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**FOREIGN INVESTMENT POLICY-MAKING:
THE CANADIAN STATE IN THE GLOBAL ECONOMY**
by

CLAIRE TURENNE SJOLANDER, B.A., M.A.

A thesis submitted to
the Faculty of Graduate Studies and Research
in partial fulfilment of
the requirements for the degree of

Doctor of Philosophy

Department of Political Science

Carleton University

Ottawa, Ontario

October 31, 1989

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ISBN 0-315-58992-2

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ABSTRACT

This dissertation on the Canadian state's response to foreign investment challenges mainstream conceptualizations of the state in the discipline of international relations. It argues that in order to understand international economic policy making, we must understand the process by which state managers learn about the international economic environment. Following Robert Cox's work, it suggests that the hegemonic status of capital historically resulted in the functional separation of politics and economics for policy makers. This separation led policy makers over time to accept a "natural" international economic order, and effectively removed political considerations from policy making targetted at the international economy.

The gradual breakdown of the international economic order has implied that international economic policy has been re-politicized, and that state managers must now seek new information about the international economy when they devise policy. The model of state action put forward contends that this information is filtered through domestic structures. State managers do not possess any extraordinary knowledge of the international environment despite their position within the state apparatus, and the information which they do receive is that mediated through domestic forces.

Through historical comparative analysis, the dissertation argues that in the creation of the Foreign Investment Review Agency in Canada, state managers accepted a series of assumptions about Canada's location in the international political economy. These assumptions included the depiction of Canada as a branch plant economy, the belief that it had enough foreign investment, and could continue to attract investment no matter the conditions which the state might seek to impose on foreign investors. Through a review of statistical data, however, this study finds that these assumptions were increasingly irrelevant to Canada's position in the international pattern of investment flows by the early 1970s, the precise time during which FIRA was created based upon these beliefs. The manner in which state managers defined their knowledge of the international environment, therefore, was critical in determining the ability of FIRA to carry out its mandate as a regulator of foreign investment. The Agency effectively sought to regulate an environment which no longer existed.

ACKNOWLEDGEMENTS

Many people have given of their time to assist me in the preparation of this dissertation, and though they cannot all be mentioned here, they should know that their help was much appreciated.

To Professors Mytelka, Molot and Dolan, whose insight, guidance, patience and friendship made all the difference, I owe a debt which I can never repay.

To those who gave generously of their time in interviews and consultations on this project, I express my sincerest appreciation.

To my friends and family, who have lived with this thesis at times as much as I, I express a heart-felt thank you.

Finally, with much love and respect, I dedicate this work to my parents, Robert and Evelyn Turenne.

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INTRODUCTION

In a 1988 World Politics review of neorealism and neoliberalism, Joseph Nye argued that "[o]ne of the most thought-provoking questions in international relations is how states learn. How do national interests become defined, and how do these definitions change?" (1988:238). Indeed, the question of how individuals charged with policy formulation within the state apparatus -- state managers -- perceive or understand the global environment in which states exist is central to the analysis of international relations. Perception of an international event or situation, after all, underlies the impetus to formulate an "international" policy. Without an answer to Nye's question, we are confounded when we attempt to assess how state managers respond to changes in the international environment, or on what basis they attempt to bring about changes within that environment.

Ironically, despite the fact that the state has long been conceptually identified as the central actor in the study of international relations, the discipline has not demonstrated a particular concern with the identification of the processes by which state actors interpret the global environment. In effect, much of international relations literature has left

unconceptualized the basis upon which a state is said to "act". Nye's question is all the more ironic when one considers that the principal or "mainstream" U.S. approaches to international relations, most of which are state-centric, are themselves inherently unable to provide an answer as a result of their failure to develop a theoretical analysis of the state. Addressing this failure, identifying the mechanisms by which state actors "learn" or interpret the international environment, and the process by which these interpretations change, is the task of the theoretical examination underlying this dissertation.

Asking the question of how state managers learn may enable us to interpret the change in Canadian state policy reflected in the move from the Foreign Investment Review Agency to Investment Canada some eleven years later. In 1973, the minority Liberal government of Pierre Trudeau introduced Bill C-132, which was to become the Foreign Investment Review Act. Presenting the legislation before the Standing Committee on Finance, Trade and Economic Affairs, as he had earlier to the House of Commons, Industry, Trade and Commerce Minister Alastair Gillespie spoke of the bill as "a necessary supplement to those measures that encourage strong Canadian-controlled business enterprises," a

"necessary part ... of over-all industrial strategy or industrial policy" (1973:26/6). The bill would create the Foreign Investment Review Agency (FIRA) to monitor foreign takeovers and the establishment of new foreign-controlled business enterprises in Canada, and to advise Cabinet as to whether these investment proposals would be likely to confer "significant benefit" on the Canadian economy.

Bill C-132 was an unusual step in the history of Canadian state responses to the challenges posed by foreign direct investment. Its distinctiveness came not so much from the fact that state managers were attempting to control the flow of foreign investment to Canada as from the fact that Bill C-132 suggested that sectoral approaches should be eschewed in favour of more comprehensive control. More than this, however, its introduction pointed to an apparent realization that previous state policies had not always been successful, and underscored a new and growing concern about the condition of the Canadian economy and the role of foreign investment within it. In his presentation to the committee, Gillespie himself appeared to link certain failures of Canadian economic development to the extent of foreign ownership of Canadian industry. In particular, he suggested that previous state policies

reflected a "laissez-faire approach that has ... resulted in our having so large a part of our economy under foreign control", and had not ensured the "fulfillment of certain of our economic goals such as diversification of exports and export markets, and increased Canadian innovativeness and decision-making capability" (1973:26/6). Bill C-132 signalled a recognition on the part of state managers that there were certain general costs associated with a high degree of direct foreign investment.

This cautious view of direct foreign investment was bluntly reflected in the opening paragraph of the Foreign Investment Review Agency's own guide to the businessmen who would be asked to comply with the new act. Canadian policy would now be to welcome direct foreign investment, but only if it could be determined that such investment would be "likely to yield benefits to Canada as well as to the investor" (FIRA, 1974:3). Having accepted that direct foreign investment brought with it identifiable costs, further investment could only be justified if state managers could point to tangible benefits.

On December 7, 1984, the Foreign Investment Review Agency was served notice that its days as guardian of the Canadian economy were coming to a close. Bill C-115

was tabled in the House of Commons, signalling the intention of the Mulroney Government to replace FIRA with Investment Canada. Industry minister Sinclair Stevens pledged that the new agency would send "a message to the world that, once again, Canada welcomes investment Investment Canada with its new mandate and new approach, will help pull Canada out of its shell and will reinvigorate this country with a flow of goods, capital, technology and ideas" (Investment Canada, 1984:1). Suddenly, the Canadian investment watchdog was issuing colour brochures with new logos, touting "the spirit of enterprise". The costs of foreign investment were no longer the focus of policy. Rather, the Investment Canada Act defined its primary purpose as encouraging "investment in Canada by Canadians and non-Canadians" alike (Government of Canada, 1985:sc. 2). Within eleven years, the political calculus which had given rise to Canada's Foreign Investment Review Agency no longer held, and assessments of the value of foreign investment to the Canadian economy appeared to have changed.

Having observed a change in perception, the question of how state managers learn leads us to ask why. How do state managers come to change their understanding of the patterns of direct foreign

investment and the consequences of these, and why do changes in understanding occur? Why, in the case of FIRA and Investment Canada, does the assumption of costs associated with foreign investment play so heavily in the former, and only seem a footnote to the latter? Answers which point simply to a change in government or personnel clearly do not provide a satisfactory explanation; by 1982 the Liberal government of Pierre Trudeau had begun to make changes in the administration of FIRA which resembled those incorporated into the Investment Canada of the Mulroney Conservatives. We can argue that the state had "learned", to borrow Nye's terminology, and that this learning was reflected in its changing orientation to foreign investment, but we cannot explain the process by which this learning had come about.

Part of the answer, we will argue, lies in the fact that there has been a change in the pattern of direct foreign investment through the 1970s and 1980s, and that this change has had implications for Canada. The question of state manager learning, however, forces us to build a bridge between change in the international economic environment and the perception of such change by state managers. Changing foreign investment patterns do not in themselves guarantee that state managers will

recognize them, that they will be interpreted in any particular manner, or that they will be acted upon. Through this, Nye's question of "how states learn" becomes more precisely one which seeks to link international patterns of foreign direct investment (which reveal changes) with the perceptions of policy makers as to their country's place within this international pattern. This question clearly has implications for the definition of state policy objectives as well as for the choice of policy instrument.

While the Foreign Investment Review Agency is the focus of this research, it is not in itself the purpose of this study. This is not to reiterate the all too prevalent argument that FIRA was merely an exercise in symbolic politics, an agency created to placate the increasingly vocal nationalist concerns by a government in a precarious parliamentary minority position. It does us well to remember that FIRA was only one of a number of policy initiatives undertaken through the 1970s by the Canadian state aimed at the redefinition of Canada's international economic position, and as such reveals important assumptions of policy makers about Canada's role in the international economy. [1] Because it focuses upon the assumptions behind policy,

however, the research contributions of this work are not to be found so much in the impressions it seeks to question about the creation of FIRA as they are in the theoretical challenges a model of state learning poses to traditional state-centric formulations of some mainstream international relations theory. The thesis challenges notions that state managers somehow respond directly to changes in the international economic environment. Rather, it contends that the very complexity of global economic change often confounds state managers, and thus limits their capacity to understand directly the international economy.

Previous analyses (see Clement, 1975, Resnick, 1977, or Carroll, 1986, for example) have commented on the extent to which the foreign investment debate in Canada has been tinged by class-based interests -- Canadian business, labour, and the nationalisms of the new middle class. Taking off from some of these analyses, we contend that these debates have conditioned the nature of what state managers have been able or willing to learn. In fact, during periods of rapid international economic change, the thesis presents the argument that state managers must rely upon predominantly domestic class-based interpretations of their country's position within, in this case, a global

pattern of foreign investment flows. As such, this is not a work centered upon the study of personalities or socio-psychological models of decision-making; rather, it seeks to identify the broad structural patterns linking domestic and international environments in the process of state manager learning.

The task of developing a model of how Canadian state managers understand the international economy -- and in particular, how they have understood their country's position within the global pattern of foreign direct investment -- has been divided into six chapters. Chapter One focuses its attention upon the elaboration of a model of state learning. It seeks to build the bridge between changes in the international economic environment and state managers' perceptions of these changes. In defining this model, the argument presented in Chapter One goes beyond either system or society-centered theories of state action. It "brings the state back in", to borrow Theda Skocpol's phrase, and defines state managers as actors operating within parameters established by both domestic and international forces. We are making an explicit a priori assumption here that while systemic and societal processes may limit the range of policy choices, state managers make these choices based on their own

particularistic understanding of the target of policy.

Central to this argument is the notion that neither domestic nor international circumstances are stagnant, and that state managers are formulating policy in response to their interpretations of these changing circumstances. These interpretations are, during periods of rapid international change, based predominantly on societal debates. In effect, policy decisions may be made in response to interpretations of the international economy which bear little relationship to ongoing processes of economic change simply because the assumptions behind policy, reflecting the perceptions of various social classes or class fractions, may be incommensurable with economic reality. In its simplest formulation, therefore, Chapter One argues that state managers face particular "learning" difficulties when confronted with periods of rapid international economic change, and that we can only understand these difficulties when we focus our analytic energies on defining the relationship between state managers, the domestic and the international environments, and in so doing, defining the processes by which state managers learn.

Where Chapter One argues that state managers face difficulties when learning about rapid international

economic change, Chapters Two and Three begin to lay out the nature of that change. Chapter Two presents an overview of theoretical work dealing with the post-war evolution in the international investment strategies of the multinational corporation (MNC). These studies reveal that the reasons for MNC investment have been changing since the 1950s; first motivated by the need for a foreign presence to secure and protect international markets, and today more broadly undertaken in order to manage the risks of international competition. This review is central to our argument that there has been a change in the pattern and nature of foreign direct investment, and that this change began during and has continued since the debates surrounding the creation of FIRA in Canada. Chapter Two also illustrates the extent to which the norms guiding international investment have been challenged in the post-war era, painting a picture, along with the reality of changing MNC strategies, of the climate of uncertainty confronted by Canadian state managers when they moved to regulate foreign investment. Chapter Two provides us with a position from which we can critically raise questions as to the usefulness of the traditional assumptions about direct foreign investment promulgated in debates about foreign investment in Canada and

embodied in the creation of the Foreign Investment Review Agency. In so doing, it begins to allow us to see the extent to which assumptions about international economic behaviour and the reality of such behaviour may differ.

Chapter Three examines more specifically the Canadian experience with foreign direct investment. As Chapter Two argues that there has been a change in the manner of and motivation for foreign direct investment, Chapter Three demands that we define how that change has affected Canada. After all, given that we are seeking to understand how state managers learn, it is crucial to elaborate what they should be learning. It traces the historic Canadian position in the pattern of international investment flows, allowing us to understand the basis of state manager perceptions of Canada as a country which would always be attractive to foreign investors regardless of the barriers which might be imposed upon such investment. This assumption is the first of four key dimensions which are used throughout the remainder of the thesis to demonstrate the evolution of state manager interpretations of Canada's changing position in the pattern of foreign direct investment flows. The other dimensions -- balance of payments (particularly capital shortage), the extraterritorial

application of home country laws, and the extent to which foreign investment has a positive or negative impact upon Canadian economic development -- are introduced as they appear in the foreign investment debates outlined in greater detail in Chapter Four. Chapter Three also details the changes in global investment flows since the 1960s, changes which reveal the extent to which the form of, and competition for, investment has dramatically increased -- between advanced industrial countries (AICs) as well as among less developed countries (LDCs) -- with real implications for Canada. This review is important for it paints a picture of the Canadian "location" in international investment flows against which state policy will be evaluated, particularly in Chapter Six.

Chapter Four uses the theoretical model outlined in Chapter One and the backgrounds of Chapters Two and Three in order to evaluate the creation of the Foreign Investment Review Agency. Having established that there has been a change in the foreign investment climate, we now turn to the specific question of how state managers come to understand that climate. Using committee briefings, official reports and statements, and interviews, it traces the way in which foreign investment was interpreted by various class actors

within Canadian society, and points to the manner in which one group -- identified here as the new middle classes -- were particularly successful in presenting their perspective to state managers. Regardless of the fact that empirical evidence existed to suggest that Canada's location in the pattern of international investment flows was beginning to change with the onset of the global economic crisis of the late 1960s and early 1970s, we see in Chapter Four, though a discussion of debates around our four key dimensions, the extent to which the analysis of Canadian state managers was bound to traditional understandings as well as to the perspectives presented by different classes or fractions. Chapter Four illustrates concretely the extent to which assumptions about the nature of foreign investment, both generally and in Canada, play a role in the formulation of policy and must be understood in order to evaluate policy.

Chapter Five traces the increasing incommensurability between assumption and economic reality. Chapter Four has provided us with an evaluation of the assumptions embodied in the creation of FIRA, and Chapters Two and Three have outlined changes in the pattern of foreign direct investment flows. While we have already seen that assumptions did

not correspond precisely to economic reality, Chapter Five looks at the consequences of this non-correspondence, up to and including the creation of Investment Canada to replace FIRA. Here we focus upon the importance of the interests of large capital, both Canadian and foreign (operating in Canada) in challenging the assumptions behind FIRA, and in leading to a new understanding of the Canadian place in the pattern of international investment flows. Together, Chapters Four and Five do not argue that there is any one "correct" interpretation of the Canadian relationship to the international economy, or that the views of capital have proven to be "better" than those of a nationalistic new middle class. Rather, these chapters trace the process by which state managers learn and accept new assumptions, and emphasize the importance of understanding domestic political struggle when seeking to identify the learning process of state managers.

