

REMARKS BY THOMAS d'AQUINO  
TO THE FINANCIAL POST CONFERENCE

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I first learned of Mexico's interest in a North American Free Trade Agreement some two and a half years ago. Responding to an invitation from the Business Council on National Issues, a delegation of senior Mexican business leaders visited Canada on their first-ever mission to this country.

The impression that they made upon us was strong and lasting. They spoke with enthusiasm about a new economic order in Mexico and the vision of President Salinas de Gortari to transform this country into a modern, industrial power. They were frank and realistic about the huge social and economic challenges that lay ahead, but expressed confidence that the path to prosperity in Mexico depended on embracing market principles, and on vigorously pursuing a policy of "apertura" -- the opening of the Mexican economy.

Even as early as then, our visitors made it clear that while they were anxious that Mexico be an active participant in the world trading community, their first interest was to look north towards new and dynamic partnerships with the United States and Canada. I must admit that the likelihood of a trilateral free trade agreement, encompassing all three countries, was still considered a long way off by my colleagues and I.

We were jolted into thinking otherwise in March of last year when we met Secretary Serra and our Mexican business counterparts in Cancun, and they made it clear to us that Mexico likely would move quickly towards the objective of a free trade association with the United States and Canada. And how right they were! On June 11, 1990, Presidents Salinas and Bush committed their two administrations to the negotiation of a comprehensive bilateral trade agreement.

The reaction in Canada to this swift turn of events was a cautious one, and I know that this disappointed and perplexed some of our Mexican friends. But the reasons for this caution are easy to understand. Simply put, Mexico has not figured prominently among Canada's political, economic, or strategic priorities. Moreover, the Mexico-United States initiative came hard on the heels of the Canada - United States Free Trade Agreement -- a very significant and controversial undertaking for Canadians that still is in the early days of implementation.

The response of the Business Council was a rapid one. Based on consultations with our members, and encouraged by our preliminary analyses<sup>1</sup> of the advantages and disadvantages of a North American free trade association, we urged, together with a number of other national business associations, that the Canadian Government be a full participant in exploratory talks that might lead to trilateral free trade negotiations. Canada's Minister for International Trade, the Honourable John Crosbie, advised the administrations of Mexico and the United States on September 24, 1990, that Canada would be a participant in the consultations.

The debate in Canada about the advantages and disadvantages of Canadian participation in a trilateral free trade association is well underway. I will outline for you briefly the case for participation, comment on some of the concerns that are being expressed in Canada, offer some thoughts on what form an eventual

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<sup>1</sup> The Business Council on National Issues sponsored a study in March, 1990, by Michael Hart entitled: A North American Free Trade Agreement: The Strategic Implications for Canada.

agreement might take, and conclude with some advice to my Mexican friends based on the lessons of the Canada-United States Free Trade Agreement.

### THE CASE FOR TRILATERAL FREE TRADE

#### **Mexico as an Opportunity**

A compelling reason for Canadian participation lies in the promise of Mexico itself. With a population of close to 85 million and a government that has begun to implement in a convincing fashion its commitment to opening its economy to international competition, it would be foolhardy to ignore the very significant trade and investment opportunities that are bound to arise. In a flurry of articles in the international business press in recent months, the potential of Mexico has been hailed as among the most attractive anywhere in the world. The Financial Times of London wrote, "Mexico has broken down one of the most formidable barriers in the path of economic take-off. President Carlos Salinas de Gortari and his youthful team...have persuaded a sceptical international community to take Mexico's development prospects seriously." One cannot ignore the problems of debt, poverty, unemployment, and the lack of infrastructure in Mexico. But let us not forget that some of the best performing economies in the world today were saddled with similar problems thirty years ago. In those countries, leadership and the intelligent harnessing of market forces made all the difference. I predict that there is a good chance that the same thing will happen in Mexico.

### **The Scope of a Trilateral Market**

The scope of a combined Canada-Mexico-United States Free Trade area would be truly impressive. It would incorporate a population of some 362 million, a GNP of over U.S. \$6 trillion, and total trade in excess of U.S. \$225 billion. It is true that the economic weight of Mexico among the three countries is by today's criteria relatively small given its share of GNP and the purchasing power of its people. However, most economists predict that with strong inward flows of investment and improved export performance, Mexican GNP growth will improve steadily and offer increasingly attractive opportunities to its North American partners. Canadian economist Richard Lipsey puts it this way: "The growing Mexican purchasing power will buy local and imported goods in large quantities. The additional demand for imports so generated will provide significant new opportunities for U.S. and Canadian firms to sell in Mexico."<sup>2</sup>

### **Canada's National Interest**

Some sceptics in Canada argue that given the small amount of reciprocal trade and investment between Canada and Mexico, the promise of a growth-oriented Mexico and of a trilateral market do not in themselves warrant Canada joining a North American Free Trade Agreement. There are additional, and in my view, convincing reasons -- both economic and strategic -- for thinking otherwise.

