

**UNLEASHING A NORTH AMERICAN TIGER:
The North American Public Good**

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Good afternoon. I am delighted to have this opportunity to speak to the Canadian Club in Chicago. I especially want to thank Canadian Consul-General Ann Charles for her support in ensuring that important issues affecting people on both sides of the border get heard and debated.

We all know the old saw that if you laid all of the economists in North America end to end, you still wouldn't have a conclusion. Well, perhaps. But I hope that I can defy that claim, if only for today.

I want to talk to you specifically about the U.S.-Canada economic relationship, and where it is helpful, the U.S.-Canada-Mexico relationship in the context of NAFTA.

No matter who wins the U.S. election — President Bush or Senator Kerry — a U.S. government will want to enhance the prosperity and security of the nation. It needs Canada and Mexico to support that mission. Similarly, many Canadians know that their relationship with the United States is critical to their nation's economy and security. They support a hard look at our relationship with US today.

I believe that we are on the cusp of a revolution in trading relations around the world, with regional *blocs* emerging as powers in their own right — in some ways assuming the role of the major nation-states of the 19th Century — all the while respecting their obligations and rights under the World Trade Organization.

I am convinced that North America, which is one of the most innovative and progressive regions in the world today, can thrive in such a system if it makes the determination to build constructively on the framework support of NAFTA. I realize that is a tall order, but the goal is achievable — and the cost to our businesses and to our standard of living of *not* doing it could be staggering.

I do not say that to be alarmist. But when we put on our global glasses, we see that Europe is dismantling internal trade barriers steadily and expanding its membership with fervour, creating an ever-more dynamic economic union. More to the point, Asia, particularly China and India, as we well know, are hugely-populated economies that are only beginning to assert their impact on the rest of the region and the world. Asian trading blocs propelled by either of these giants will be even more formidable challengers to U.S. and Canadian businesses and our economies than they already are.

In fact, in a recent *Commentary* written for the C.D. Howe Institute, my colleague at the University of Toronto's Rotman School, Wendy Dobson, wrote — and I quote:

Canadians must take more seriously both the opportunities and the potential risks of China's emergence as a major economic force. Canadian manufacturers will have to face the painful possibility that they can be priced — or pushed — out of their main U.S. market by low-cost, China-based producers and Canadian policymakers should recognize that China may eventually supplant Canada as the

largest trading partner of the United States. There is still time to adjust public policy to take advantage of China's surging growth — but not much.

I mention this just to illustrate the magnitude of the economic challenge that our two countries face — and as economies, we are joined at the hip, although some might wish it were otherwise.

It was to enhance that relationship and enrich businesses and consumers in both countries that Ottawa and Washington signed the Canada-U.S. Free Trade Act of 1989, which became the North American Free Trade Agreement, NAFTA, in 1994, with Mexico's accession.

Certainly, from the Canada-U.S. perspective, the free trade agreement is a major success. Each day, more than \$2 billion — that's in *real* dollars — of goods and services crosses the Canada-U.S. border in two-way trade. Canada and the U.S. are each other's largest trading partner. Canada is the largest importer and exporter of all goods and services with the United States, outranking Mexico, China — still — Japan and Europe. In fact, the single province of Ontario is the United States' third largest trading partner, after Canada as a whole and Mexico. Canada is also the largest outside supplier of the energy that powers U.S. factories and fuels homes and offices — yes, bigger even than Saudi Arabia.

The northern U.S. states are tightly integrated with Canada. For example, this state, Illinois is the most important trading partner for the provinces of Alberta and Saskatchewan, and second most important for Manitoba.

With the U.S. as the dominant partner, our dynamic economies are tightly linked, providing significant advantages for businesses to locate here. If Canada, Mexico and the United States play it smart by enhancing NAFTA, they could unleash a North American Tiger that will be a formative region for economic prosperity in all countries. This will be good for business and the millions of workers who prosper from a strong economy.

I will try to explain that vision for North America.

The world has changed a great deal during the past 10 years and we can no longer sit idly by, thinking that NAFTA's architecture is good enough for the future.

Canada, Mexico and the United States should consider a strategy to make North America a strong regional bloc in the world. We have common shared interests. And today, I want to discuss those interests and talk about how we could unleash a North American Tiger in the future and enhance what I call the North American Public Good.

With the U.S.-Canada Free Trade Accord and with NAFTA, our primary objective was to reduce obstacles to the flow of goods and services across national borders. This is the typical aim of most free trade agreements and the usual way we think about these accords.

However, I believe that now is the time to deepen that relationship — and for Canada to step up to the plate and greatly strengthen its military contribution to North American security, as well. Our focus, of necessity, should be on the Canada-U.S. space, while always keeping the door open to Mexico when it can take advantage of the opportunities. And we should never lose sight of the fact that what we are doing is building a North American regional economic bloc to compete with other emerging blocs around the world.

