

North America: A vision for 2020

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It has been said that in order to see where you are going, you have to know where you are. There is little doubt that the North America of 2020 should differ substantially from what we know today. Trilateralism is undoubtedly a word to describe the desirable vision to be fulfilled in the future.

It is clear that market forces are moving us in that direction. Today, the U.S. exports 40 percent more to Canada and Mexico than to the European Union. For their part, Canada and Mexico are now heavily reliant on the the U.S. market for nearly 90 percent of their exports. For Mexico, people have also become an integrating force; by some calculations the U.S. population of Mexican origin is now $\frac{2}{3}$ the size of Canada's population.

Of course, the FTA and NAFTA have also played important roles. But they were negotiated as the Cold War was ending. During 1990's, the information and communications technology revolution has transformed part of the North American economy into production networks. Increasingly as well, a high value-added knowledge based goods and services profound in clusters that are strung across borders. And New research is showing that the productivity performance of traded industrial clusters is superior to those that serve the local market.

From a Canadian perspective this means that the provisions of NAFTA have largely out run their usefulness. NAFTA was mostly about goods trade. Now deeper integration is needed to remove the obstacles to flows of people, investment, technology and knowledge.

Business is ahead of policy. Presidente Vicente Fox's common market proposal is the only official vision, but it is ahead of its time. A common market frees up restrictions on the flows of people and technology as well as capital, goods and services, but the benefits of liberalization--a single price throughout the market--are usually realized through extensive harmonization of existing domestic standards regulations and policies to a common norm. Common institutions are necessary to administer their application.

Creating a common market is more difficult than it looks on paper. Strong political leadership and public support was required for the sustained effort that in Europe's case took 50 years. A vision of political union was the end point. Today, almost nothing could be further from people's minds in the North America. If a common economic space is to be contemplated, it must be in a way that preserves political independence and distinctiveness.

So if we are to begin in the present, it is one dominated by the realities of September 11th. The flip side of the openness of globalization is vulnerability. Homeland security is the top U.S. political priority and Canada and Mexico are perceived to have porous borders.

While the border is a tangible symbol of the new realities, I would argue the policy imperative goes much deeper. Canada and Mexico should completely reevaluate their strategies to accommodate the new U.S. position in the world. Too easily we overlook this fact because we are so used to dealing with U.S. dominance. Today, however, strategic, not incremental, change is the order of the day.

We need a Big Idea that attracts all three countries to a common purpose. Clearly that common purpose is to secure the North American economic space. A broad framework is needed that links security and defense with economic goals. I have proposed a framework that can be envisaged as having four pillars: security, defense, natural resources and economic efficiency.

On security, much is already being done to secure borders and separate low risk NAFTA cargo and people from high-risk flows. But significant issues remain. We need to erase the border for these flows, by moving security away from the border using electronic means. Substantial technology development and investment will be required to make this a reality. Equally important, bureaucratic coordination is needed to avoid, within NAFTA, policies like the INS sign in and sign out proposal. Even so, illegal migration remains a substantial issue between the U.S. and Mexico. With respect to third countries, much work is needed to deepen understanding and build trust in each other's procedures and policies to allow for mutual recognition.

On defense policy, a public debate is required in Canada after decades of declining expenditures on defense. Should we renew our North American Air Defense assets? Should we beef up our ability to monitor our ocean boundaries? Should we have highly mobile land force units equipped and trained to play roles in the natural disasters, peacekeeping, and moving Canadian Forces to international combat roles? Or should we stay with the status quo? Surely military security expenditures are one price Canadians are willing to pay for the openness on which they depend for their economic success. Is there a key capability in which we could achieve world-class excellence as our contribution to North American defense?

On natural resources, I think we need a secure North American natural resource area in recognition of the importance of natural resource endowments and trade in North America. As political uncertainty increases in the Middle East, so do uncertainties about U.S. crude oil supplies from the area. One way to reduce these uncertainties is to increase North American production. Under NAFTA, U.S.-Canadian energy trade is driven by market forces and much of Canada's energy infrastructure is already linked with U.S. markets. Since the 1980's, U.S. presidents have called for continental energy plans to coordinate with Canada and Mexico to access their exportable resources. These issues have always been difficult to deal with because of complicated and decentralized

regulatory policies, including Mexico's constitutional constraints. Since 2001 the North American Energy Working Group has been pursuing " closer energy integration " among the three countries, identifying areas of cooperation consistent with national sovereignties, and expediting the delivery of Northern natural gas.

With energy security a strong U.S. interest, it seems possible, within the framework of a Big Idea, to address both the US interest and the Canadian interest in more secure market access for forest products. A natural resources area could be based on the principle of mutual recognition of federal and state or provincial regulations in the three countries as a major step forward to address respective concerns. As events in the past two years have demonstrated, stand-alone disputes like softwood lumber have been insoluble, in part because of the absence of linkages and trade-offs that are possible in a large package.

The fourth pillar--promoting economic efficiency--looks like small change compared to the others, but it is fundamentally important. It includes the possible reduction or removal of bilateral tariffs in the customs union-like arrangement for the, greater facilitation of labor mobility, and measures to address regulatory obstacles that reduce competition.

- Doing away with bilateral tariffs and negotiating a common external tariff would leave the rest of each country's external policies intact while doing away with NAFTA's rules of origin. Customs inspectors with the longer police the border. Indeed a customs union already exists for computers and related products.
- Cross-border labor mobility needs to be freed up beyond what was possible with NAFTA. The TN visa should be extended beyond business and professional people to a wider range of technical experts better now frequent travelers in North America among value chain segments and clusters.
- A common competition policy is something that governments have already committed to. Progress has been modest because of national interests wishing to

preserve domestic markets. But with rising cross border transactions in transportation, telecommunications and financial services-each a backbone of integration-merger control is still more complicated than it needs to be.

It might be asked whether a common currency should be part of the package. Canada can have any currency regime it chooses as long as it is willing to pay the price. A common currency's price would be the loss of policy independence. The United States has shown no interest in the negotiating such an arrangement, so I conclude it is a red herring at the present time that represents a potential diversion of scarce leadership and negotiating resources.

In conclusion, it needs to be asked whether public opinion would support this strategic approach. Recent public opinion surveys indicate Canadians are more confident of their identity than decade ago. Indeed as the economy becomes more deeply integrated, national identity is on the rise. This suggests to me that our focus should be on changing the rules of the game to fit the new realities. We have a platform on which to build, one created for the Smart Border programs, based on an unprecedented level of bureaucratic cooperation both across and within the two governments. This momentum should be broadened to tackle the other pillars through ad hoc working groups that are charged to develop mutual recognition of each other's rules, policies, and regulatory regimes.