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<sup>2</sup> Richard G. Lipsey, Canada at the U.S.-Mexico Free Dance: Wallflower or Partner?, C.D. Howe Institute Commentary, 1990.

If Mexico and the United States proceed on their own and negotiate a free trade agreement, a pattern in hemispheric trade will begin to emerge that has popularly come to be called the "hub and spoke" model. The United States will be the hub, and Canada, Mexico, and possibly other states, in the not too distant future, will be the spokes. Under this model, the United States would be the only country with tariff free access to the markets of each participating country. The spoke countries -- Canada and Mexico among them -- would have tariff free access only to the United States market. In such an arrangement, the United States would be the beneficiary of trade diversion. The same principle would apply to direct investment. As a businessperson, I would be tempted to locate my plants in the United States in the knowledge that I could supply, on a tariff free basis, the markets of the spoke countries.

The economic arguments for avoiding trade and investment diversion are strong ones. But there is a broader, strategic consideration as well. If the United States concludes separate economic agreements with a number of nations, but none of those countries have similar agreements with each other, the already immense bargaining power of the United States in relation to each of its bilateral partners will be significantly enhanced. This could invite political and economic problems that are best avoided.

The dangers of a hub and spoke approach to North American trade are plain enough to see. The more desirable alternative is a model that is common in trade practice around the world and that has withstood the test of time. It is known as plurilateral regionalism where each of the trading partners shares with all the others broadly the same privileges and obligations. This is the approach that the Government of Canada has chosen in entering the consultations with Mexico and the United States on the possibility of free trade arrangements

linking all three countries. It is an approach that best serves Canada's national interests. I believe that it is an approach that best serves Mexico's national interests as well.

### CANADIAN CONCERNS ABOUT TRILATERAL FREE TRADE

There are a growing number of individuals and organizations in Canada that are voicing opposition to the idea of a trilateral free trade agreement. The most commonly heard argument, in particular from the Canadian trade union movement, is that Canadian jobs will be threatened by Mexico's massive reserve of low-cost labour. I always have had some difficulty with this point of view. It ignores what we have learned from the experience of decades of global trade liberalization; that high-wage countries have achieved enormous gains from lowering tariffs, not only against one another, but also in relation to low-wage, poor countries. It also fails to recognize a fundamental economic principle -- that the exchange rate is the mechanism that helps equilibrate trade, or as Richard Lipsey reminds us, "What matters in international competition is not how much local labour is paid in terms of purchasing power. What matters is how unit costs of production compare internationally at the going exchange rates."

Another criticism of the trilateral free trade concept comes from those who say it will undermine multilateral liberalization. This argument was heard many times during the debate in Canada about the Canada-United States Free Trade Agreement. In fact, it is an argument that has been largely discredited. The Canada-United States initiative was welcomed by GATT officials, and by leading trade authorities in many parts of the world as a catalyst for many of the reforms

now being sought in the Uruguay Round. Moreover, more than fifty preferential trade arrangements have been sanctioned under GATT Article XXIV.

Stiff opposition to a trilateral initiative also comes, predictably, from those who remain adamantly against the existing Canada-United States Free Trade Agreement. They argue that the extension of the free trade agreement to include Mexico is the next step in a conspiracy, led by United States multinationals, to maximize profits at the expense of Canadian and Mexican sovereignty, and the well-being of workers in both countries. Of course, such a point of view is unfounded and nonsensical, and the temptation to simply dismiss it is a strong one -- except that it continues to garner considerable support among Canadians, particularly at this time when Canada is in the grip of a recession and unemployment is on the rise. I will return to this subject at the conclusion of my remarks.

### CANADA-MEXICO-UNITED STATES -- THE OPTIONS

Canada, Mexico, and the United States are now engaged in consultations on how to approach a North American arrangement. A number of options are being discussed by interested parties in all three countries. One is that Mexico simply accede to the existing bilateral agreement; a second is that Mexico and the United States conclude a bilateral agreement and bring Canada into the agreement at a later date; a third possibility is for Canada and Mexico to conclude their own separate bilateral agreement after the Mexico-United States agreement is in place; and a fourth option is to negotiate a so-called "core agreement" among the three countries that would cover free trade in goods, services, investment, and dispute settlement. To this core agreement would then

be appended a number of arrangements germane to the special interests and concerns of each signatory.

At this rather sensitive stage in the tripartite consultations, it is vital that all the parties be flexible and open-minded, and that the various options be studied with great care. I will not attempt to assess each one in detail, but I will offer a brief comment on why, from a Canadian perspective, some have more appeal than others. Asking Mexico to accede to the existing bilateral arrangement would raise fears in Canada that it would be reopened. This would not be a popular move and likely would be opposed by a great number of stakeholders in Canada. The Canadian Government, and my own organization, the Business Council, hold the view that a reopening of the Canada-United States Free Trade Agreement would be unacceptable.