Chapter Six, finally, evaluates the successes and failures of the Foreign Investment Review Agency through an historical and statistical overview. Rather than contending that the Agency was or was not a symbolic gesture as reflected in the allowance and disallowance rates, the chapter argues that the Agency was inherently

limited in its potential effectiveness because it was designed to regulate an international environment which was increasingly less relevant to Canada's international location. The contrast between the "branch plant" assumptions accepted by state managers in the creation of the Agency and the reality of international investment no longer as focussed on the establishment of international subsidiaries reveals both the limits of state policy making and the importance of understanding the interpretations of state managers as they define policy.

This dissertation employs comparative historical analysis as its primary research method in the discussion of state policy and foreign direct investment. The identification of the class interests articulated to state managers is derived from the storehouse of public testimony, official reports, hearings and statements, newspaper coverage, and House of Commons debates available on the issue of Canada's foreign investment policy. In its discussion of changing international investment flows, the thesis presents a statistical picture compiled from a variety of national and international organizations -- particularly documentation from FIRA, the Organization for Economic Cooperation and Development (OECD), the

United Nations Centre on Transnational Corporations (UNCTC), Statistics Canada, and the U.S. Department of Commerce.

Theda Skocpol has argued that it is possible to generalize about a very limited class of historical phenomenon through the adoption of "comparative historical analysis with selected slices of national historical trajectories as the units of comparison" (1979:35). Of course, as well noted by Skocpol herself (1979:38-40), the method is fraught with its own difficulties. There are limits to defining the precise historical "slices" to fit the logic of a particular comparison, and one must never forget the fact that the historical periods being compared are always contingent upon each other rather than independent, as theoretically "pure" comparative historical analysis would suggest. Comparative historical analysis does however serve to provide, in Skocpol's terms, "a valuable check, or anchor, for theoretical speculation" (1979:39). Of little relevance without theory, it can be used effectively to reveal, and set the limits to, theory. Comparing Canadian state managers' historical conceptions of their country's location within a pattern of international investment, to the changing nature of foreign investment, provides us with the methodological

tool to engage in cautious speculation about the manner in which state managers in industrial democracies more generally understand the international economic environment in the formulation of state policy.

ENDNOTES

- [1] Through policy papers, public statements, diplomatic overtures, and official policy, the Canadian state attempted to address questions of Canada's international competitiveness. FIRA was in fact part of a more general policy program designed to diversify Canadian markets, to reinforce and develop Canada's manufacturing and technological capabilities, and to encourage the cultivation of areas of specialization within the Canadian economy. In addition to FIRA, we find the creation of the Canada Development Corporation, of Petro-Canada, and of the Canadian International Development Agency (CIDA), as well as the articulation of the "Third Option" of Canadian trade policy and the pursuit of a "contractual link" with the European Economic Community.

The extent to which these concerns continue to occupy both academics and policy makers is patently obvious in studies of trade and the role of the state in shifting a country's comparative advantage. See, for example, the collection edited by Duncan Cameron and Francois Houle (1985). In addition to the numerous publications of the Science Council of Canada and the Economic Council of Canada, the issue has been of much concern to the Canadian government itself; witness the Department of External Affairs' key foreign policy statement of the Mulroney years [Canada. Department of External Affairs (1985)].

CHAPTER ONE

THE STATE AND THE INTERNATIONAL SYSTEM: A THEORETICAL PERSPECTIVE

Joseph Nye's question as to how states learn is the takeoff point for this first chapter. We want to discover the way in which changes in the international economy are interpreted by state managers. In attempting to do so, this chapter will outline a model linking the international economy to domestic structures, in order to locate the sources of information or knowledge which play a role in the shaping of state policy. This discussion, located at the level of domestic and international structures, rather than at the level of the individual policy maker, will allow us to derive general hypotheses about the nature of state manager learning.

While the development of a model of state manager learning is the aim of this section of the thesis, it is useful to first look briefly at the way in which the concept of learning has been defined by mainstream international relations scholars. Nye defines learning as the process by which knowledge is developed through study or experience (1987:578). Ernst Haas' study of the potential for state learning in the building of collaborative regimes leads him to conclude that learning has taken place "when the actors adopt new

rules of behavior that make use of new information or knowledge"; that learning "means that the prevailing dogmas are being relaxed sufficiently to allow for the introduction of new information" (1980:390). These authors see the process of learning as taking place primarily on an individual level, leaving decision-making theory as the analytical tool of choice, or as the result of international interactions, of collaboration between states on a regional or global level.

These approaches to learning suffer from two main flaws. To begin, largely because they tend to focus on the building of collaborative regimes, they embody a liberal bias viewing learning as a positive process. While these authors agree that learning involves the acquisition of new knowledge, such a process does not inherently imply that this knowledge encourages the choice of "better" policy or leads to "better" behaviour. In fact, learning only implies that our understanding of reality has changed in some way, even if this leads to the reinforcement of existing beliefs. Learning does not inherently signify a positive change; state managers whose perception of reality has changed are not necessarily more collaborative as a result.

Perhaps more importantly, the failure of these

international economic environment. How do we understand the state, how do we define it? Without such a definition, we cannot begin to detail the process by which state managers interpret the international economic environment.

Defining our understanding of the state will also help us to make explicit the links between the state, civil society, and the international environment, in fact, situating the state within its broader context. The specification of these links will provide the groundwork for the detailing of a model of the state's interaction with the international economic environment, an interaction which we will claim is necessarily mediated by domestic interest groups or classes. This model will allow us to understand the interests behind particular state policy choices, and the interpretation of the international environment encapsulated in those interests.

APPROACHES TO STATE ACTION IN INTERNATIONAL RELATIONS

Ikenberry, Lake and Mastanduno have dichotomized the principal perspectives on the state in international relations as system-centered and society-centered approaches (1988). These approaches have been prevalent in the study of international relations, yet neither can

provide a satisfactory theoretical analysis of the Canadian experience with the regulation of foreign direct investment. In fact, as we will find, neither can provide us with a satisfactory perspective on the state itself. Illustrating the failing of these analyses, however, helps to clarify the conceptual tools that we need to develop a theory of state action relevant to policy decisions, such as the regulation of direct foreign investment, which target a "national/international" problem. Furthermore, each perspective allows us to identify the environment external to state actors, an important step, for it is the interpretation of the international economic environment which is of particular concern to us here.

System-Centered Explanations

System-centered explanations, or system-level theories, are easily identified as the most distinctively "international" of the approaches devised to guide our understanding of state action in the international environment. [1] System-level theories assign primacy to international structures as the "first-cut" to understanding political and economic environments. Kenneth Waltz, for example, argues that the international system should be viewed as distinct

from any individual nation-state (1979:40), and that a theory of the international system should allow us to derive propositions about the subordinate level of state action. In this form of theorizing, the international system effectively defines the parameters of state action, and often its actual behaviour.

We see this same focus on the level of the "international" in regime analysis. Regimes are simply the "norms, rules and procedures agreed to in order to regulate an issue area" (Haas, 1980:358). The international system becomes the cause or condition of state action and the source of knowledge for state managers. For example, the application of national treatment principles to foreign investment was long held to be the cornerstone of an implicit regime dealing with international direct investment (see Lipson, 1985). International regime theory focusses on the policies which states adopt in order to maximize the benefits of participation in the international community, and embodies a normative orientation as to the desirability of creating or maintaining particular international orders. To varying degrees, depending upon the analyst, the international regime inherently limits the range of state action. From this perspective, the analytic task is to identify a "regime", whether explicit or implicit,

dealing with international investment, in the expectation that such a regime would constrain state behaviour [2].

While the notion of an international investment regime may be useful to our investigation of foreign investment policies, neorealist analysis has its problems in providing us with a guideline for state manager learning. Richard Ashley has argued that neorealism identifies states as "the national individual actors whose interests and calculating actions and coactions give form and moment to the international system" (1984:244). The problem here is that states do not exist in a social context. Because neorealist systems-level analysis does not define the generative structures of the international and domestic political economies which have constituted states as particular kinds of social actors, temporally and contextually located, these theories cannot provide us with a useful theory of state action. We cannot know how state managers learn because we do not understand their interrelationship with domestic and international structures. We are thus limited to devising a theory of state action which contends that state managers respond to changes in the international system as rational actors. Beyond an assumption of rationality, we cannot

explain the choices of state action and any changes in these choices -- and the assumption of rationality has long been severely challenged in international relations.

From a completely different normative perspective, Immanuel Wallerstein's world systems theory also identifies an international system, locating the problems associated with the autonomous formulation of state policy within the processes and contradictions of international capitalism (1974). Once again, we see that the logic of the international system, this time a specifically capitalist international economy, sets the parameters for state action. Capitalist competition and expansionism provide the motives for the state's use of force, and the logic of state action is to be found in the processes underway in the international system. The interests of the capitalist state are most often found in the interests of the dominant capitalist class; in fact, the relative strength of the state in the world economy is a function of the degree of coalition between the institutional state and the capitalist class (see Wallerstein, 1974:403, for example). Through time, the logic of the system becomes so pervasive that policy choices which would challenge the system are not perceived to be realistic options.

Where neorealist systems analysis lends primacy to the state as the motivating actor, world systems theorists have the opposite problem; lending ontological primacy to the level of the system. In so doing, they reduce entities such as states and class agents to being "effects of the structure of the [capitalist] world system" (Wendt, 1987:346). The international system becomes the actor and the social structure of the world system is thus effectively reified. These critiques are not limited to world system theorists; we see echoes of the same problem in Waltz's description of ideal system-level theory. As Wendt observes, there seems no recognition that "only human action instantiates, reproduces, and transforms ... [international] structures" (1987:345). This reification is particularly alarming for it completely removes the political from a discussion of state action; states do no more than passively implement the conditions necessary for system reproduction. The state does not even make a self-maximizing, rational, "as if" calculation of its interests; actions are undertaken completely in response to the dictates of a pervasive international order. While a theory of state action is not possible within neorealist analysis, which gives primacy to state agents and thereby removes them from

their structural -- and social -- context, such a theory is also not possible from a world systems perspective, which conceives states to be passively dragged along by the inevitable and ongoing march of international structures throughout history.

All systems-level theory, regardless of its normative orientation, understands national capabilities and state choices as a function of the nation-state's position within an international system. Such a perspective would lead us to expect that we could explain the Canadian state's decision to create FIRA, to make changes in the administration of FIRA, and finally to replace FIRA with Investment Canada, by reference to aspects of the international system found in changing investment patterns. Whether these changes are understood as rational, value-maximizing responses to new international circumstances, or as inevitable adaptations to the capitalist world order, the state itself remains an unexplained and unconceptualized actor. The relationship between international investment and state policy with regard to that investment becomes straightforward in systems-level analysis; policy makers simply respond to changes in the international environment. In sum, we are faced with a reactive model of state policy, where changes in the

international environment lead directly, with a greater or lesser time-lag, to adaptations of state policy.

One of the greatest difficulties with this perspective is that it leads us to conclude that a country's location in the international political economy is so unambiguous as to be interpreted in only one way by a coherent group of policy makers or state managers. While it is conceivable to contend that such action by one state as a declaration of war against another can be interpreted in a relatively unambiguous manner by state managers (although the choice of response may not be unambiguous), it is far more difficult to argue that the complex pattern of international exchange which makes up the area of foreign investment can be so easily penetrated by prescient analysis. If the pattern of international transactions was never subject to change or upheavals, it would be possible to contend that, over time, state managers would come to a consensus over their country's place in the pattern of international investment flows. Under the dynamism of the international economy, however, we cannot assume that an international "input" is unambiguously processed through a state computer in order to generate a uniform "output", nor even that stable -- or hegemonic -- world orders are never

subject to change.

Finally, and perhaps indicative of a more fundamental failing, systems-level analysis leaves us with a whole range of inexplicable state policy. If state managers develop policy directed to the international environment solely in response to changes in that environment, how can we explain modifications of international state policy in the absence of international economic change? Because systems-level explanations all too often specify for us the nature of the important or relevant "input" to state policy (in this case, the international environment), we are unable to trace the genesis of new state policy which does not appear to be responding to international stimulus. Until we define the state within a broader social context, we cannot come to grips within this perspective with the question of how states learn. Despite the critiques of systems-level analysis, we cannot reject its contributions to our understanding of an important source of state manager learning.

Society-Centered Explanations

Society-centered explanations, the second predominant form of analysis identified by Ikenberry, Lake and Mastanduno, locate state policy options within

"the ongoing struggle for influence among domestic social forces or political groups" (1988:7). Politics becomes the input to decision-making. State policy is a function of domestic politics, whether as a reflection of the preferences of a dominant class in society, or as a result of a struggle for influence among various interest groups. As Skocpol has outlined, "government" was thought of as an arena within which groups or classes contended or allied with one another in the shaping of public policy decisions -- decisions which were understood to be "allocations of benefits among demanding groups" (1985:4). Within society-centered analysis, the level of the international system is almost an afterthought; state policy is the result of pressures from its domestic environment. [3]

Society-centered approaches, rather like the system-level theories reviewed above, reflect a lack of focus on the state actors themselves; state managers are not perceived to be autonomous from important classes or social groups, and their function lies in reflecting the desires of successful or "winning" interest coalitions. State managers do not play a determining -- or even constraining -- role in formulating and electing to pursue particular policy options. State managers themselves do not provide an input to decision-making;

they are akin to an empty shell reflecting the desires of society's politically powerful groups or classes. Society-centered approaches risk obscuring any intervening role which the state may play in shaping interests in the policy process. In the words of Ikenberry, Lake and Mastanduno, society-level analysis "focusses exclusively on ... the 'demand' for policy, but not its 'supply' " (1988:9).

A society-centered framework of analysis leaves us with a state as non-agent; the state is, in effect, irrelevant to the understanding of politics, be they domestic or international. This Eastonian "black box" approach to understanding state action is reflected in Theda Skocpol's observation about the role traditionally played by the state as a focus for analysis in American thought in the immediate post-war era:

"Government" was viewed primarily as an arena within which economic interest groups or normative social movements contended or allied with one another to shape the making of public policy decisions. Those decisions were understood to be the allocations of benefits among demanding groups. Research centered on the societal "inputs" to government and on the distribution effects of governmental "outputs". Government itself was not taken very seriously as an independent actor.... (1985:4).

Stephen Krasner has observed that from the late

1950s to the mid-1970s, "the term state virtually disappeared from the professional academic lexicon. Political scientists wrote about governments, political development, interest groups, voting, legislative behavior, leadership, and bureaucratic politics, almost everything but 'the state'" (1984:223). This black box approach to the state is one which explicitly or implicitly questions state autonomy, and stresses the degree to which policy choices are shaped by domestic political actors and decision-making processes (Ferguson and Mansbach, 1985:1). The consequences of this assumption are evident. Without acknowledgement of the state as an autonomous agent, capable of defining goals in at least a partially independent fashion, no theory of state action can -- or even needs to be -- developed. The net effect of the trends to system- and society-level analysis led Krasner to conclude in 1976 that, "[i]n recent years, students of international relations have multinationalized, transnationalized, bureaucratized, and transgovernmentalized the state until it has virtually ceased to exist as an analytic construct" (317). Society-centered analysis, as with system-focussed theory, tends to obscure the state as an actor in the decision-making process. Where system-level analysis would lead us to conclude that

Canadian state actions to regulate direct foreign investment are a consequence of international investment patterns and changes within these, society-centered analysis would find explanations for state decisions exclusively in terms of the desires of the dominant capitalist class.

