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**NORTHERN TIGER:
CANADA IN NORTH AMERICA**

by

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Let me say how delighted I am to have an opportunity to talk with you today about a critical decision that Canadians will have to make in the coming decade – how should their country position itself in continental North America. The challenge that this issue poses are monumental. But the rewards that the *right* approaches can provide are incalculable.

So far, the debate is relatively muted and the opinions that are offered too often are stumbling and incoherent. It reminds me of an incident that took place at Yankee Stadium on a sweltering August afternoon in the late 1960s. Yogi Berra, a man never short of words, but often baffling in his comments, was wearing a new, light, white, then-stylish silk suit when he ran into the wife of Mayor John Lindsay. Mrs. Lindsay looked him over and commented: My, don't you look cool? Yogi, not quite getting it, but determined to reply, shot back: You don't look so hot yourself!

That is sort of the tenor of our national conversation on North American integration at the moment.

Economic considerations clearly suggest that there are substantial gains to be made for Canadians if our economy becomes more closely integrated with those of the United States and Mexico as well as with other countries. But, living beside the US elephant, Canadians have throughout their history looked at economic integration with trepidation.

A central question often discussed by Canadians is whether integration will compromise our sovereignty to such a degree that Canadians will just throw in the towel and join the United States?

As a general point, I have argued for several years that Canadians strongly believe in guarding sovereignty when we are prospering. Thus, the model for Canada should be “smart sovereignty”, the kind of sovereignty that can withstand any pressures that arise from increasing openness to the world at large. Canada's sovereignty will be best exercised by using smart economic policies that improve our standard of living in a global economy. Smart means Canadians will have great confidence in themselves because we can outperform our competitors. Shutting ourselves off from the rest of world – like a western North Korea – will not make us smarter or better.

Smart sovereignty means that we will choose the best path for Canada. But the best path is not cutting off or cutting back trade with other countries, especially the United States. Instead, the best route for us is to become a **Northern Tiger** by taking advantage of the fact that Canada is poised to become the best-performing economy in North America.

A potentially major obstacle, however, has arisen in the past year. With September 11, 2001, we discovered how vulnerable our border with the United States can be and how this can affect our way of life in Canada. With terrorism, the US has focussed on protecting its citizens. If it means long delays at the Canadian border, so be it. For Americans, security seems to take precedence over trade with Canada, though the truth is that most Americans are not even aware that such a paradox exists or of the vast potential losses they could suffer if trade traffic with Canada were halted for even a few days,.

Canada and the United States have worked well together to deal with border security issues so far. But more remains to be done and the big question for Canada is how to move ahead in the future.

North America as a Unit

The starkest reality for Canadians is the fact that we have become much less European and more American in our culture and identity. This does not mean we are no longer distinctive. I believe Canada has a rich history and culture of its own. But our outlook has become distinctly North American.

Recently, I had an interesting experience when I spent a week in Germany just prior to this conference. In my discussions with colleagues, I found that I kept referring to differences between North America and Europe. Only sometimes did I refer to Canadian practices as something special. I was struck by this since I am usually so fiercely Canadian when discussing issues with friends from abroad. There are distinctions between Canada and the rest of North America, of course, in terms of our history, economics, social and cultural practices and politics. But there are also similarities.

Certainly, economic linkages dictate that Canadians are very much North American in outlook. And those linkages are powerful. As much as 85 percent of our exports are sold to the United States. At the same time, we purchase fully 25 percent of all US exports, making the two countries each other's -- and the world's -- largest trading partners. Indeed, Canada is far and away the United States' leading trading partner, dwarfing such countries as Japan, Britain and even Mexico. In the NAFTA context, about two-thirds of Canadian foreign direct investment is in the United States and Mexico.

Our relationship with the United States is therefore special. The US and Canada, particularly, have shared historical experiences, including being colonised by Britain and France, building national transportation networks and prospering from immigration, not to mention fighting shoulder-to-shoulder in two world wars, as well as in Korea and Afghanistan.

