent world of recovery as opposed to the 12 per cent world of recession.

As Mr. MacEachen says, the choice is ours. And it has to be a group choice. There has to be a willingness on the part of all Canadians to join together to resolve our common problem. We're all in this together and we can solve it only together.

There are some labour leaders who want to stand aside, to let others assume the burden which they want to evade. As a member of the only group in Canada whose income was actually cut by the budget, the members of Parliament, I think that I'm entitled to say that unless we all participate ourselves, and exercise our influence to try to ensure that others do so as well, we can't succeed. This is really a problem, I think from which no group can be entirely exempt. Well, there is one group that I think we will all want to exempt, and that is the group of old-age pensioners who are on the guaranteed income supplement, those who are by our definition living in

poverty and who are getting extra assistance through the guaranteed income supplement. They will not, by the budgetary proposals, be affected either in the old-age security part of the payments or in the guaranteed supplement itself.

But I think that even other old-age pensioners will want to be part of the solution to this problem which affects us all. They are citizens like the rest of us and I think that they would want to share in their way. It's not a large way, because the impact on them will not be great, but all of us will participate to the extent of our income in this attempt to halt the advance of inflation.

**Problem of
all Canadians**

This is not someone else's problem. It is our problem. There isn't anybody else to solve it. We can't pass it off to somebody else. The government is giving leadership. That's what Canadians are asking for, and the government has laid out a program to suggest to Canadians how to handle this.

But the government is not the country. The government can't do it all itself. This is what the OECD tells us we must do and it's what our own common sense tells us we must do. It's not someone else's problem, it's our problem. There is no one else to solve it. We are in effect the problem. We must also be the solution. We must not fail ourselves, we must not fail our world....

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