Concluding a Mexico-United States agreement first, and then inviting Canada to join later, raises another set of problems. Interests vital to Canada may be touched upon in the first negotiation, and Canada's bargaining power in the subsequent negotiation may be compromised as a result of not having been at the table. I realize that this sequential approach has many supporters in both Mexico and the United States, and I have heard the arguments in both Mexico City and Washington as to why: for example, that a bilateral negotiation is easier than a trilateral one; or that Canada may be a spoiler in the discussions; or that Canada's heart is not in it. Consider the other side of the argument: do we really want to give de facto legitimacy from the outset to the "hub and spoke" model? Will Mexico not be a beneficiary of Canada's experience and know-how at the bargaining table? Will a trilateral negotiation not offer the best hope for a balanced and politically acceptable arrangement?

As to the third option -- the negotiation of a separate, Canada-Mexico bilateral free trade agreement -- I would not rule this out but neither would I give it much hope. Given the relatively small amounts of trade between our two countries, it might be difficult to raise a sufficient degree of enthusiasm in either nation for such an arrangement.

Perhaps the most promising approach is the core agreement concept complemented by arrangements designed to accommodate the special needs of the individual signatories. Such an approach, plurilateral in nature, would allow for additional signatories so long as they were willing to accede to the rights and responsibilities contained in the core provisions. It is the approach that offers a balance of consistency and flexibility. It is the approach that establishes an appropriate framework for expanding the trilateral free trade agreement to include, eventually, other states in the hemisphere.

### FREE TRADE -- LESSONS FROM CANADA

Mexicans often ask me, "why did Canada seek out a free trade agreement with the United States, and how has the initiative worked so far"? There are some interesting lessons to be learned in the answers to these questions. It is important to remember at the outset that Canadians took the first steps; we did so, overturning a long, and deeply-rooted antipathy within Canada to the idea of continental free trade; and we did so largely in the face of scepticism and indifference in the United States.

Canada's objectives in making this historic and far-reaching initiative happen were to provide our exporters of goods and services with more secure and expanded

access to the huge United States market. I readily admit that part of our motivation was fear of American protectionism. But in large measure, we acted in response to our expanding trade and investment ambitions. We knew that an agreement would encourage our enterprises and our workers to become more competitive, and that more open trade in the long term would lead to a quicker adjustment to global change. We also knew that continued prosperity in Canada depended heavily on our ability to export successfully. The hard lessons we learned from our dealings with the Americans on trade and other economic issues over the years, taught us that our bilateral relations would improve if governed by effective binational institutions and the rule of law. We rejected outright the idea of a customs union or common market. Our goal was, and remains, to expand economic co-operation with the United States while ensuring that Canadian sovereignty remains fully protected.

More than two years have passed since the passage of the Canada-United States Free Trade Agreement. The Agreement is still in its infancy, and therefore difficult to assess with any accuracy. On the whole, I believe it is a success, and this view is shared by the members of the Business Council. The Agreement has had a significantly positive impact on investment -- both in the lead-up period to its implementation, and since. It has generated new jobs, although it is impossible to quantify how many. Slowly, but surely, it is establishing a new and more predictable institutional order between Canada and the United States. It is having a salutary influence on perceptions in both our boardrooms and in the workplace by encouraging Canadians to think globally. Among foreign investors from outside North America, Canada's entry into a comprehensive, bilateral free trade relationship with the United States is almost universally praised. The Agreement is not without its costs -- and most of us who supported the initiative predicted they would come. The adjustment to the new environment has resulted

in some plants being shut down and jobs lost. Critics say that the current economic difficulties being experienced by Canada are attributable largely to the Agreement. They are mistaken, choosing to ignore that after seven years of one of the highest growth rates in the world, Canada is experiencing a cyclical downturn. But then again, they have been wrong before. They predicted that free trade with the United States would lead to the dismantling of Canada's social programs, to the extinction of our culture, and to the despoliation of our environment. What we are hearing from some of the ingenuous critics now was prophesied some time ago by one of the Agreement's foes. "Every sparrow that falls from the sky," he said, "will be blamed on free trade."

Those of you here today, from Mexico and who are engaged in advancing Mexico's bold free trade initiative, will be able to identify with many aspects of the Canadian experience that I have described. The road ahead will not be as easy as it seems. There will be ups and downs. The move will carry with it a certain cost. And do not be surprised if the free trade initiative generates a great deal of controversy in the United States, in Canada, and even in your own country. But keep one thing firmly in mind -- the long term benefits of a properly negotiated free trade agreement are indisputable. The outcome for Mexico will be one that your children will thank you for -- greater prosperity for all, a confident and productive partnership with your two northern neighbours, and a brighter window on the world.