While society-centered explanations may not tell us much about the nature of the state and the specific manner in which state managers interpret the international environment, they do tell us something about the domestic constraints under which state actors formulate policy. Most importantly, for the purposes of this analysis, these perspectives lead us to focus on classes or societal groups. Theories based upon the identification of classes or the differentiation of groups are, at their fundamental level, theories about society, the distribution of power within it, and the ability of the powerful to influence policy outcomes in their favour. The differentiation between classes and groups, while at an empirical level perhaps moot, is a relevant one for it points to a contrast between theoretical perspectives on the manner in which power is allocated within society.

The elite analysis of Pareto, Mosca, Michels, and even of C. Wright Mills, Domhoff, and Dahl, defines

power as an attribute which rests with a particular societal group -- an elite. The elite in society by virtue of personal characteristics (smarter, stronger, wealthier), or organizational hierarchy (the role which an individual fills) has "power". Power belongs to the elite (which is not necessarily a closed group); it is something which the elite has and holds. The masses (everyone not a member of the elite) are held captive to the elite's desires because they do not hold power, in effect because they have no power of their own.

This approach provides a useful contrast to those who look at society from a class perspective. While some of the elaborate schemes to determine which individual is a member of which class closely resemble the attempts of elite theorists to determine who is a member of the elite, these tasks are actually different because they relate to a different understanding of how change comes about within society. To begin, the class analyst is examining relationships and not attributes, in particular, the relationship of an individual to the means of production. This focus on relationships introduces the notion that power resides in all classes, rather than in one particular "elite" class. The difference between classes lies not in the allocation of power "attributes", but rather in the ability of a class

to control the processes fundamental to capitalist society found in the relationship between capital and labour -- processes which necessarily include certain policy decisions taken by state managers. Society-level analysis teaches us that there is a relationship between the state and society -- just as systems-level analysis points to a relationship between the international environment and the state. Class approaches to society inform us of the possibility for change within society, for the source of politics becomes the outcome of the interplay between class actors. Different classes, not simply a dominant class, become crucial to analysis as potential predictors of change.

As George Ross (1978) has argued, perhaps the most interesting challenge to class theorists has been the emergence of an intermediate strata -- a class neither properly labour nor capital -- in advanced industrial societies in the post war era. A variety of definitions have been offered to identify this class, most of which are formed around the basic thesis that the new middle class does not own its means of production, and yet does not engage in labour which directly produces surplus value. In the main, the new middle class does intellectual, rather than manual, work (Ross, 1978; Ng, 1983). Access to this new middle class is controlled

through education, which provides the individual with skills allowing him to perceive himself to be different from the worker. The new middle class perceives its work as a career, in which efforts will be rewarded with promotion, while labour sees its work as a job to be endured (Ross, 1978:173). This class has traditional links to the petite bourgeoisie (largely made up of independent shopkeepers), although its political agenda is ambiguous and uncertain. Contemporary studies of class, therefore, assign a key role to the potential for the mobilization of the new middle class to serve the interests of either labour or capital.

Class analysis tends to be focussed, naturally enough, on the class composition of particular societies, and the relationship of particular classes to individual states. This would suggest that class analysis would minimize a discussion of an international dimension -- that classes or fractions thereof are primarily useful in discussions of the domestic context. Classes or groups are not defined only within national contexts, however. While most significant as actors within societies, because they seek to influence the policy of a given state, classes or groups are also actors on the international stage. Keohane and Nye's pioneering of the concept of transnational actors forced

us to acknowledge that domestic societies were not isolated from each other, interacting only through their respective state agents. The fact that classes do have an international component (international capital, for example), will be seen to have profound implications for the question of state knowledge.

In the end, though, society-centered analyses guide us to examine competing societal claims, the support for foreign investment review by the new middle classes in Canada, for example, or the opposition to such review by certain segments of the capitalist class. As in the case of system-centered perspectives, however, these analyses do not offer insights into the political calculations taken by the state to reconcile, or choose between, competing demands. We have no insight into why state managers choose to reconcile interests through one set of policies at one point in time, and through a different set of policies at another point in time. These perspectives do not allow us to theorize about the state's knowledge or understanding of the country's location within an international environment.

Clearly, our traditional understanding of the state as a variant of the billiard ball (the rational, value-maximizing actor) or the black box (the arena in which social conflicts are resolved), while providing

insights into the state's environment, cannot answer the more specific question of how state managers gain the knowledge upon which they act in formulating policy. International and societal constraints do exist, and cannot be ignored. Their existence, however, cannot be assumed to be determining on the nature of state policy. We must turn our attention when developing a theory of state action to identifying how these constraints are translated to state actors; to re-iterate an earlier point, we cannot assume that state managers can always identify the changing constraints under which they operate. In order to do this, we will briefly consider the state itself.

THE LOGIC OF STATE ACTION

In part arising out of the limitations inherent in pointing to non-state actors or processes as determinant of state behaviour, state-centered explanations have surged to some prominence in social scientific study and analysis over the last decade. Theda Skocpol has argued that this renewed focus on the state signals "a paradigmatic shift ... underway in the macroscopic social sciences" (1985:7), although one not wholeheartedly embraced by the discipline of international relations. The birth of a state-as-actor

approach, which understands the state as both an institutional organization or structure and as an actor, made up of individuals engaging in goal-oriented behaviour, and not always acting in a homogeneous, coherent, or rational fashion, has, at a minimum, defined the state as an important intervening actor in the policy process. It is in such intervention that we can understand the Canadian state's creation of FIRA.

A state-as-actor focus cannot return to a narrow view of state institutions alone. System- and society-level approaches have clearly taught us that we must define the state within a context (although these analyses have not always been successful in presenting that context); and this context must include both the international and the domestic environments. In fact, we will see that this context is crucial in mediating the state manager's knowledge about the international economic environment. Any examination of state actors, even within a perspective which stresses that the state may behave as a social agent, must endeavour to understand the limits or opportunities placed upon state action as the outcome of a combination of system and societal pressures. As Theda Skocpol has argued, "an existing economy and class structure condition and influence a given state structure and the activities of

the rulers. So, too, do geopolitical environments create tasks and opportunities for states and place limits on their capacities to cope with external or internal tasks or crises" (1979:30).

States, once conceived in theory as objects worthy of study, must definitionally be understood to be relatively autonomous from social classes and groups, on the one hand, and determinant international structures, on the other. The state remains an actor with a dual anchorage found in class divided, largely domestic, socioeconomic structures, and an international system of states (Skocpol, 1979:32), but the state does not behave as if it represented only one particular social class or group, or as strictly the metropole or hinterland in an international division of labour. Such a depiction of state behaviour would necessarily lead to the conclusion that contexts and circumstances do not change, a conclusion which can hardly be substantiated. Rather, the Janus-faced state is continually in the process of adjusting to changes in the international and domestic economic and political realms. In a world of states integrated into a single global economy, as United States analysts discovered after the economic shocks of the early 1970s, the problems of economic change, whether or not these are defined or chosen by state

actors, necessarily bear upon both the domestic and the international political economy, and the state's policy choices within these spheres. [4]

If we accept as given the need to define the constraints and opportunities presented by the environments in which state action takes place, we must also seek to define the nature of that state. From Fred Block's alternative formulation to the narrow limits of the relative autonomy thesis, we find the hypothesis that "state power is sui generis, not reducible to class power" (1980:229), that the state directly defines policy, and that classes, regardless of their policy preferences, do not. This is an important distinction, yet one which does not imply the absence of a relationship between classes and states, but rather acknowledges that states have a particular role within domestic society and the international environment.

Within a capitalist society, the state has an interest in maintaining the capitalist accumulation process, of acting in the long term interests of the capitalist class. Yet, the state is not a homogeneous "entity"; it is made up of individual decision makers. These individual decision makers, whom we refer to as state managers, are those in the executive branch of the state, Cabinet ministers and senior public servants,

while the state itself is made up of the executive, legislative, administrative, and judicial organizations. We must, however, resist the temptation so prevalent in international relations to think of these state managers as somehow uniformly constrained by, or uniformly autonomous from, the class struggle within their domestic and international environments.

For these state managers as individuals, themselves concerned with their future careers, failure to create and maintain conditions of international competitiveness may raise "the spectre of fewer resources available internally and [of] effective challenges by outside or inside forces to the state manager's control over the state apparatus" (Block, 1980:230). Strengthening the accumulation process provides resources which can legitimize the state's authority within the domestic and international environments [5]. Yet, while the Canadian state, for example, might be a capitalist state, it is not strictly beholden to the capitalist class or to any particular fraction of that class over the short term, within the dynamics of a particular class struggle and its discrete effect on national policy. The state may even appear to act against the interests of dominant capitalist fractions as it seeks to preserve the legitimacy of the capitalist structure within domestic

society as a whole, as well as the legitimacy of the position of individual state managers over the state apparatus. [6]

While state managers or officials have a measure of autonomy by virtue of their pursuit of goals related to their own position within the state structure, they also derive a measure of their autonomy from their interaction -- however sporadic -- within the international environment. States are uniquely positioned to interact on a common footing with other states, unlike other domestic or international actors. As Gourevitch (1978:911) reminds us, this autonomy is important, for constraints under which the state operates do not in themselves define policy, no matter how compelling they may be. As he writes, "[s]ome leeway of response to pressure is always possible, at least conceptually." Or, as Rianne Mahon has argued, "[t]he state is not a simple transmitter, whose policy outputs are a direct function of political inputs" (1984:38).

The state is not a black box, not even a self-maximizing capitalist black box. To begin, the capitalist class is itself not homogeneous, and different interests are represented in the concerns of different fractions of that class. Rianne Mahon

contends that the various organs and branches of the state can be understood as "representatives of the interests of the classes and class fractions present in a social formation" (1984:39). The various institutions which make up the state act as the conduits by which differing interests, either of different social classes, or of fractions of one social class, are "heard" by the state, thereby allowing policy formulation in response to the conflicts and compromises inevitable in the presentation of these different interests. And yet, again to quote Mahon, the structure of representation of these interests is unequal; just as relations among these classes and class fractions is unequal, "so too does the quality and form of their representation within the state vary" (1984:39).

Mahon's work is crucial in illuminating some of the reasons why not all policy initiatives can be adopted, why some choices are likely to be pre-eminent. Certainly, Block outlines some of the factors which condition choices; primarily the structure of capitalist social relations. Mahon takes this one step further, arguing that in different countries, with different political, economic and social histories, the interests of different fractions of the capitalist class as well as of other classes or fractions may assume different

positions within the state's representational structure. The administrative arm of the state becomes a forum through which class struggle continues. In Canada, for example, she contends that the Department of Finance has been charged with a central role in policy formulation, and in the maintenance of an equilibrium of compromises preserving existant class relations, a charge consistent with the hegemonic position within the capitalist class of financial capital (see Naylor, 1975a,b, for a detailed elaboration). With its broader mandate, the Department of Finance has traditionally been in a unique position to provide coherence to the definition of state "interests". As she writes,

[t]he structure of representation embedded in the state executive-administrative apparatus is ... the mechanism through which new policy compromises may be formulated in a manner consistent with the maintenance of a pattern of hegemonic class domination. The demands of particular forces are translated by their state representatives, and in the process certain possibilities are filtered out (1984:41).

Crucial to note, within this argument stipulating the veritable limits to the type of policy initiatives likely to be put forward (limits conditioned by the balance of class forces within the state apparatus, as these are defined in part by the historical pattern of

capitalist class relations), is the notion that the hegemonic class fraction does not always "win". Political conditions dictate that bargaining over policy cannot always find resolution in a "winner take all" non-compromise. The flexibility needed to securely maintain the leading position of a particular fraction of capital necessitates that concessions occasionally be made in favour of a non-hegemonic class or class fraction (Mahon, 1984:42). Mahon's model is useful for the picture it paints of state managers involved in reflecting the broader class struggle. She acknowledges, however, and this needs to be underlined, that the structure of representation within the state is variable; that patterns of representation effectively change by reference to changing class struggles within domestic society. It is this condition of change which needs to be examined more closely at this point, for it is argued here that the broad international economic upheavals of the late 1960s and 1970s had implications for the nature of the class struggle within Canada.

The structure of representation embodied in the state apparatus is crucial for our question of state knowledge, for it is through the state apparatus that state managers often gain the knowledge which forms the basis of their decisions. State managers -- both

government and bureaucratic leaders -- rely on bureaucratic structures for the information which guides the choice of policy. However, political leaders need not only rely upon established bureaucratic structures for knowledge or interpretations of the international environment; in Canada, the expansion over the last two decades of the Prime Minister's Office (PMO) and the Privy Council Office (PCO) provide mechanisms by which non-specifically bureaucratic or "independent" assessments of problems can be provided. Bureaucratic departments and agencies are reorganized, created or eliminated just as the societal interests and claims represented therein also shift. Bureaucratic reorganization takes place, as well, in order to respond to the changes in the international economy -- changes which may also be giving rise to shifting class interests within national boundaries, and thus reinforcing the move to bureaucratic adaptation. Neither process of reorganization takes place overnight or even quickly; vested bureaucratic interests and the demands of organizational structure make such change unlikely and perhaps even unwise.

As is implicit in this previous discussion, there are different processes of state manager "learning". State managers include two fundamentally different

groups of individuals -- political leaders, and senior bureaucrats. As Robert Cox points out, there is a difference between political decision makers and "those who inform those decision makers about what their options are" (1987:261). This difference in role makes each susceptible to particular kinds of information, and to a particular kind of learning. While both political leaders and senior bureaucrats are constrained by the need to reproduce the structures of capitalism, political leaders in advanced industrial democracies must also secure their electoral futures. For Cox, the civil service leadership is thus characterized by its relative autonomy from these directly "political" considerations (1987:294), and as such is more likely to develop a long term definition of "national interest", albeit within the objectives of the particular class or fraction represented by the particular bureaucratic structure in which these senior bureaucrats find themselves.

Political leaders, by virtue of their role and concerns, must at least appear to be more sensitive to societal pressures which do not seem to easily find representation within existing bureaucratic structures. Bureaucratic reorganizations do not take place every time new claims emerge from society, and existing

bureaucratic mandates and definitions of the national interest may make it difficult for these claims to be readily accommodated within existing bureaucratic mandates. Political leaders are most likely to seek extra-bureaucratic sources of knowledge when the conflict between the existing policy guidelines and international practice begins to reveal itself, in part through the growth of societal claims reflecting this "gap". Bureaucratic structures offer solutions to policy agenda by reference to interests which they represent. When traditional solutions no longer appear to be adequate, extra-bureaucratic structures may need to be consulted. These represent different or emerging interests, reflecting different assessments of the international environment -- interests to which established bureaucratic structures have not yet responded, or do not incorporate. Whether or not extra-bureaucratic sources of information are consulted depends upon the explicitly political calculations of political leaders. We must never forget that we are dealing with the state managers of Block's liberal democracy, and that the rise of new societal expectations may have electoral implications, and thereby implications for the future career of the state managers themselves.