From the perspective of the United States, Canada provides important resources, including energy, agricultural goods, minerals and forest products. But Canada is steadily diminishing its traditional role as a hewer of wood and drawer of water. Canadians export substantial amounts of manufactured products, such as automobiles, and provide services to the US, including consulting and research. However, the US is certainly the dominant partner for Canada.

Still, since the United States finally abandoned dreams of annexation in the late 19th Century, Canadians have, for the most part, found it difficult to capture and hold the attention of the Americans, perhaps because the close and peaceful ties of more than 100 years make our country *not* one that Americans feel *needs* to be top of mind. The fact remains, however, that the overwhelming magnitude of our bilateral trade provides Canada with a distinct advantage in dealing with the United States. Our inter-country trade -- more than US\$1.5 billion in goods and services crosses the border in both directions Every. Single. Day. -- leaves the countries' economies intimately linked and co-dependent.

Because of these economic facts, Canadian people and businesses are increasingly thinking of their place in North America. Not only is trade in goods and services important, so is the movement of people. Canadian and Mexican citizens are found in large numbers in the US. Many Americans work in Canada and Mexico. Greater trade and people flows will affect our relations for many years to come.

So How Should Canada Position itself in North America

Given the economic realities of increased economic integration within North America, what is the best strategy for Canada to pursue?

Let me begin with what we should not do. We should not try to exercise our sovereignty by imposing high tariffs, quotas and stiff regulations that prevent integration with the rest of North America. I believe that would be foolhardy. We would only cut ourselves off by making it difficult for Canadians to exploit foreign markets. Making Canada inward looking will mean that businesses and people will look to the south to create jobs. Canada would be left out in the cold.

Another destructive strategy would be simply to react to the forces of integration on an ad hoc basis as problems arise. Under this strategy, we would wait until an issue comes to a head and then deal with it. If, for example, lumber producers find that they are no longer competitive, they would bring a trade action to make it more difficult to import products from other markets. Or, to protect jobs in times of rising unemployment, our governments might subsidize producers, whether in the film or the auto industries. Such policies deal with the issue on the table, but they do not provide a basis for ensuring strong economic growth in the future.

Instead, the best strategy for Canada and its North American partners to choose is to embrace economic integration by ensuring that goods and services can move freely across national boundaries. Free trade is a far superior approach to ensure that all partners enjoy the gains instead of choosing only one special group to receive special protection. Dismantling barriers to trade is bound to make all partners in North America better off.

The original NAFTA agreement has certainly benefited all three countries. Mexican growth has been stellar, especially in the North. One of the few highlights of Canada's economic performance in an otherwise poor period of economic growth was our substantial increase in exports to the United States. For its part, the US certainly experienced high productivity gains during the 1990s, a fact partly attributed to greater trade.

After a decade of free trade with the United States, Canada has looked to improve its overall relations with the United States. Greater mobility of people and businesses made it important to think of adopting new measures that would improve the efficiency of North American markets. Before September 11, 2001, some Canadians and Americans were already alluding to a North American perimeter, which would ease trade and people flows between the two countries.

With September 11, however, matters changed quickly. The United States feels vulnerable to terrorist attacks. Its borders had to be made secure. Canada and Mexico both witnessed tighter controls on people and goods going into the US. It was like a new tariff imposed at the border – it became costlier to trade in North America. Canadian and US authorities are working out a border agreement that would reduce the time taken to cross the border for most Canadian and American citizens, but make it far more difficult for others to enter each country.

The Need for a Big Idea

The vulnerability of the border is a key economic issue for Canada. Without the easy transit of goods and people, we might become a Northern Tiger, but with our largest market difficult to penetrate, we would, unfortunately be a toothless tiger. Without access to the US market, businesses and people would locate in the US rather than in Canada to serve the North American market.

One year later, we have dealt with the most critical issues at the border, though much remains to be done.

The United States is focussed on security, but understands the economic value of trade with other nations. From its perspective, it has much to gain from trade with Canada and Mexico – secure sources of energy products, low cost production of many manufactured products, high quality personnel and a close allies.