The responsibility for developing and presenting an overarching framework for a much deeper economic and security relationship rests with Canada; Washington isn't likely to take the initiative because as the world's only superpower, the U.S. doesn't feel the same pressure to act.

I will come to specific recommendations, most of them intended to bolster businesses on both sides of the border, in a moment. But first, I want to sketch for you the underlying logic for a far-reaching new accord.

We have to remember that along with mobility of goods and people — and millions of Canadians and Americans are linked as families and friends, as well as business and academic associates — come shared interests that go beyond dismantling barriers to trade.

Let me introduce a somewhat different way of looking at the concept of shared interests. As North America becomes more economically integrated, actions taken by Canada and the U.S. affect not only their own citizens but also all those living in the North American region.

And that is what I mean by the North American public good. Certain interests, including reducing barriers to trade, are commonly shared by Canada, Mexico and the United States — it is in the interests of all three countries to make sure public institutions are developed to promote the prosperity of a North American Tiger.

Let me give a clear example of a North American public good. We have seen that terrorism can strike hard against Canada's and Mexico's most important neighbour: the United States. The United States — with a great record of keeping its territory secure from attack by other nations — found that terrorism has no international boundaries and can strike innocent civilians on U.S. soil at any time. The eventual response to these security concerns was North American; it was not confined to the U.S. alone. Bilateral border agreements with Canada and Mexico were concluded to provide security to all of North America. In other words, security was not just an issue for the United States, but a public good for Canada and Mexico, as well, because terrorism could also be launched from or at either of those two countries.

It is not difficult to identify other examples of North American public goods and arrangements for enhancing them, such as the North American Air Defence Command (NORAD) and the Canada-U.S. International Joint Commission to manage the Great Lakes.

Those are only a few examples of North American public goods, or shared interests.. Public goods highlight that our economic relationship is about more than just trade — it also involves living in a North American space where three sovereign governments, working to protect the interests of their own people, also affect their neighbours sharing that space.

And it will be joint actions of Canada, the U.S. and, where possible, Mexico, that will foster and expand our economic prosperity in the future. We *can* create a strong, economically integrated North America, with businesses taking advantage of a large, internal market of close to 350 million people, while competing effectively in international markets.

However, important security concerns — most strongly felt in the U.S., but shared by Canada and Mexico — if not dealt with effectively, could serve as barriers to trade within North America. If the September 11 attacks are allowed to raise the costs of crossing the Canada-U.S. border they could dampen trade and make it less attractive for those serving the North American market to locate investments in Canada.

Certainly, the U.S. Ambassador to Canada recognized the importance of maintaining the strong trading relationship with the U.S. in the face of security threats when he recommended that Canada, Mexico and the United States negotiate measures that would secure the North American perimeter in a way that would provide greater security, while facilitating trade among the three countries.

So Canada, Mexico and the United States have recognized the importance of maintaining a strong and secure North America. I now wish to propose some common actions we can take to build a better future for citizens in all three countries by unleashing a North American Tiger.

Unleashing the Tiger is an enticing prospect and not nearly as dangerous as it sounds.

A framework for accomplishing this would have two major elements. The first would be to develop those institutions that would enhance North American public goods and require the joint action of the NAFTA partners. The second would be a further enhancement of the primary aims of NAFTA by facilitating trade and the mobility of people and capital across borders through deregulation. Both in my view are essential elements of creating a more prosperous North America. A more detailed look at unleashing the North American Tiger is provided by Bill Robson in a paper released by the C. D. Howe Institute last week.

As I mentioned, the outcome of September 11, 2001, demonstrated how important it is for North American governments to work together to ensure their security and defence. Governments are moving further in their cooperation to ensure that their citizens are protected by inspecting cargo ships abroad, sharing information to stop terrorist acts, tightening immigration and visa standards and looking at new missile defence arrangements against rogue states. The United States could act on its own to protect its borders, but much greater security can be achieved if Canada and Mexico are also involved. And Canada and Mexico both understand that their homelands must be protected, as well.

Another initiative that would deepen economic integration and promote the public good would be one aimed at setting common standards. Common standards would involve Canada and the U.S. abandoning their own and moving toward a new standard or, more likely, have Canada harmonize its standards to the U.S. model.

Another approach to the same end would involve mutual recognition. That is, each country would keep its own standards, but *accept* each others'. That would mean that goods would be tested, inspected and certified only once for the entire Canada-U.S. market.

On security matters, Canada and Mexico, as sovereign countries, obviously have foreign policies that are distinct from those of a superpower like the United States. While Canada did not participate in the Iraq war, it did contribute people and equipment and played a significant role in Afghanistan after the fall of the Taliban. In the future, Canada will have to define its role in protecting the North American public good when it comes to defence and security. Neither Canada nor Mexico will be superpowers, but they have unique roles in ensuring the safety of North America. And that should be an objective of foreign policy *today*.