As we have argued above, classes are social groups which have power, and in this power we find the basis of struggle between the perspectives and understandings of different classes or fractions. The very dynamism of struggle can imply that the bureaucratic representation of interests becomes "unrepresentative" of new class interests. International "realities" are construed by social agents, and constructions of reality are always contextual. By their very nature, bureaucracies are crystallizations of a specific balance of class forces, and as circumstances alter the nature of society and the definition of interests (however slightly), bureaucratic structures are left to "catch up" with those changes. The worldwide rise of the new middle classes (professional workers, intellectual labourers), for example, has challenged models of class struggle defined only in terms of capital and labour, as well as the bureaucratic structures representative of those predominant interests. In the Canadian case, it will be argued that the growing influence of the new middle class outside of the state bureaucracy effectively challenged state managers to seek extra-ordinary sources of knowledge in determining foreign investment policy. As Mahon has argued elsewhere, the creation of regulatory agencies (of which FIRA, by virtue of its

restricted mandate, is not a perfect representation) may indicate precisely a situation in which new class perspectives must be incorporated within the state structure, and through which the rights of capital, as the hegemonic class, may be compromised in order to maintain a social structure which continues to support the viability of state managers in their positions (1979:191). Seeking sources of knowledge outside the existing bureaucratic structures may result in state managers situating their policy response outside existing structures as well.

Our notion of the state thus far can be laid out simply. State officials are constrained by the pattern of capitalist class relations in which the state is embedded. Different state institutions effectively "represent" the interests of various parts of that social structure, if only by virtue of an historically and politically defined mandate. Bureaucratic officials, whether or not they perceive themselves to be representatives of particular classes or class fractions, act within administrative structures which reflect those interests -- and, as goal oriented individuals, often act within these structures to bargain effectively for those interests. The fact that compromises must be made in order to preserve the

stability of the existing social structure necessitates that state officials be flexible enough to move beyond the interests of specific groups, a task perhaps more easily accomplished by political leaders rather than senior bureaucrats. State managers of either type are not, however, etherial agents without ties to societal structures. Furthermore, just as societal structures are dynamic and inherently subject to pressures for change, so too is the representational structure of the state subject to change. It is during these periods of uncertainty which may be precursors to change, most visibly seen in the rise of new societal claims reflecting a growing gap between bureaucratic policy guidelines and international practice, that political leaders, are most likely to solicit information and knowledge from non-hegemonic bureaucratic structures or social groups.

To this point, we have discussed the problem of how state managers gain knowledge largely by establishing the domestic context in which they operate, and by defining a model of state structure which can represent the interests of particular classes or fractions in the compromises surrounding the formulation of state policy. This is only part of the picture, however. We have also pointed out that states interact in the international

system, a fact which helps to define them as autonomous agents. Before we continue, this point needs some further elaboration. As Richard Ashley describes, the question of state autonomy is as intimately related to the international system, as it is to domestic social and economic demands. He persuasively argues that;

[t]he state's claims to autonomy do not necessarily derive solely from the state's role as mediator of pluralistic domestic demands, from the state's institutionalization of prior demands made upon it, or from the state's manipulations of historic symbols [T]he state's claim to autonomy may also derive from its historic adaptations to the requisites of participation in an international rule system (1980:21).
[7]

Not only does a state adapt to the international system, but participation in it creates patterns of interaction which provide the state manager with channels of information, and reasons for expectations about the international structure. Ashley's balance of power logic provides "rules" for interstate relations, and these rules can create room for international cooperation. As Brian Barry has remarked, "[i]nternational affairs are not a pure anarchy in which nobody has any reason for expecting reciprocal relations to hold up. In economic matters particularly, there is a good deal of room for stable expectations" (cited in

Lipson, 1985:10). Participation in the international systemic logic not only provides a means by which states define their autonomy, but also creates a series of expectations about the international system making long term exchange relationships between actors in that system, and thus knowledge about it, possible. It stands to reason, however, that in periods of economic change, previously defined expectations about the international system are likely to seem suspect, and the knowledge gained from those expectations may well be questioned. State managers are not managers of international firms. While state interests may at times coincide with the interests of particular domestic firms, state managers cannot always act in pursuit of the same goals as these domestic firms. The relationship between state managers and international firms, detailed in Chapter Two, is even less congruent -- and thus the state's knowledge about the international economy is often ambiguous, particularly in periods of international economic change.

This idea can be further elaborated by reference to Robert Cox's conception of the separation between economics and politics. He argues that, both theoretically and practically, politics has been "abstracted from the structures of power within which it

takes place" (1982:37). This removal of the political from the economic structures which define politics in the minds of state managers, reinforced by mainstream theoretical analysis, has specific practical implications. In effect, the dominance of economic hegemons (first Britain, then the United States) has been assisted because it appeared to take place "according to nonpolitical economic laws ... [although it] was made possible by the existence of a world economy which was in fact guaranteed by political and military power" (1982:38). For Cox, the economic structure and rules created by the hegemon become part of the "natural" order [8], an order which is not politically challenged although its benefits may not accrue evenly between systemic hegemons and non-hegemons.

Once the prevailing order begins to breakdown, however, the task facing state managers is overwhelming. The rules which had been assumed to be "natural" are found to be suspect, and the non-political patterns of the relationship between state managers and the international economic environment become contentious and subject to redefinition. Furthermore, certain types of states, most likely hegemons, may continue to find that the existing, but challenged, international order

continues to be of benefit to the interests of state managers and the social groups which they represent. State managers, therefore, may not only find themselves in a position where the "natural" international economic order governing particular transactions is suspect, but they are pressured by other state managers not to abandon it regardless of domestic social pressures to do so. The collapse of Bretton Woods, the oil crisis, the diffusion of manufacturing production to an increasing number of countries, the rise of multinational corporations -- all challenged the post war "rules" of economic exchange, and demanded adaptations by hegemons and non-hegemons alike. The notion of an eroding hegemonic world order thus has its own implications for the ability of state managers to gain knowledge about the international system, or in fact to trust their prior assumptions about that system.

STATE MANAGERS AND KNOWLEDGE

We can come one step closer to defining a model of how state managers come to understand their country's position within an international pattern of investment (how state managers gain or define knowledge which forms the basis of policy) by turning our attention to some of the theoretical limits to state action. How have the

constraints which we've identified been assumed to combine to limit the range of possible state action?

Peter Katzenstein's book, Small States in World Markets, assesses the industrial policy choices taken by small European states in response to the economic upheavals of the 1970s and early 1980s; a period of widely documented international economic change. His work seems at first glance to be an important theoretical contribution to the study of Canadian political economy, providing a comparative context within which we can understand the economic policy decisions of Canadian state managers. There are important differences between Canada and the small European countries which Katzenstein examines (Sweden, Norway, Denmark, the Netherlands, Belgium, Austria, and Switzerland), Canada's colonial past, for example, or Canada's geographical proximity to, and intensity of relationship with, the United States. The similarities, however, are also important; like these countries in post-war Europe, Canada is "close to the apex of the international pyramid of success" (Katzenstein, 1985:21). Like these European states, Canada has also achieved this degree of international economic "success" (defined in terms of relative standard of living) with a comparatively small, open economy, heavily dependent

upon international trade. Like these states, as well, Canada industrialized in the same broad historical period, confronting the global economy at the same time. [9] This is crucial for Katzenstein, for a similar period of industrialization has ensured that these countries "have related to the international economy in a distinctive manner" (1985:21); at least distinctive from the later industrializers of the European periphery. While comparisons are at best imperfect, Katzenstein's analysis can provide us with clues as to the manner in which small states, including Canada, have interpreted the constraints under which they operate in the formulation of policy.

The key to Katzenstein's analysis is his insistence that small states do not have the same latitude for action as larger ones when confronted by the instabilities of the international economy. He argues that small European states have tended to respond to international economic change through policies emphasizing domestic compensation rather than attempting to confront or resist the changes in the international system. Wage and price controls, generous public spending on social welfare programs, and an increase in the size of the public sector have characterized the measures taken by many of these small states in order to

gain control of the national economy, measures also undertaken by the Canadian state over the past two decades. For example, public expenditure in Canada as a percentage of gross national expenditure increased dramatically from barely over 12 percent in the mid-1960s to between 18 and 20 percent throughout the 1970s and early 1980s; an increase of over 50 percent in only a few years. Katzenstein presents this increase in the public sector economy as the primary mechanism by which small open states have engaged in domestic compensation of the effects of external economic dependence (Katzenstein, 1985:54).

In essence, therefore, Katzenstein's position is simple:

For the small European states, economic change is a fact of life. They have not chosen it; it is thrust upon them [e]llites in the small European states, while letting international markets force economic adjustments, choose a variety of economic and social policies that prevent the costs of change from causing political eruptions. They live with change by compensating for it (Katzenstein, 1985:24).

The logic of Katzenstein's argument is founded on his assumption that small open European states must choose strategies of domestic compensation because their size and openness does not permit them to do otherwise.

Implicitly at least, Robert Cox's depiction of a hegemonic international capitalist order holds sway here, effectively constraining state managers of small international economies in the range of options perceived to be open to them. The flows of an international economy which has been depoliticized, and its consequences, bring small states to adjustments rather than confrontation. The United States or Japan, on the other hand, "states whose power is sufficient to exercise effective control ... over parts of their international environment or over parts of their own societies" (that is, states displaying hegemonic qualities), can choose economic strategies based on "exporting or preempting the costs of economic change in times of adversity" through the adoption of ad hoc or systematic protectionist policies (Katzenstein, 1985:23). Here again we see reflections of earlier analysis; ascendant or hegemonic states may choose to emphasize an international order which continues to be of benefit to them, or can move to create a new "natural" order. For Katzenstein, small states are too dependent upon the world market to consider protectionist solutions (Katzenstein, 1985:23-4), nor do they have the "breathing room" to target structural sectoral transformations within their own economies

[10]. He contends that such policies require a great deal of state "control" over the various groups making up the domestic economy, and that control is not easily achieved in a national economy highly dependent upon, and integrated with, the international economy.

Where does this lead us? The argument is straightforward. Small states have adopted reactive, flexible and incremental policies, in part because they do not have the capacity of larger states to effect change in the international environment. Cox would argue that the road is more difficult for small states in periods of economic change (lower down in the hierarchy of power) because the separation of politics and economics increasingly seems, to these state managers, to be unreal. These states adjust to an uneven distribution of benefits by playing a more interventionist role in their economies than do larger states (Cox, 1982:38). The United States, on the other hand, governed by an ethos of the liberal market economy, has generally relied upon macroeconomic policies and market solutions in order to deal with the challenge of the economic upheavals of the recent decades. Where these solutions do not produce adaptation of the domestic economy to the international economic changes within a range of bearable costs, the

United States has tended to "export the costs of change to other countries through the adoption of a variety of limited, ad hoc protectionist policies" (Katzenstein, 1985:23). We have thus witnessed the growth of the American "negotiated" imposition of voluntary export restraints (VERs); and the unilateral imposition of restrictions against trading partners, such as the tariff and quota levels determined under U.S. escape clause actions.

Katzenstein argues that Japan, from another perspective, has been able to adopt statist solutions to the problems of economic change. He points to the historical role of the state in Japan and to the evolution of Japanese institutions as factors which allow the state to preempt "the costs of change through policies that pursue the structural transformation of their economies" (1985:23). This strategy of seeking, and in fact pursuing, structural changes in the domestic economy often implies the adoption of protectionist policies, at least in the short term.

For Katzenstein, therefore, a small open economy such as Canada's does not have the luxury of seeking such solutions -- offensive state strategies in Ikenberry's terminology (1986). The international system and the balance of societal forces are more of a

constraint for certain classes of states -- small, open economies -- than for others. While we may be willing to concede that larger states can play a different role in shaping the international economy by virtue of their size, Katzenstein's presumption goes one step further. Small states "know" their place in the international system; they "know" which challenges they can confront, and which challenges must simply be accommodated.

The "bottom line" protectionist solutions of the United States, for example, are not viable options for these countries, and small states "know" them not to be. "The openness of their economies has resulted in a fully developed awareness of the inescapability of economic change" (Katzenstein, 1985:27). Small countries may seek to forestall change, but they do not expect to be able to escape it. Equally, the Japanese strategy of seeking to preempt adverse economic change cannot be adopted by small open economies, which "apparently lack the political capacity to employ the full range of policy instruments in a far-reaching policy of structural transformation" (1985:27). The implications of this state knowledge are certainly far-reaching; Katzenstein claims, for example, that small European states have known to "consistently welcome ... the flow of foreign capital, which they see as an ingredient

essential rather than detrimental to their economic and political aspirations" (1985:57) [11]. Canada may not have the latitude of action shared by larger countries such as the United States and Japan, but from the later 1960s its state managers clearly did not have the small European state's knowledge that international economic liberalization is a necessary given, only to be balanced by some measure of domestic compensation. In other words, while the pattern of international economic exchange may constitute a "given", it is not necessarily interpreted by state managers in a similar way. The process of learning, or constructing the "givens" of an international reality, are quite simply different in different social formations.

However important the processes of change underway in the international system, and however significant the positions adopted by particular groups or classes within domestic society, these do not in themselves define state policy. These lessons force us to question Katzenstein's conclusions, for these too easily lead us to assume that constraints are defined by all states in the same, or very nearly similar, way. We must conceive of the state as an actor operating within the context of constraints, but not necessarily defined by them. In order to explain policy choices, such as FIRA, which

straddle the international and domestic environment, we must develop a more formalized conception of how state managers perceive the international economic environment, and thus how they act on the basis of these perceived constraints. Without such an understanding, we are limited to making blanket statements along the lines of Katzenstein's contention that small, open states do not attempt to regulate direct foreign investment because they know not to do so -- responding in fact as systems-level analysts, attributing the actions of state managers to a pervasive international system.

As we have argued, knowledge about the international system is not, and effectively cannot, be as well defined and articulated as is knowledge about domestic structures. The pattern of state-society interactions which provides state managers with information about the changes in domestic society is not mirrored for the state by a similarly routinized pattern of interactions at the level of the international system. This is particularly the case during periods of economic change, when a hegemonic pattern of international exchange appears to be breaking down. [12] This is a crucial observation; for while the state operates in both domestic and international

environments, its links to the latter are not as formalized, and thus the knowledge of state managers about the constraints posed by the latter is not as clearly defined, and may lag considerably behind as a result.

Moreover, different social groups, many with independent links to the international economic environment, present different interpretations of the changing pattern of international investment, and that these differing interpretations influence policy. Foreign investment policy becomes the outcome of a struggle within the state, a struggle between groups each having its own interpretation of a country's position within the international investment environment, and of state managers' own prior assumptions about the "rules" of the international economy. The role of domestic classes is crucial. International events may lead to a convergence of small state perspectives and expectations of the international system along the lines of Katzenstein's argument, but they do so through the filter of domestic events, buoyed by an oftentimes sporadic state interaction with other state actors in the international system. This domestic filter, the collective of interpretations and assumptions held by different classes and class

fractions about their country's place in the pattern of international investment, may limit the capacity of state managers to formulate particular policies ensuring a country's competitiveness in the international economy. Further, during periods of change in which existing bureaucratic policy recommendations no longer appear to respond to growing social concerns, the state seeks to reinterpret its knowledge. State managers do so because their continued position within the state structure is dependent upon their ability to maintain some semblance of a consensus -- at least in the short (electoral) term.

States as institutions have a history and an orientation towards the range of "possible" action in any given policy area. Bureaucratic state managers, through a representational state structure, promote their own interests as well as the interests of classes or class fractions with which they have historically become associated. Domestic and international environments set limits and opportunities upon the range of politically and economically viable policy options, limits and opportunities which are not always understood or respected. Interpretations of the international environment are filtered through domestic structures, particularly so because states have only sporadic direct

contact with the international economy as a result of the historically "non-political" definition of the international economy. State managers make policy decisions within these contextual "layers", contextual layers which are themselves changing, so that state managers may act on the basis of perceptions which are no longer reflective of the context in which they operate.

