

# Trade can brush in a new border

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NAFTA has outlived its usefulness, says economist **WENDY DOBSON**. If Ottawa won't cut a new deal with the U.S., the private sector will have to do so itself

**T**he most important policy issue facing Canadians today is our relationship with the United States. Washington has assumed a changed, newly assertive role in the world. Whatever they might think about that role, Canadians should expect Ottawa to take the lead in managing this swiftly changing relationship because it is critical to our future.

Aided no doubt by the North American free-trade agreement, but also by rapid economic growth in the 1990s, trade between the two countries has doubled in the past decade. Canada is the leading export market for 38 U.S. states; Ontario is the fourth-largest U.S. trading partner after Canada, Japan and Mexico. Canada and the U.S. are growing more interdependent: While more than 85 per cent of Canadian exports are destined for the U.S. market, combined U.S. exports to Canada and Mexico are 40 per cent more than U.S. exports to the 15-member European Union.

NAFTA was mostly about facilitating the movement of goods. Increasingly, however, bilateral trade consists of knowledge-based services. Firms are located in global supply chains spread across the continent, and in industrial clusters that are increasingly tightly interconnected internationally.

These patterns were just beginning to form when the Canada-U.S. free-trade agreement was negotiated in the late 1980s. The key implication for Canadians is that people, services, investment and technology must now move across borders to succeed.

In this context, even before Sept. 11, NAFTA had largely outlived its usefulness. The border delays after the tragic attacks greatly focused minds on how widely the effects of disruptions to market access can ripple through the economy. At a minimum, NAFTA needs to be deepened to remove the obstacles to the flows of people, investment and technology, all of which are critical to the growth of the knowledge economy, and for the interconnectedness of cross-border value chains.

The next steps will be shaped by three factors. One is asymmetric interdepen-

dence. While the United States dominates, North America's increasing interdependence means that if U.S. economic policies damage its two neighbours, they hurt U.S. prospects as well.

A second is Canadian political sensitivities. We are more comfortable with an integrated North American economy than a decade ago. But the next steps must be ones that preserve and enhance political independence and distinctive national institutions.

Third, political realities constrain what is possible. Canadian concerns about

economic security must be linked with U.S. domestic priorities to attract U.S. notice. And homeland security is the single overriding U.S. goal.

What's needed is a strategic framework that links security and defence with economic goals. The framework could have four parts, using as a platform the unprecedented level of co-operation within and across governments that underpins the "smart border" plan (drafted by Canada and the United States after Sept. 11 to work together on customs and border policing):

- A security initiative that creates an efficient, seamless border for low-risk cargo and NAFTA travellers; NAFTA visas for retirees, and agreed common procedures and shared intelligence to handle third-country migrants and inspect third-country cargo;
- A distinctive Canadian contribution of a world-class capability for North American defence;
- A secure natural-resources area, created by changing the rules of the game to rely on mutual recognition of each other's domestic regulatory and environ-



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mental regimes. If Middle East oil supplies to the United States were disrupted, Canada would have to ramp up production under NAFTA provisions. A 10-year program of regulatory changes, training and infrastructure development would be required. At the same time, Canada will want more secure market access for other natural resources, such as forest products.

■ A North American economic-efficiency initiative that includes broadening the NAFTA visa for business and professional people to technical people; a single North American standard in such areas as competition policy (one area where a NAFTA commitment has not yet been implemented); negotiating a simple customs union that eliminates the bilateral tariff and burdensome rules of origin.

This strategic package avoids the pitfalls of the conventional (read European) approach to deeper integration. Some North American sectors, such as autos and energy, are already more deeply integrated by policy and market forces. European-style liberalization, achieved by harmonizing existing domestic standards, regulations and policies to a common norm, is not applicable to North America. Here, all partners seek to preserve political independence, not achieve political union.

There will be barriers to overcome. The high degree of concern post-Sept. 11 has dissipated. Both countries have policy silos. Canada's Trade Minister has floated the idea of loosening NAFTA restrictions on labour, but at what price, if the policy stands by itself, unconnected to other priorities?

A strategic package like this one needs champions, preferably in a framework agreement between the U.S. President and the Canadian Prime Minister. But one leader is distracted by a potential war; the other by his domestic political troubles. Thus, the initiative must be spearheaded by the private sector — in the auto, energy and transportation industries — and among border states, provinces and cities (The new Canadian Council of Chief Executives' initiative could be the catalyst).

Canadians should expect a coherent strategy on North American economic security from their government, one that asserts our sovereignty. Small ideas or temporizing will get lost in the highly diffused (and highly focused) U.S. political system. Staying with the status quo will see our sovereignty eroded when we are forced to react to, rather than shape, our assertive neighbour's initiatives. The time to act is running out.

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