For Canada, access to the US market provides all the important gains from trade, particularly more jobs for its citizens.

The three North American countries must deal with a host of different issues to remove unnecessary trade irritants. All countries would gain from having the following:

- Greater ease of travel for those working between the two countries.
- A reduction in regulations that hinder the flow of goods, services, capital and people.
- An integrated energy market, including the development of northern sources of gas in Alaska and the McKenzie Valley.
- Co-operation in defence, such as in strengthening Northern security.
- Elimination of subsidies that distort trade patterns and reduce economic gains from trade.

Much can be gained from extending NAFTA with a new bargain that would improve the free flow of products, capital and people across our borders. As Wendy Dobson proposed in a paper released by the C. D. Howe Institute this year, we should entertain the notion of a Big Idea that would engage Canada and its NAFTA partners in a new arrangement that goes beyond NAFTA. A grand bargain dealing with many outstanding issues at one time would certainly provide a basis for a new partnership in North America.

I won't go on much longer. I don't want to leave you feeling like Lady Caroline Astor as she was being helped over the rail of the sinking Titanic. She looked down at the freezing scene below and said to nobody in particular: Well, I did ring for ice, but this excessive!

Domestic Policy Revisited

Many Canadians are indeed concerned about further enhancing our trading relationship with the United States.

Some are concerned about a loss of jobs. However, if we learned anything from the experience we had with the introduction of NAFTA, all partners gain from greater trade. Some will argue that Canada should not orient its trade solely to other parts of North America. Canada, instead, should look for opportunities of trading with Europe, Asia and other countries, they say. There should be no disagreement here. Greater trade with the US and

Mexico does not preclude trading with other countries. Canadians, in fact, now invest over a third of their capital in countries outside of the United States and Mexico – so improved trade with other countries will be important in future years.

Most importantly, many Canadians will be concerned that improved trade linkages with the United States will compromise our sovereignty. At worst, we would become a 51st state. The thinking goes that Canada's domestic fiscal, tax and regulatory policies will have to be harmonized with those of the United States in such a way that eventually Canada will, de facto, lose its independence.

The concern over sovereignty is very real to Canadians and it is a theme that runs through our historical consciousness. However, there is no evidence that increased trade with other countries eventually means that domestic policies will need to be harmonized. In many federal states, where goods, services and labour are perfectly mobile, we find that there are sub-national governments pursuing quite different economic policies. For example, many of Alberta's economic policies are quite different from those of Ontario or Quebec – and Ralph Klein is proud of it!. In the US, the state of Georgia's economic policies are quite different from those of California or New York.

Increased economic integration at the international level implies that Canada will need strategies that would maximize economic opportunities. With its northern weather and dispersed, well-educated population, Canada can provide advantages to people and businesses serving the North American market only if we have smart economic policies.

And we have been making substantial improvements to our economic policies. Recent economic growth, far stronger than that in the United States, is largely due to better fiscal policies. We have managed to cut government debt and lower taxes since at least the mid-1990s. The dividends from these actions are now being enjoyed.

But, we still have more to do if Canada is to become the Northern Tiger. Our total government debt, still over 70 percent of GDP, is one of the highest among OECD countries. Governments continue to use significant resources to provide public goods and services. Government revenues are 43 percent of GDP, similar to the average in Europe, but well above those countries enjoying robust growth in the past number of years, such as Iceland, Ireland and Australia. Canada does not yet stand out as an attractive place for business because our governments continue to pay public debt charges and often provide inefficient programs at high tax levels. Governments must continue on a path of improving efficiency in the delivery of program services, reducing debt and cutting taxes if we are to become the Northern Tiger.

Easing border obstacles and bottlenecks will make our smart domestic policies even more effective. I see the access to North America and other foreign markets as part of an overall strategy to make Canada a Northern Tiger. Instead of compromising our sovereignty, we could enhance it. A strong, vibrant Canada in future years will be the magnet that attracts ambitious people from around the world to live free from poverty, earn good incomes and enjoy the proven benefits of ever-freer trade under the North American umbrella.

Thank you.