In sum, bureaucratic and political state managers (our key policy makers) are influenced within the state structure by bureaucracies, which represent the interests of defined classes and class fractions. State managers also solicit information from outside formal state structures, and this, we argue, is more likely during periods of international economic change, and thus of uncertainty about the nature of the international system. The underpinnings of both state and non-state information about the international economic environment are found in the interests and perceptions of different social classes and class fractions. It is through the filter of these class interests that most information to state managers is presented.

Social classes or groups, for their part, do not only interact in an international environment as a

consequence of state action. Social classes, to a greater or lesser degree, have their own ties to the international environment through their participation in an international class structure. These ties to the international environment condition the development of domestic class interests about international circumstances. State managers do not only understand the international environment through the filter of social classes, however. They also participate, with other states, in the creation of international rules systems governing international economic exchange, and creating a pattern of expectations about those exchanges. For non-hegemonic states, such as the Canadian state, the rules system passes into the realm of the non-political, in effect becoming a "natural order", until challenges to the system appear to erode it. These rule systems can be formalized, such as the GATT, or can be based upon informal patterns of expectations, such as the national treatment provisions implicitly governing foreign direct investment. In either case, these form the basis of the prior expectations of state managers. Other states have interests bound in the rule systems as well, and may interact to support or challenge these systems.

We have argued that state managers may base their

policy decisions upon assumptions or interpretations which are no longer appropriate to a changing international economic environment. While state managers understand the international economic environment in part as a consequence of a pattern of expectations and routines created by states, class agents understand that environment as a result of their direct participation within it. Those understandings do not necessarily coincide, nor, in periods of international economic change, are they necessarily reflective of the international economy itself. Furthermore, these different perspectives are not translated directly to state managers. All class agents do not have equal access to the state, so that all perspectives of and interests in the international economic environment are not on an equal footing. The international economic "regime", for its part, is not on the political agenda until it is challenged by international -- primarily state -- actors. When challenges to the established economic order do arise, they re-politicize the international economy, and, in the short term, confusion around the re-definition of policy options is almost necessarily a result.

This dissertation, in seeking to answer the question of how states learn, looks to contribute to the

field of international relations and to solving its unanswered query. It does not, however, seek to deny the importance of the international system. In fact, it argues that an examination of the international system and the definition of international structures is a critical step in understanding the nature of state choices and the success of state policies. We cannot pretend to understand the Canadian experience with the Foreign Investment Review Agency without understanding first the changing patterns of foreign direct investment and Canada's place within these. We cannot assume, however, that Canadian state managers -- the actual policy makers -- have knowledge of changing international investment patterns to such an extent that they are uniformly capable of making rational, self-interested, value-maximizing decisions based on that understanding of the international system. Neither, however, can we assume that Canadian state managers are incapable of interpreting, or even of ignoring, the international environment when policy decisions are taken. We cannot conclude that particular patterns of foreign investment cause state behaviour, or limit it to such an extent that other choices are not possible. No matter how constrained, state managers do have choices, and state policies are at least in part

reflective of those choices. It is possible to identify international structures and yet still accept that actors have choices. A structure, after all, does not "regulate behavior so much as create the possibility of particular forms of behavior" (Ashley, 1984:235; emphasis added).

In the case of FIRA, the Canadian state created an Agency embodying a view of Canada's international position which, in terms of the economic reality, was quickly becoming questionable. In defining state knowledge about the benefits of foreign investment, state managers responded to the interpretations of particular social classes which defined Canada as the recipient of largely branch plant and resource investment, despite the fact that investment patterns were in fact changing. Comprehensive regulation of foreign investment came into play in Canada when two assumptions were prevalent. First, the belief that Canada "had enough investment" was widely accepted. At the same time, many believed that investment flows would continue in any case, because Canada was an investment location attractive enough to stand up to any international competition.

The difficulty in creating an agency based around these beliefs, which originated both from class-based

perspectives and from an assessment of the traditional pattern of international investment as it had affected Canada, was that the international economic environment was itself changing. "Having enough foreign investment", as we shall see in Chapter Two, no longer captured the essence of the foreign investment question. Conceptions of investment built up only around capital and production ignored the new reality of the importance of technology to investment, where notions of "enough capital" do not apply. As well, the second belief was undermined by the fact that it was patently no longer the case; advanced industrial economies began competing among themselves as well as with newly industrializing and less developed countries for new investment, and Canada did not stand up well as a most-favoured investment location.

Just as policy initiatives do not spring up in a vacuum, policy outcomes do not operate in a vacuum. The state is neither a monolith, nor a permanent crystallization of social forces. The relationship between state managers, and the domestic and international environments in which they find themselves, is not carved in stone. The balance of class forces, both within the state and domestic society, the state's policy experience with an issue

such as direct foreign investment, the economic and social conditions, both domestic and international; all are subject to change (see Mytelka, 1986:147). The capacity of a state to act must be judged in light of that changing environment, and the evaluation of the success or failure of a state's strategy must be understood within this dynamic context.

ENDNOTES

- [1] See, for example, Charles Kindleberger (1973); Robert Keohane (1980); or Stephen Krasner (1976). On world-systems theory, see I. Wallerstein (1974); or Christopher Chase-Dunn & R. Robinson (1977).
- [2] Neither the United States (as the system hegemon) nor the Third World (through the United Nations code of conduct for MNCs) has been able to establish a formal international investment regime. As Lipson argues, however, the elements for such a regime did exist from the mid-nineteenth century, as the development of international property rules were "hardened into general principles of international law" (1985:8). These rules include the application of national treatment principles to foreign owners (particularly evident in the Paris codification conference of 1929) except in extraordinary circumstances. In such circumstances, independent judicial review and full compensation had to be provided for interference with foreign property.
- In 1962, through the Hickenlooper Amendment, the United States Congress attempted to influence aid dependent states to respect the terms of international property rules. The Hickenlooper Amendment created a statutory link between the disbursement of aid and repayment for expropriations, such that unless a foreign government undertook immediate steps to compensate an expropriated U.S. company, bilateral aid was to be automatically suspended (Lipson, 1985:202). By 1973, however, the Amendment had been effectively deleted with the addition of a provision allowing presidential discretion in the waiver of sanctions against expropriating states. The addition of this right to waiver only put into law the presidential nonapplication which had been in effect during the ten years of the Amendment. The Amendment was only formally used once, in Ceylon in 1963, although the threat of its use did become an important issue in several other expropriation cases (Lipson, 1985:202-03).
- [3] See, for example, Peter Gourevitch (1986); or Timothy McKeown (1984).
- [4] The observation that there exist international economic insecurities which might impinge on

domestic policy making, thus challenging the capacity of the United States to manage the international environment, first appeared in post-war mainstream academic thought under the rubric of the concept of interdependence. Keohane and Nye's seminal 1977 work, Power and Interdependence, reflected the seemingly fundamental shifts in the world political economy marked by oil crises and the collapse of the Bretton Woods system of pegged exchange rates. New transnational actors were seen to be increasing in importance as economic production became more diffuse, and the consequences of change in international finance and trade were felt by a broader range of national actors, including the United States.

These systemic changes have raised questions about the relative decline of U.S. hegemony; questions which have been with us in the study of international relations for over fifteen years. Susan Strange offers that the notion of lost or declining hegemony has raised one main politically important proposition; for the perception of U.S. loss of hegemonic authority over the international economic system has been seen to lead, as its most significant consequence, to "the instability and aimlessness of the international political economy" (1987:553). Hegemonic stability theory contends, in fact, that there is a relationship between the presence of a systemic hegemon and stability in the international system, and that this stability has been threatened by changes in the international economic system.

- [5] It is important to stress that Block does not argue that alternative policies (those at odds with strengthening the capitalist accumulation process such as the challenge to private property rights through nationalisation) are necessarily precluded. He stresses that all limits placed upon state managers are "contingent and not absolute" (Block, 1980:230). Because these limits are not absolute, expropriation or the placing of severe restrictions on the property of dominant classes can conceivably occur. He argues, however, that because propertied classes cannot survive without the state, "those classes have little choice but to seek a modus vivendi with the state managers" (1980:230). The dominant historical accommodation has been highly favourable to the owners of capital (thus, the

Marxist formulations of the state as an executive committee of the bourgeoisie), but the modus vivendi can break down or be strained (Block, 1930:241fn10).

- [6] Block's emphasis on the collective goal of state managers to maximize their gains within particular political "rules of the game" does not preclude the choice of any individual manager to pursue self-aggrandizement at the expense of broader goals. Political norms and class relations will limit the inclination of the collective to pursue their narrow interests beyond the boundaries of the rules of the game. Block contends, for example, that analysis of the politics of parliamentary victory, reveals that "it is generally foolish for a particular group of state managers to take excessive actions to preserve their power in the short term if these actions might jeopardise their party's future chances for electoral victory" (1980:229). Presumably, those taking excessive actions also risk censure from colleagues more interested in their long-term position.
- [7] Ashley's international norms, developed through long-term historical processes, provide a conceptual range of action which states perpetuate. While he acknowledges that there exists a prior relationship between state and society (the state only participates in the international balance of power logic once it has secured a monopoly over the legitimate use of force superimposing the state upon society), he does not define state participation in the international system in terms of society. The interstate system exists as one largely divorced from the politics of domestic society, which allows Ashley to assume that society can "act as a singular unit in a 'state of nature'" (Ashley, 1980:38).
- [8] This represents in fact Cox's notion of hegemony: "the temporary universalization in thought of a particular power structure, conceived not as domination but as the necessary order of nature" (Cox, 1982:38).
- [9] Alexander Gerschenkron (1966), Economic Backwardness in Historical Perspective, has made this argument with respect to the "late industrializers", those countries cited by

Katzenstein, and equally applicable to Canada. For Gerschenkron, three significant factors stand out as similar for countries which industrialized in the period after the industrial "leaders" -- roughly 1840-1890; the historically specific nature of technology and its role as catalyst for industrialization, the problems posed by a scarce industrial labour force, and the overwhelming scarcity of capital (1966:8-15).

- [10] Katzenstein's argument on this point does not hold for a small, open economy such as Canada's, given the protectionist Canadian stances toward such goods as textiles, clothing, and automobiles.
- [11] Katzenstein's argument does not even hold through for all the countries he investigates; Sweden is certainly an historical exception to his rule.
- [12] Katzenstein indirectly acknowledges the asymmetrical nature of the state's "ability to learn" when he observes that "international factors affect political strategies and outcomes only indirectly; they are funneled through domestic structures that are shaped by different histories and embody different political possibilities" (1985:37).

CHAPTER TWO

MULTINATIONAL CORPORATIONS AND THE STATE

Chapter Two presents an overview of theoretical perspectives on the post-war evolution of the international investment strategies of multinational corporations. Central to our argument is the fact that the pattern of direct foreign investment was changing during the period of the Canadian debates over the utility of creating the Foreign Investment Review Agency. Mapping the the underlying strategies responsible for these changes will assist us in interpreting the extent to which Canadian debates captured the reality of international investment flows. This chapter goes beyond the early 1970s, however, and continues to map changing strategies into the 1980s, changes which had consequences for the effective operation of the Foreign Investment Review Agency. The task of Chapter Two, therefore, is to provide a review of the underlying motivations for firm movement abroad, which in turn will assist us in interpreting the historical evolution of foreign investment patterns detailed in Chapter Three -- the patterns which state managers are trying to understand in order to formulate policy directed toward the international economic environment. We are here beginning to define changes in

the international economy, processes which may not be captured in the state manager's expectations about the international environment, or in the interpretation of that environment through class struggle.

In this chapter, we will begin by examining the reasons which have been offered for firm movement abroad, essentially offering different answers to the question of why firms become multinational. This discussion will provide us with two insights: first, how the process of international investment (and thus that part of the international economic environment of concern to the Canadian state in the creation of FIRA) has been changing. From this discussion of theoretical perspectives on the process of foreign investment, it will become evident that multinationals have moved from conceiving of foreign investment as a process by which markets can be penetrated or defended to a process through which firm competitiveness may be assured, although it remains possible to achieve competitiveness through the penetration and defence of markets. This progression of MNCs from suppliers of regional markets to truly global enterprises has important implications for our comparison of actual processes of foreign investment and Canadian state managers' understanding of them. The discussion provides us with a basis against

which to assess where Canada might be located in this global pattern of investment.

The chapter will then turn its attention to an evaluation of the relationship between state actors and multinational corporations. What range of action have states taken in response to the costs and benefits believed to be generated by foreign investment? What kinds of relationships do state actors and multinational corporations (MNCs) have? These are not the same question, for while patterns of foreign investment are economic phenomena, MNCs are actors, whose class interests find representation in the struggles taking place within the state. While MNCs and state actors are not the same, state managers are limited in their capacity to act wholly autonomously from the interests of multinational capital. This discussion of the state-MNC relationship will help us to locate the creation of FIRA in a broader comparative context, again underlining the assumptions of Canadian state managers embodied in the Agency.

Finally, the discussion of this chapter is crucial to our theoretical understanding for it highlights the extent to which the implicit norms of national treatment for foreign investment began to be challenged in the 1960s. Pointing to the breakdown of implicit

private international capital movements, customarily distinguished as a choice between direct investment and portfolio investment. As Stephen Hymer has told us, while these categories have been defined in different ways, "basically it is a question of who controls the enterprise in which investment is made. If the investor directly controls the foreign enterprise, his investment is called a direct investment. If he does not control it, his investment is a portfolio investment" (1976:1).

[1] Hymer's attribution of control as the central point of differentiation between portfolio and direct foreign investment has important theoretical implications, for the same factors cannot be said to underlie the reasons for undertaking both forms of investment. Portfolio investment is most simply understood as investment motivated by differentials in interest rates, so that "[e]ach investor maximizes his profits by investing where returns are the highest" (Hymer, 1976:6). Risk, uncertainty, and barriers to capital movement will of course affect the simplicity of this equation. Importantly, though, interest rates, even lent complexity by the vaguaries of the international economic system, do not explain the key economic factor of control.

Hymer begins his explanation of control by

dichotomizing notions of direct foreign investment. The foreign investor may, in the first instance, seek control over a foreign enterprise in order to ensure the safety of his investment. Interest rates still play a factor in this investment decision, but direct investment will be undertaken in preference to portfolio when "the distrust of foreigners is high or when fear of expropriation and risks of exchange-rate changes are high" (Hymer, 1976:24). In the second case, however, a firm may chose to embark upon direct investment because it seeks to "remove competition between [itself] ... and enterprises in other countries" (Hymer, 1976:25), or to exploit advantages peculiar to itself, so that the motivation for the investment is not a higher interest rate abroad, "but the profits that are derived from controlling the foreign enterprise" (1976:26).

Hymer's argument, that foreign direct investment is not analogous to portfolio investment, led him to ask particular questions about the nature of the international firm. He postulated that firms likely to engage in multinational activities possess a combination of intangible assets, such as patented technology, a differentiated product, and marketing experience. These intangible assets provide the firms with a source of monopolistic advantage at home and abroad, such that

"[t]he way to maximize the profit from this package of assets is to exercise direct management control over [its] ... foreign assets" (Newfarmer, 1985:19). Hymer traces the metamorphosis of the tightly controlled, single family-owned U.S. firm through the rapid growth of the American economy and resulting firm mergers into large corporations with control vested in centralized administrative hierarchies. The emergence of a division of labour between head office and the firm's individual departments is seen as the result of the growing need for increased knowledge inputs (in the form of centralized planning and decision-making) in order to respond to production increasingly integrated on a national, and continental, basis. This centralized structure arises, therefore, in order to handle the demands of continent wide, vertically integrated production and marketing. The new firms, complete with centralized administrative structures, tremendous financial resources, and secured oligopolistic market position at home, begin to extend their advantages in the home market to foreign investment in markets abroad (Hymer, 1976:392).