Security and defence are perfect illustrations of North American public goods. However, many others come to mind, as well, and I will mention just a few of them before closing.

- The security of energy resources plays an even more important role today for a North American Tiger. Reliance by North American consumers on Middle East oil and, in future years, liquefied natural gas, does impose some special security problems when Middle East conflicts spill over to energy markets. One of the most secure sources of energy supplies is in North America — the NAFTA countries own oil and gas. Energy production has become less regulated in Canada and the United States. Mexico would have to move further towards a more integrated approach to enable Canadian and U.S. producers to help bring supplies to markets. However, all countries should make sure that their regulatory and tax systems do not interfere with sound economic decisions — whether to extract natural gas in Alaska or offshore Eastern Canada, or explore for West Coast oil and gas off British Columbia.

- Environmental public goods are also important. Mitigation of pollution and conservation of resources are beneficial in preserving economic growth in the long run by protecting consumers and industry from harmful actions that hurt the environment. With energy prices soaring, we have an opportunity to conserve usage and reduce pollution.

Canadian provincial, and U.S. state governments should strengthen acid rain-prevention agreements because airborne sulphides and nitrates need no clearance to cross national borders. Clean water is critical, too — and all governments have a role in making sure that water is properly priced so that users conserve. At the same time, our forest resources should be properly developed with conservation in mind — governments should design regulations and forestry taxes to provide the right incentives for reforestation, while making sure that they do not use anti-dumping and other protective actions that inhibit free trade in lumber and other wood products.

- North American governments could also develop joint programs to improve foreign aid to developing economies. Like the Asian Development Bank or the European Bank for Reconstruction and Development, a North American Development Bank, operated by Canada, Mexico and the United States, could create greater leverage in helping poor nations to improve prospects for economic growth. Foreign aid and the joint removal of tariffs would be a powerful tool in the claws of a North American Tiger, and its businesses, looking to broaden trading relations with the rest of the world.

I could discuss North American disease control, medical testing and other sorts of initiatives that would improve the effectiveness of governance in North America. It would require new co-operative arrangements to be developed in North America, either on a bilateral or trilateral basis. They all have one key and common feature – the payoff for us acting in concert is greater than what we can achieve individually. Whatever the arrangement, North America as the world's strongest economy, could make a quantum leap in competitiveness.

Before wrapping up, I would like to say a word about the critical role of trade facilitation. Facilitating trade among the NAFTA partners can be accomplished in different ways. The key aim is to reduce as much as possible those rules that inhibit trade and factor flows. The agreements could be reached bilaterally between Canada and the U.S., or on a trilateral basis, depending on the interests of the governments. Without going into a long list of possible measures, let me describe some key points.

Trade could be enhanced by moving to common tariffs for certain goods, which is already the case for computer parts sold to North America. Eliminating differences in tariffs for goods would remove the necessity of applying the complex country-of-origin

rules. Without moving to a full agreement on all commodities, the NAFTA partners, or just Canada and the U.S., could agree to common tariffs where there is currently little difference in levels. In some cases, such as steel, a common tariff could also reduce frictions arising from anti-dumping challenges that each country faces. It would also reduce the necessity at the border of confirming that goods comply with origin regulations.

Similarly, moving to some common standards would make it easier to ship goods across borders, as well as increasing competition among businesses to the benefit of consumers, who would enjoy lower prices.

Trade in services would be enhanced by easing rules to make it easier for employees of companies to operate in the NAFTA countries. More common professional standards, in fields such as medicine, would provide greater opportunities for skilled North Americans to work in more than just one jurisdiction.

North American capital markets could be integrated much more efficiently if countries seek opportunities to reduce obstacles to the flow of capital across borders. The most obvious one is to eliminate, on a bilateral or trilateral basis, withholding taxes on interest, dividends and other payments to encourage capital market integration. In this regard, Canada and the United States should finally conclude a new protocol that would eliminate interest withholding taxes, an idea that is now almost six years old. As well, Canada should extend the dividend tax credit to shares sold in the U.S. and Mexico because those two countries already have done so. All countries should examine their personal and corporate income tax laws to reduce barriers to cross-border mergers and acquisitions.

Capital market integration can be further enhanced by harmonizing financial regulations in North America. Harmonization is a fairly tricky problem because of the role of each government in regulating solvency, consumer protection and efficiency of financial institutions. However, with increased cross-border activity by banks and insurance companies, harmonization would enhance market competition to the benefit of consumers.

In short, let me say that in a world being defined economically by the development of regional trade blocs, we in North America already have a great advantage — we have in place a rules-based free trade agreement and we know it works. Now, we have a chance to make a great advance in NAFTA's ability to compete and thrive at the same time that we recognize and enhance the Public Good. Businesses and investors will benefit, but so will North Americans generally; they will enjoy higher incomes and better jobs. We should press our politicians to move ahead. It is an opportunity that all of us must seize — and soon.

Thank you.