Hymer points out that firms participating in foreign direct investment do so in the expectation that their particular assets will lead them to achieve higher

profits abroad than they would have at home -- the higher returns necessary to compensate for the greater costs and risks involved in investment abroad.

Additionally, because firms indigenous to a particular country have specific advantages not shared by foreign firms (such as better information about that country), foreign investors must expect that their advantages will confer upon them returns greater than those expected by domestic firms investing in the same activities (Hymer, 1976:32-64).

Charles Kindleberger provides more explicit reasons for the multinationalization of firms in his monopolistic theory of direct foreign investment. Like Hymer, Kindleberger criticizes the theory of international capital movements from the premise that if the expectation of a maximized rate of return were the only criteria for international investment, investors would simply move their capital through organized capital markets rather than through firms engaging in the production and distribution of goods. Kindleberger equally supports Hymer's assertion that it is the unequal distribution of advantages between firms which conditions multinational investment. He specifies that: "[f]or a firm to undertake direct investment in a foreign country it must have an advantage over existing

efficient manner in situations where a regular market fails to operate (Dunning, 1981). This is particularly true for the products of technology, given that each piece of technology is unique and that there exists, as a consequence, no organized market for the product. What are the implications of this? Internalization theory argues that in order for a firm to reap the full reward on its expenditures on research and development (which are ever increasing in an era of knowledge-intensive production), it must be able to keep its technology a secret. Transferring or leasing technology to another firm in a foreign location can create serious problems. As Peter Gray argues, the high costs involved in negotiating a technology transfer agreement, not only in terms of legal and material expenses, but also in view of the uncertain price of technology and the risk of leakage to competitors, creates an "incentive ... to internalize the technology transfer by establishing a foreign subsidiary" (Gray, 1987:433).

The internal market of the MNC permits the firm to assign property rights to knowledge itself, and leads the MNC to attempt to create a monopolistic market where its knowledge advantage can be developed and explored in an optimal manner on a worldwide basis. The firm in

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or potentially competitive firms in that country. If not, these firms, operating more cheaply in other respects because nearer the locus of decision-making and without the filter of long lines to distort communication, would put the intruder out of business." (Kindelberger: 1979:95).

Kindleberger adds specification to Hymer's model by explicitly identifying the market imperfections which can confer monopolistic advantages on the multinational firms. He cites departures from perfect competition in goods markets, including such aspects as product differentiation, or special marketing skills, which favour multinationals. Departures from perfect competition in factor markets -- such as the existence of patented or unavailable technology or discrimination in access to capital -- also tend to favour multinational corporations. Economies of scale also favour the multinational firm in Kindleberger's analysis; horizontal integration of production can extend to the point where one firm has some control over the price of a good (i.e. monopolistic, or some oligopolistic, situations), while vertical integration permits a firm to coordinate production over several stages of a productive process, often more effectively than a competitive market. Finally, governmental action

-- to limit trade through the imposition of tariffs, for example -- can set the conditions for multinational investment (Kindleberger, 1979:96-102). The 1879 National Policy tariffs in Canada, for example, have been cited as responsible for the extent of early United States investment in Canadian industry (see Innis, 1956, for example). Kindleberger clearly points out that market imperfections, which may be key in defining the unequal advantages of firms, are also important in providing sufficient reason for direct foreign investment.

Hymer and Kindleberger have defined one particular multinational strategy for us; it is one by which multinationalization occurs in order to penetrate foreign markets. Firms engage in this form of investment by virtue of oligopolistic advantages, unevenness across national markets (in terms of consumption patterns, relative factor costs, transportation and communication costs, and barriers to export), and the desire to maintain technological advantage. As Charles-Albert Michalet reminds us, though:

[c]e qui est important à souligner, c'est le fait que ... la multinationalisation se présente simplement comme la procédure appropriée pour suivre le même objectif: la pénétration des

marches étrangers. Les exportateurs deviennent multinationaux sans modifier fondamentalement leurs conceptions (1976:150).

Subsidiaries born of this type of strategy are characteristically thought of as "branch plants", firms whose major purpose is to supply the local, or perhaps regional, market. While we conceive of firms following this strategy as multinational, they are not truly global; the firm sees production through a series of national or regional lenses rather than in world wide terms. Michalet identifies subsidiaries of this strategy as "filiales-relais", arguing that they are in some measure mirrors of their parent firm (or of the larger group made up of parent and subsidiaries), and that they find themselves half-way between export strategies and those which envisage the true internationalization of the production process (1976:152). This description of multinational activity is an apt characterization of the Canadian experience with U.S. foreign investment through the 1960s, and it is as such reflected in the Gray Report (1972).

More recently, and yet still building upon Hymer and Kindleberger's focus on the unequal attributes of firms, internalization theory has argued that the firm is itself capable of organizing an alternative to the market in order to produce and distribute products in an

efficient manner in situations where a regular market fails to operate (Dunning, 1981). This is particularly true for the products of technology, given that each piece of technology is unique and that there exists, as a consequence, no organized market for the product. What are the implications of this? Internalization theory argues that in order for a firm to reap the full reward on its expenditures on research and development (which are ever increasing in an era of knowledge-intensive production), it must be able to keep its technology a secret. Transferring or leasing technology to another firm in a foreign location can create serious problems. As Peter Gray argues, the high costs involved in negotiating a technology transfer agreement, not only in terms of legal and material expenses, but also in view of the uncertain price of technology and the risk of leakage to competitors, creates an "incentive ... to internalize the technology transfer by establishing a foreign subsidiary" (Gray, 1987:433).

The internal market of the MNC permits the firm to assign property rights to knowledge itself, and leads the MNC to attempt to create a monopolistic market where its knowledge advantage can be developed and explored in an optimal manner on a worldwide basis. The firm in

fact becomes an alternative to the market, and is thus able to develop its firm-specific intangible advantages (found in such areas as technology, managerial skills, or corporate organizational structures). The internalization thesis differs from Hymer's argument because the firm organizes an internal market, in the case of knowledge, as a substitute for a missing regular external market. For Hymer, the firm's ability to organize a market stems from the imperfections of the existing market arrangements (Dunning and Rugman, 1985:229). Within the arguments of internalization theory, foreign direct investment and the establishment of foreign branch plants become vehicles through which the MNC integrates foreign markets into its worldwide internal market, thus avoiding any dissipation of firm-specific knowledge.

Discussion of the oligopolistic advantages specific to multinational firms, of course, does not paint more than a general picture as to the motivations for specific investments. Raymond Vernon's Sovereignty at Bay (1971) provides an early statement of sectoral distinctions, while remaining supportive of Hymer's qualification of oligopolistic advantage. Vernon reminds us that direct foreign investment is a blanket term covering many forms of economic activity -- ranging

from the establishment of wholly owned and controlled foreign branch plant operations, through to the establishment of minority ownership joint ventures with national firms or host country state actors. Whatever the form of the investment, Vernon re-emphasizes that success in a firm's overseas expansion is dependent, as a necessary condition, upon some kind of oligopolistic advantage.

The successful overseas expansion of such companies as Corn Products, General Foods, and Coca-Cola during the 1920s and 1930s drives home the point that this kind of success depended on the development of some oligopolistic advantage, whatever the nature of that advantage might be. These industries, like those associated with industrial innovations, were dominated by large firms and were highly concentrated in structure (Vernon, 1971:85).

Oligopolistic advantage may be necessary, but for all these theorists, it is not a sufficient condition for engaging in direct foreign investment. Raw materials extraction, for example, has attracted foreign investors wishing to secure sourcing of a particular primary resource. Often, a firm wishes to develop its own backward linkages, developing the primary resource necessary to supply its own manufacturing endeavour. Such firms must be capable of providing the resources to meet the scale of the operation, the technology to

conduct the extractive activity, and, most significantly, the market -- not necessarily as inputs to the firm's own production process -- to support the raw materials extraction. Vernon acknowledges, however, that the gains from multinational investment in raw materials production are not necessarily permanent; the obsolescing bargain implies that "foreign investors must resign themselves to the fact that national goals and preferences to which they were responsive at the time they entered any country are likely to undergo periodic metamorphoses" (Vernon, 1971:53).

These metamorphoses have been understood as a change in the bargain first struck between the multinational investor and the host country; once the multinational's investment is proven sound, the state no longer perceives the high levels of return to the company originally negotiated to be appropriate. The bargain struck between the MNC and the host state is seen to obsolesce. The important point here is that the relationship between the MNC and the state is not defined in a static environment. As we shall see later, Canadian state managers accepted the implications of this obsolescing bargain model in their perception of Canada's attractiveness as a location for investment. Barbara Jenkins (1986) has argued, for example, that

this perception carried on as far as the creation of the National Energy Program in 1980, where the Canadian state sought to increase tax revenues from the lucrative, and largely foreign owned, oil industry.

Manufacturing investment is controlled by somewhat different motivations and processes. Vernon argues that those U.S.-controlled enterprises which "multinationalized" began by generating new products in response to the high per capita income and the relative availability of productive factors in the United States, products based on knowledge-intensive inputs. Having developed new products or productive processes, they introduced these abroad through exports. When their export position became threatened, usually coincident with the diminished importance of specialized inputs from the U.S. (so that the more conventional costs of labour and capital come to dominate the profit calculation), they established overseas subsidiaries in order to retain what was left to them of their (oligopolistic) market advantage. This advantage however, is a temporary one, eventually eroded as the technological skills leading to product innovation become widespread (Vernon, 1971:66-74). For Vernon, a partial solution to both the obsolescing bargain and the product cycle of manufactured goods is the capacity of

the firm for technological adaptation or product -- and production -- diversification (1971:27).

It cannot be overstated that Vernon's product cycle model is most applicable to U.S. firms during a specific historical time period. Japanese foreign investment, for example, cannot be explained by simple reference to a product cycle model. Rather, as Ozawa argues, the Japanese state directed its national firms to locate abroad through the adoption of a policy to require the restructuring of industry. The policy emphasized "a shift from "pollution-prone" and "resource-consuming" heavy and chemical industries toward "clean" and "knowledge-intensive" industries; it assigned a new role to overseas investment -- as a catalyst to houseclean the economy" (1978:523).

However, elements of Vernon's theorization can be found in Canada's early experience with U.S. MNCs. As a source of raw materials, Canada afforded the advantages of proximity to U.S. firms with the technological capacity and the market needs for natural resources. As a market, Canada was not only attractive as a high-wage area, but -- as discussed above, and as Vernon re-emphasizes -- the threat to U.S. exports to Canada "was heightened by tariff increases ... and by the extension of the Imperial Preference System" (1971:83),

encouraging the expansion of U.S. MNC activity in Canada.

Just as the obsolescing bargain can change the logic of multinational investment in raw material extraction, so to is the product cycle model subject to pressures. As Vernon himself acknowledged, by the early 1970s, "the product cycle model was beginning in some respects to be inadequate as a way of looking at the U.S.-controlled multinational enterprise" (1971:108). The central assumption of the product cycle-model, that innovations are developed in the United States, then marketed abroad, seemed increasingly to come under challenge by firms "that have long since acquired a global scanning capacity and a global habit of mind" (Vernon, 1971:107). The growth of the global, rather than national, firm, implied that "stimulations to the system could come from the exposure of any element in the system to its local environment, and response could come from any part of the system that was appropriate for the purpose" (1971:108). What is crucial here is the fact that the product cycle model was particularly applicable to the behaviour of U.S. multinationals in the period from 1900 to roughly the late 1960s. [2] The behaviour of U.S. firms in this period, as will become clear in Chapters Three and Four, helped to define the

Canadian state's understanding of the pattern of international investment; firms locating abroad to secure their export position and to serve local markets more advantageously. This formed part of the pattern of expectations held by Canadian state managers about the international economic environment.

The Internationalization of Multinational Investment

Vernon's acknowledgement of the diminishing relevance of the product cycle model in the face of newly internationalized production was being discussed by other theorists as well. During the late 1960s and early 1970s, the calculation of firm strategies began to change in the face of an accelerated rate of technological innovation and diffusion which spawned growing numbers of new competitors (from Japan, Europe, and the NICs in particular), and a decline in the rate of productivity increase "making it more costly for governments to maintain high levels of mass consumption through Keynesian demand management techniques" (Mytelka 1987:48). In addition, the growing wage differential between the advanced industrial economies and the developing countries encouraged firms to seek solutions to their impending profitability squeeze through movement abroad. Henry Ergas has also listed factors

which have contributed to the challenges faced by firms, including the approaching saturation in a number of previously rapidly-growing product markets, and the continued pressure on prices and profit margins as a result of adverse distribution shifts and or movements in raw materials prices (1984:327). Once again, we are reminded that the environment in which multinationals operate is not static.

This new literature focussed on the growing phenomenon of worldwide sourcing, leading to a new international division of labour. Authors such as Gyorgy Adam (1975) advanced the concept of globalism, the process whereby firms look upon the entire world as their market. Adam argued that global firms engage in production, distribution and selling activities with as little regard to national political boundaries as the realities of time and space permit. Worldwide sourcing resulted when firms began to see formerly national lines of production in international terms, and responded to such a vision through mechanisms such as international subcontracting in order to reap the benefits, for example, of lower labour costs in those phases of a production process which are labour-intensive.

Folker Frobels, Jurgen Heinrichs and Otto Kreye further developed the notion of a new international

division of labour stemming from a turn to world-wide sourcing. They argued that the tendency of capital to establish parts of one production process in various locations around the globe was a function of the world wide industrial reserve army of labour (characterized, as compared to much of the industrial world, by lower wages, longer working hours, equivalent productivity, and no hiring/firing limitations), modern transportation and communication technology making international production less costly and more efficient, and the tendency to the fragmentation of production tasks. In particular, this fragmentation process allowed capital to secure monopoly over the knowledge needed to control each phase of the production process. For Frobel, Heinrichs and Kreye, the development of the new international division of labour is the result of institutional innovations on the part of capital (the outcome of individual decisions taken by MNCs), and not the result of altered country strategies or governmental policy decisions. This fact creates growing tensions between states and multinationals, and states themselves in fact fuel the tendency toward the NIDL. "The trend toward greater mobility and relocation is fueled by the competition among various parts of the world to offer the most favorable local conditions for the expansion of

capital. Capital relies on the state for its expansion, but not necessarily on any particular state."

(1978:857).

Adam, and Frobel, Heinrichs and Kreye point out that not all subsidiaries are simply branch plant representations of the parent firm in a local foreign market. The production process itself has become global in some industries, largely in order to take advantage of the savings possible from lower factor costs in different markets. Such a subsidiary is a "filiale-atelier" (Michalet, 1976:153), whose production takes place within an international network, and cannot operate in isolation of that network. The filiale atelier is not primarily, or even largely, concerned with serving the needs of a particular market; it is rather likely to export all of its production back to the parent firm (the export taking the form of an intra-firm transfer). The filiale-atelier is a fundamental part of the new international division of labour.

Adam, and Frobel, Heinrichs and Kreye point to factors external to the firm (relative labour costs, effective transportation and communication methods), as well as to fragmentation of the production process, as at least partial determinants of firm movement abroad.

The fragmentation of the production process accelerated the claims of the de-industrialization thesis, motivating studies such as Bluestone and Harrison's The Deindustrialization of America (1982) and underpinning the Waffle's concerns about Canada's economic future. Through it all, "access to cheap foreign labour used in producing commodities overseas" was seen as the important "motive for ... foreign investment" (Bluestone and Harrison, 1982:44) -- cheap labour which was not to be found in Canada.

It must be underscored, however, that analyses of world wide sourcing and the attendant symptom of deindustrialization are not always sensitive to the point implicit in Vernon's own assessment of the universal applicability of his product cycle model, the realities of changing time and space. The growth of protectionist action against imports -- particularly in the negotiation of ever more restrictive "gentlemen's trade agreements" or voluntary export restraints, and the increased imposition of ad hoc import relief provisions -- placed pressures upon a strategy based on the export of goods produced abroad back to the industrial home country.

It is important to consider that, in addition to protectionist pressures, developments in the

microelectronics industry have the potential to profoundly affect the globalisation strategies of MNCs. These developments offer a counter-trend to pressures for internationalisation, and remind us that we cannot take any pattern of MNC activity as set in stone. Kurt Hoffman's review of the garment industry's adaptation to microelectronic innovations brings to light a number of important considerations. Hoffman points out that the use of microelectronics-based innovations (MRIs) have integrated, rather than fragmented, discrete stages of the garment production process (design, grading, and market making activities) (1985:376). Kaplinsky refers to this integration of once discrete elements as an illustration of inter-sphere automation, the coordination between activities in different spheres of production, and sees this as a process mitigating against a new international division of labour based on complementary production between various affiliates in different countries and regions (1985:426,431). Hoffman points to the fact that the re-integration of production processes is likely to lead to changes in MNC investment strategies, commenting that his survey of international garment manufacturers brought him to the conclusion that "these factors would in the future lead them [MNCs] to consider favorably investment in automation as an

alternative to offshore production. The use of MRIs in the North is reducing production costs and, as this happens, the economic rationale for the current international division of labour is being undermined" (Hoffman, 1985:379,372). Thus we have trends toward globalisation and trends counter to this process, emphasizing the complexity of the foreign investment environment confronting state managers.

Integrated automation technologies can create needs for increased technological flexibility. We are all familiar with the mass production model; factory lines geared to high volume continuous output of a standardized product. In their review of the automobile industry, Jones and Womack reveal how the introduction of much more flexible automation, involving such elements as robots, automated handling, and machining cells, has changed the economies of scale in production dramatically (1985:401). They write that;

The major consequence of these advances in production technology has been to reduce the economies of scale in production, thereby decreasing the pressure for a minimum output of 2 million units. A full range of cars can now be produced in one or two plants at a much lower total volume at a competitive cost with much larger producers. This has been the biggest factor that changes the fortunes of smaller and medium sized producers (Jones and Womack,

1985:402).

Piore and Sabel contend that this move on the part of some industries towards technologies which are flexible enough to render short production runs economically viable constitutes a second industrial divide -- a moment when the path of technological development is itself at issue (1984:5). They comment that the current shift toward greater flexibility is provoking a turn to technological sophistication, the result of competitive pressures stemming from a growth in new producers world wide, and increasing costs.

As firm have faced the need to redesign products and methods to address rising costs and growing competition, they have found new ways to cut the costs of automized production. And the more they have narrowed the gap in cost between mass and craft production, the easier it has become to draw customers away from the formerly cheaper mass-produced goods (Piore and Sabel, 1984:207).

This flexible specialization, they contend, also imposes fewer constraints than mass production in terms of its interplay with the international economic system. Flexible specialization "could operate effectively in a large, open world economy; but it does not need the markets that such an economy would provide. The more technological development renders economies of scale irrelevant and raw materials substitutable, the more

likely each nation would produce a wide range of products on its own" (Piore and Sabel, 1984:276-77). New technologies not only affect the range of products we produce and consume, but the manner in which these products are produced. Specialized production based on flexible technologies can profitably be undertaken even with limited production runs in a wide variety of industrial sectors, ranging from computers through steel.

What do we learn from this discussion of changes in firm strategies, of the contrast between moves toward the internationalization of production on the one hand, and the move toward retrenchment through the adoption of integrated or flexible technologies on the other? Importantly, we must not assume that any process is firmly dominant or yet even indicates the likelihood of becoming so. We must take Piore and Sabel to heart; "[I]ndustrial technology does not grow out of a self-contained logic of scientific or technical necessity; which technologies develop and which languish depends crucially on the structure of the markets for the technologies' products; and the structure of the markets depends on ... fundamentally political circumstances" (1984:5). Struggles take place, and policy emerges from them. The aggregate of these

struggles "shapes economic institutions for a long time into the future" (Piore and Sabel, 1984:5).

Multinational strategies are the product of choices, not all of which are identical across firms or economic sectors. These strategies are not written in stone; they result from the firm's assessments of its market opportunities in the light of changing -- and fundamentally political -- realities. The 1970s were a turning point in patterns of internationalisation and international competition, and it is precisely for this reason that the question of the understanding of Canadian state managers becomes crucial. As the economic uncertainties and upheavals of the 1970s and 1980s have given rise to a number of different strategic options, it becomes increasingly difficult for state managers to assess Canada's location in the emerging international division of labour.

Lynn Mytelka has argued that current multinational options are influenced by the degree to which these will permit firms -- particularly, although not exclusively, in dynamic, high technology industries -- to cope with the accelerating pace of technological change. Product life cycles in most dynamic industries are shortening, "because the very nature of the products, their uses and the manufacturing techniques required for their

production differ substantially from one product generation to the next" (Mytelka, 1987:50). The rapidity of these changes has meant that multinational firms cannot make assumptions as to the nature of a future market for products it may be developing, given that "the very conception of what might constitute the market for a new technology or product is unclear" (Mytelka, 1987:50). To remain competitive firms in a range of industries (everything from data processing, through pharmaceuticals, chemicals, aerospace and automobiles, to household appliances) must attempt to gain the knowledge to alter production in order to control the transformation of the market. Rather than responding to market pressures, these new strategies are designed to permit the multinational to anticipate, and thus to shape, market changes.

While Vernon places primary emphasis on multinational investment strategies designed to secure sourcing (for raw materials investment), or to guarantee already existant market share (for manufactured goods), strategies defined by the need to ensure a role in defining a future, and undefined, market necessarily reflect different concerns -- concerns born of "the rising costs, risks and uncertainty of knowledge production" (Mytelka, 1987:51). These rising costs and

risks have led to firm behaviours designed to maintain competitive position whatever the future shape of the market while attempting to spread the risks -- financial and otherwise -- as broadly as possible. Among these strategies we find included the decentralization of research and development activities to autonomous research units within the firm -- a strategy which both gives the firm increased flexibility in its knowledge production activities and allows it to develop an autonomous, productive and creative environment which may encourage researchers to stay with the firm rather than to pursue independent careers. As well, this decentralization can extend to bringing foreign subsidiaries into the research process, integration made possible through the expansion of computer networks linking foreign subsidiaries and their parent firm (Mytelka, 1987:52-54).

Firms may also choose to delocalize or subcontract knowledge production to universities or independent research centres. This strategy is, in the first instance, a cost-reduction strategy, yet one which permits the firm to capture the fruits of a wider range of research activities. The strategy may also permit the firm to participate in joint research activities in which it otherwise could not afford to engage, but needs

in order to retain its competitive position in the oligopolistic market structure of much of MNC activity (Mytelka, 1987:55). In this same light, firms increasingly choose to participate in design and development joint ventures with their corporate rivals, reducing R & D costs, and market defining risks (since competitors gain a vested interest in similar technological adaptations) (Mytelka, 1987:60-66). The increased importance of partnerships between firms in the design and production of products in knowledge-intensive industries can be interpreted as an attempt by firms to secure their competitive position in an uncertain future market.

Finally, many multinationals are also choosing to reduce costs and risks through the granting of world product mandates. As Atkinson discusses, world product mandating appears to have advantages for the subsidiary firm (and, by implication, the host country) because ideally, the mandate "grants a single subsidiary the right to sell a specific product or product line on a world-wide basis" (1985:126). The subsidiary is assumed to thus gain responsibility for all aspects of research and development pertaining to the product or product line, responsibility in manufacturing, and responsibility for the international marketing of the

product. World product mandates allow the multinational parent to tap into local research and development resources (such as government incentives and grants), to gain access to host country procurement contracts, and to take advantage of host country investment tax credits and export subsidies (Mytelka, 1987:55). World product mandating, as with other strategies defined to come to grips with the pressures of increased competition, rising costs, and rapid technological changes, spreads the costs and risks of production.

In sum, while firms choose to invest abroad for a variety of reasons, the relationship of technology to international competitiveness has become an increasingly important one. Shorter product cycles, the rapid diffusion of sophisticated technologies, and competition for U.S. firms from European, Japanese, and developing country multinationals has eroded the monopoly position of the MNCs of the 1950s and 1960s. As the maintenance or enhancement of a firm's competitiveness becomes the motivator of a firm's investment decisions, locational concerns also tend to increase in importance. With an increasing trend toward knowledge-intensive production, both in traditional and high technology industries, firms are now concerned with the ability of an investment location to offer such factors as an educated

workforce, access to technologies, reliable infrastructures (from communications, transportation, and energy supplies), market proximities, and "quality of life" considerations (clean air, low crime), enhancing management and worker satisfaction with the investment location (confidential interview, Investment Canada, 1987). The product cycle model based on a slow worldwide distribution of new products is no longer applicable, and the pace of technological innovation and diffusion today would cause a firm to lose much of the rents it earlier gained from proprietary knowledge. Moreover, the high costs of research make it unlikely that many firms could amortize these costs solely by introducing new technology-based products in the domestic market. These new realities of international competition increase pressure toward flexible specialization on the one hand, and to the entrenchment of a "global" perspective upon the international market on the other.

The new realities motivating international investment also underline the fact that such investment can no longer be conceived solely in terms of the capital it brings. The amount of foreign investment in a domestic economy cannot be only reflected in figures of the dollar value of the assets of foreign firms. A

firm's ability to bring to a domestic economy the technological innovations related to increasingly knowledge-intensive production is as relevant for economic development as is foreign capital in most advanced industrial economies (including Canada). Research joint ventures with corporate rivals may not involve any transfer of capital, but if foreign investment is conceived in terms of the control it implies (as we earlier argued), then this venture involves participation in a technological environment whose direction is shaped by MNCs. State managers may well conclude that it is beneficial to encourage national firms to participate in joint endeavours with MNCs where the failure to do so may result in the non-competitiveness of national firms.

Danish firms, for example, have participated extensively in European joint ventures under the auspices of the European Strategic Programme for Research and Development in Information Technology (ESPRIT). While they have thereby gained access to new technologies, this access is not without costs. The nature of science and technology developed by small countries may well be decided by interests outside the country. Furthermore, in order to become and remain competitive, small countries may find themselves

spending a relatively larger share of their resources on R&D costs (Mytelka, 1988:20-1). Katzenstein's discussion of the limited options of small states seems particularly relevant here. Compromises in terms of control may have to be made in order to participate in the new technological environment.

THE STATE AND FOREIGN DIRECT INVESTMENT: PROTECTION IN NUMBERS?

Having examined changes in the nature of investment decisions taken by multinationals over the past two decades, we will now turn our attention to the manner in which state actors have interpreted that foreign investment. Outlining the costs and benefits which have come to be associated with the presence of multinationals in a national economy allows us to locate the Canadian state's concerns over direct foreign investment in a broader context, and itemizes the motivating factors for the state regulation of investment flows.

The broad question of the benefits and costs accompanying multinational investment is actually a relatively recent one. As briefly mentioned in Chapter One, the rules governing international property rights were well established by the mid-nineteenth century,

although the dictate that foreign investment would receive national treatment was in many respects more implicit than explicit. As Charles Lipson has noted, though, the norms governing foreign investments have changed dramatically since the mid-1960s, suggesting the breakdown of the implicit regime.

Expropriations were rare as recently as the mid-1960s, and reasonable compensation was expected. J. Paul Getty's observation still applied: the meek shall inherit the earth -- but not the mineral rights. Now this same regime is fragmented, and strictures against expropriation much weaker. Direct investments, in their many forms, are now subject to equally varied national treatment (1985:258).

The widespread development of broad measures to regulate direct foreign investment is but a part of this sign of regime breakdown. This is not to argue that there had been no restrictions to foreign investments before the 1960s; as we shall see, some sectoral restrictions applied well before then in Canada, among other countries. Those restrictions were generally longstanding, however, and were not imposed quickly. In theoretical terms, the rapid increase through the 1960s of nationalizations and regulatory policies and networks symbolized the fragmentation of the implicit assumptions about the right to national treatment, having implications for the strategic choices of multinational

corporations and the policy choices of state managers.

It is important to recall that the Canadian decision to regulate the flow of direct foreign investment was not anomalous in the early 1970s; many states were adopting legislative responses to issues raised by the activities of multinational firms. We will review a range of such state responses, thereby providing some indication of the international climate in which Canadian state action was taken. The MNC is, after all, the institutional embodiment of the processes and patterns of direct foreign investment, and as such, it provides a focus for concerns over foreign control of the activities of domestic firms.

Although there was some debate in the literature as to whether the state was being eclipsed by the multinational corporation (see Barnett and Mueller, 1974; Murray, 1975; Warren, 1975, for example), seminal books such as Vernon's Sovereignty at Bay and Servan-Schreiber's Le defi americain seemed to reflect a growing concern with the erosion of state power. In Canada, analyses of eroded sovereignty at the hands of the multinational corporation took on particularly dire tones. Kari Levitt warned that Canadian reliance on direct foreign investment had led to the "silent surrender" of indigenous capital, as in the postwar era

the Canadian economy became incorporated into the American empire:

In Canada economic resources are allocated primarily to suit the requirements of large private corporations, and the majority of these are under United States control. The constellation of the old east-west economy and strong central government has largely been destroyed by the economic forces of corporate continental concentration and corresponding regional political fragmentation. The Canadian entrepreneurs of yesterday are the coupon clippers and hired vice-presidents of branch plants today. They have quite literally sold out the country (1970:39-40).

Wallace Clement expressed similar concerns in The Canadian Corporate Elite. He argued that: "[p]rimarily using the multinational corporation, U.S. economic elites have penetrated the Canadian power structure," creating a situation where Canadian autonomy has decreased with economic development (Clement, 1975:117,119). In studies of Canadian dependency, the multinational corporation and its domination of domestic industry was pointedly seen as the vehicle through which the Canadian capacity for autonomous policy-making undermined.

In Canada, as first in Latin America, the benefits of MNC investment were being seriously questioned. These questions were heightened because the

multinational corporations in question were most often subsidiaries of U.S. firms. Just as Cox suggests, an hegemonic economic world order begins to break down when the non-hegemonic members begin to question whether the distribution of costs and benefits is equitable. Certainly, for Canadian political economists like Levitt and Clement, the answer was no.

The conventional wisdom of neoclassical economics has been to view the impact of foreign direct investment on host countries benignly. Foreign investors bring new, scarce resources to the host country, including capital, technology, management and marketing skills. Their presence is believed to increase competition, improve efficiency, and create jobs (Moran, 1985:3). As Black, Blank, and Hanson have pointed out, however, changing attitudes toward multinational corporations cannot be divorced from the international political system:

The fact remains, however, that the enormous increase in the international operations of business, particularly American business, in the 1950s and the early 1960s was a function of the growing affluence in the developed world, of the new degree of openness of national borders of the developed nations, of the increasing importance of foreign trade in the world economy, and also of the formation and stabilization of the Western Alliance under the political

and economic leadership of the United States.

Similarly, growing worldwide hostility to multinational corporations in the late 1960s and early 1970s reflects a number of conditions: the aggressive independence of the developing nations of the world; the insecurities within nations caused by increased openness and growing demands for enhanced national autonomy; the enormous increase in the sheer number of MNC operations in the world; the emerging opposition to many of the policies of the U.S. government; the weakening of the Western Alliance; and the decline of U.S. leadership within the international system (1978:8).

Black, Blank, and Hanson help illuminate the historical period which gave rise to the creation of FIRA, and throughout which there were important intellectual and legislative challenges to the neoclassical assumptions of the economic benefits of MNC investment. In effect, the implicit rules governing international investment were being seriously questioned; the international "regime" was at best being challenged.

Virtually all aspects of multinational investment became subject to criticism. As sources of scarce resources, multinationals came to be criticized for failing to bring in new capital when they invested, instead appropriating local capital for their own use; for failing to develop technologies appropriate to the

host-country economy; for failing to undertake substantive research and development activities in the host country; and for failing to make significant or serious use of indigenous management personnel. In addition, multinationals began to be held at least partially accountable for the host country's poor economic performance, particularly if they failed to source their production inputs from within the host country, failed to export their products and thus had not generated new export markets for the host country, failed to process raw materials within the host country, or if they had increased corporate concentration and lessened competition in the host country, mirroring their oligopolistic market position at home. These economic questions became compounded by concerns over the influence of multinational corporations over the host country's domestic political and social development, particularly over its foreign policy making and over its cultural and media industries (see the Gray Report, 1972:291-317, for example). Multinationals may provide employment, and can create economic activity, but their presence in a host country was no longer uncritically assumed to entail no costs.

The picture of MNCs running roughshod over the economic priorities and plans of the host state helped

to galvanize host state managers into action, and in so doing, altered any consensus about the vulnerability of states in their relationship with multinational firms. While it is important to stress that policies evolving to respond to the challenges of MNC investment are particular to each state's history and to a unique pattern of domestic and international circumstances, it is possible to develop a general typology of state regulatory initiatives. [3] This argument paints state actors and multinational corporations too distinctly, however. The late 1960s and early 1970s, as we discussed earlier in this chapter, witnessed the development of new MNC strategies in partial response to the emergence of MNCs from a variety of different countries. Different states underwent different struggles as their indigenous, and multinationalizing, capital either confronted, or allied with, existing (largely U.S.) multinational capital. At times, these struggles led to state initiatives to nationalize or divest the foreign assets operating in the country [4]. More often, however, struggles between nationalist classes (including some fractions of national capital) and multinational capital have led to some form of regulation of MNC activity, varieties of which we will discuss here. It is useful to recall that the very

introduction of these regulatory initiatives indicated in part the extent of the challenge to the "regime" principle of national treatment which had before implicitly governed international investments.

State Regulation

Regulatory policies -- formal authorization procedures for foreign direct investment -- are prevalent among many countries. Most members of the OECD, for example, employ some form of regulation, whether formal or implicit. Regulatory initiatives are employed to a far greater extent than are either nationalizations or divestments. This, of course, is to be expected; as we discussed in Chapter One, state actors are more likely to choose policies which lessen the political and economic costs of governance. Further, the hegemonic status of capitalism creates structural limits to the extent to which policies directly against the interests of capital can be put into place, although these limits vary with the nature of the class struggle in various countries and the position of multinational capital within these.

Regulatory initiatives have generally assumed three forms, which may exist together, or may exist independently. Further, each of these initiatives

possesses general characteristics reflecting the state's orientation toward the questions posed by direct foreign investment. Policies may be more limiting, or more encouraging, of foreign investment. Certainly in the early 1970s, we were witness to an expansion of limiting policies; that is, policies which sought to restrict or control the flow of foreign direct investment to the country. While economic change in the late 1960s and early 1970s saw an increase in limiting regulatory initiatives, the economic crisis of the late 1970s and early 1980s has encouraged some softening of those stances; softening apparent in Canada in the creation of Investment Canada to replace FIRA.

As well, regulatory policies can be more global or more sectoral. Just as nationalizations and divestments with rare exceptions (such as post-revolutionary Cuba) have been targetted toward particular sectors, so too have regulatory initiatives tended to favour sectoral limitations. Finally, regulatory initiatives may offer "carrots" rather than "sticks" in order to attract particular kinds of investments. The two can work in tandem as well; controlling foreign firms by insisting upon specified performance requirements, and yet permitting the same firms to qualify for national incentives programs should they comply.

Equally, of concern to the imposition of regulatory initiatives in a manner not applicable to either nationalizations or divestments is the issue of "transparency." This question was to come up repeatedly with the Foreign Investment Review Agency. Foreign investors faced with a regulatory regime in a host country are naturally concerned about the extent to which its policies are formally specified and embodied in clearly identifiable legislation. As well, foreign investors wish to understand the process by which decisions regarding the suitability of their investment proposals are made -- they wish the guidelines of acceptability to be "transparent" to them. Transparency for the state may, however, be a double-edged sword. Clearly enunciated policies may become a subject of great criticism, and thus of potential political cost for state actors. Thus, we find Safarian's argument about FIRA that, "it bears repeating that a number of other countries are doing similar things if more informally, and often less systematically, while providing only general statements of conditions" (1983:66).

The first form of regulatory initiatives typically used are entry policies, those which attempt to screen out unwanted investments, or seek to encourage a

particular structure of investments. Entry policies include the key sector approach, involving the closing off of particular sectors to foreign investments, or limiting the extent of investment in those sectors. As we will see, the key sector approach was one long utilized by the Canadian state, as it has been in Switzerland, Norway, Sweden, and the United States, among other developed countries (Safarian, 1983:56). Closing off a sector to direct foreign investment, or limiting the extent of such investment, is an issue relating to ownership, rather than to influencing the behaviour of foreign firms. Such regulatory policies concentrate upon the issue of foreign ownership, equating the level of foreign capital in a particular industry or economy with foreign control. The goal of these policies is to limit ownership. Sectors most often subject to some restrictions include defence and defence-related industries, public utilities, transportation and communications (including radio and TV broadcasting, and newspapers and magazines), primary industries, and financial services (OECD:1982). The Andean Pact's Decision 24 of 1970, for example, prohibited new foreign investment in utilities, insurance, commercial banking and finance, transport, advertising, and communications (Mytelka, 1979:62).

Entry policies also include provisions to encourage a particular structure of investments in a domestic economy. Here we find policies which require the membership of host country nationals on boards of directors, or the inclusion of nationals among the firm's key officers. Entry policies may also involve the negotiation of particular concessions from the investing firms, such as the requirement of host country equity participation. As well, we find policies such as the regulation of foreign takeovers of existing national enterprises, or policies which require the state to scrutinize the equity and debt financing provisions of the incoming investment.

Operations policies are the second form of regulatory initiatives employed. These may involve regulations affecting the taxation of foreign firms, for example, or which specify the terms under which foreign firms will be eligible for national incentives programs. Japan, for example, has maintained exceptions to national treatment of foreign firms in its government procurement programs and in research subsidies programs (Safarian, 1983:28). Finally, exit policies complete the litany of regulatory initiatives. These most often deal with requirements or restrictions affecting the repatriation of capital, and may have implications for

both voluntary and forced divestments.

States and MNCs in a Dynamic Context

The depiction of the range of policy options which have been employed by states seeking to redefine the nature of their relationships with multinationals suffers from one specific flaw. Such depictions describe state policy in a static environment: multinationals are seeking to invest and states adopt policy measures to confront their presence. This static environment has us reacting more to what has happened than to what is happening, in part because of lags in interpretation, compounded by the stereotypes we have formed. In truth, however, multinationals and states enjoy a reciprocal relationship, and the consequences of action, as we have outlined in Chapter One, can be as much unintended as intended. As Biersteker has argued with respect to the lessons learned from his case study of the relationship between the Nigerian state and multinational firms in the 1970s,

...it is clear first that an increase in the frequency of state actions is by no means equivalent to an increase in the effectiveness of state actions. Second, the sharing of equity is a long way from the sharing of control in joint ventures with transnational corporations. Third, any assessment of the balance of bargaining power

between states and transnational corporations must take account of the dynamics of change within each of the major protagonists (1980:207).

Where a review of possible state actions would lead us to conclude that the balance of benefits in the MNC-state relationship is shifting inexorably toward the state, Biersteker's admonition forces us to turn to the dynamic context in which states and firms truly operate, and react to each other.

States can "win" in their dealings with multinational firms. Joseph Grieco's examination of India's experience with the computer industry suggests that state managers can take advantage of competition between foreign firms in order to improve their own prospects for increased control over MNC activities within their boundaries (1982). In India's case, changes in the structure of the international computer industry (growth in number of competing firms, reduction in cost of computer components, development of the microcomputer) provided the state with greater options. Capital operating in the computer industry was not homogeneous, and did not ally -- giving room to nationalist forces within the state. As new firms, both indigenous and foreign, began competing in the Indian market, the state found itself in a stronger position to

extract concesssions from multinationals. The loss of one large firm, in this case IBM, was of less consequence in a competitive market; other firms were prepared to accept the Indian state's terms. Grieco's study contends that the state can bargain to extract concessions from the MNCs to which it is host. He does point out, however, that the changing structure of the international industry was crucial in providing the Indian state with the option to successfully expand its control over its national industry; in essence, that state gains are not independent of the broader industrial context.

Gereffi's study of the pharmaceutical industry in Mexico, on the other hand, underlines that not all states are successful when they seek to bargain with the multinational corporation (1985). The Mexican state sought to use its sovereign contro^l over barbasco (a source material for steroid hormones) in order to force negotiations with multinationals over their contribution to the development of a national steroid hormone industry. Continued domination of the technology needed to produce steroid hormones by MNCs, coupled with the declining international importance of barbasco as a source for these hormones, undermined the position of the state vis-a-vis the international industry.

Further, the international pharmaceutical companies were able to politically redefine the terms of the Mexican state's challenge from one perceived in national-foreign terms to one seen in terms of business opposition to the interventionist economic policies of the central government. In this case, capitalist class fractions did ally, severely limiting the ability of state managers to effect a nationalist outcome. This redefinition permitted the multinationals to reduce their own profile while gaining private sector allies against a common threat. As Moran underlines, Gereffi's study is important for it emphasizes that "[t]he outcome of any bargaining relationship between host authorities and foreign investors may be substantially shaped by the ability of the latter to form political alliances, and exercise political influence, within the host society itself" (1985:16).

The discussion of the relationship between the state and the multinational corporation must leave us sensitive to the fact that neither of these institutions is defined in stone; in effect, both the state and the multinational have been evolving in response to each other, as well as in response to changes in their environments. We cannot, after all, ignore that changes have happened; they have taken Vernon from Sovereignty

at Bay (1971) to "Sovereignty at Bay: Ten Years After" (1981), and a conclusion that his 1971 text would have better been titled Everyone at Bay. This dynamic context does not make the definition of policies any easier for state managers, of course. As difficult as it is to define state policy in a dynamic domestic environment, it is particularly difficult to do so when the target of policy is an international economic environment with which state managers do not interact systematically.

This chapter has served to further emphasize that state policy takes place in a dynamic environment. State initiatives in response to multinational firms are changing, just as the nature of multinational investment is itself changing. In fact, theory gives us an insight into the historical progression of these changes. MNCs, accustomed to branch plant investments in order to secure markets in the 1950s and 1960s, were challenged by the economic crises of the late 1960s and early 1970s to seek cheap labour and raw materials in order to ensure their own competitive position. These challenges were fuelled by the wider growth of MNCs in both the advanced industrial and newly industrializing countries; a growth in competition which spurred some firms to make concessions both to local capital and to

state managers. The simultaneous increase in the importance of technology to production brought about new joint arrangements between firms, research centres and/or states as MNCs sought to lessen the risk of high-cost high-technology activities. As we have seen, these developments brought about parallel moves to internationalization and technological flexibility, changing the pattern of foreign investment through these decades.

The difficulty with rapid, and occasionally seemingly contradictory, changes in global foreign investment patterns, of course, is that state managers are hard-pressed to design policy which meets these new challenges. New understandings of a country's position within a changing pattern of investment are simply difficult to gain. Existing norms of national treatment no longer seem to hold when nationalizations and regulatory policies have become an unavoidable feature of the international economy. Just as we have seen that constellations of power within domestic society may change, so too may the relationship between states, multinational corporations, and the international economic structures of which they are both a part. As we will argue, based on a prior understanding of Canada in the international political economy, FIRA was

ill-equipped to confront the new changes in international investment flows as these occurred. In Chapter Three, we will detail this historical perception embodied in the policy orientation of the Canadian state, and begin to contrast it with the empirical picture of international investment flows.

ENDNOTES

- [1] As Hymer points out, foreign control is not an easy thing to define, and is not always synonymous with foreign ownership. As the Gray Report discusses, for example, foreign control of Canadian industry grew more rapidly than foreign ownership between 1954 and 1967 (1972:16), reflecting a concentration of investment in those industries whose voting stock is controlled by non-residents. For purposes of classification, FIRA assumed control if more than 5% of the voting shares of a publicly traded corporation lie in the hands of a non-resident individual or corporation, or if 20% of the shares of a private firm are in the hands of a non-resident individual or firm.
- [2] Mira Wilkins' study of U.S. multinational investment (1974) led her to conclude that the primary motivation of corporate investments in manufacturing outside the U.S. in the period to 1970 was the desire to acquire or protect markets. She argues that it was often impossible to obtain effective market penetration solely with exports from the U.S., and that this penetration was a more important reason for manufacturing investment than differential rates of return per se. With a stable political system, high wage levels, and good prospects, Canada was an attractive location to establish manufacturing subsidiaries. Faced with growing demands from other host states with respect to MNC investment in raw materials production, U.S. firms also turned increasingly to Canada for investments in petroleum and mining as well.
- [3] Many states also develop incentive programs to attract investment, usually responding to regional objectives (promoting a better distribution of activity or deployment of resources across the country) or to industrial objectives (such as the promotion of productive investment or of industrial innovation). These incentives are quite prevalent; the OECD revealed that all of its members used investment incentives (often coupled with performance requirements) as instruments of industrial policy. Virtually every investment incentive program surveyed by the OECD did not discriminate between domestic and foreign-owned firms. See, OECD (1983).

- [4] Certainly the most dramatic of host state initiatives with respect to the presence of foreign multinationals has been the turn to nationalization -- the transfer of certain segments of economic activity, typically an industry, to national owners (Kobrin, 1980:69). Particularly prevalent during the late 1960s and early 1970s, the nationalization of foreign corporate assets appeared to symbolize the new reality of the relationship between less-developed countries (LDCs) and multinational corporations involved particularly in natural resource industries.

As a policy instrument, nationalization seemed an appropriate weapon to redress the inequities of a biased international economic system, but its benefits were perceived to be more concrete as well. In particular, nationalization was often motivated by a desire to achieve a larger share of the economic rents. Nationalization was to make rational economic planning possible for the economy as a whole and was to enhance the state's financial position sufficiently "to make economic diversification and the promotion of balanced economic growth attainable" (Shafer, 1983). Nationalization was seen as having the potential to generate greater employment, to make possible the promotion of local employees to management status, as well as to silence nationalist critics.

Charles Lipson points out, quite rightly, that in the face of firm nationalizations, multinationals have responded themselves by self-consciously planning to diminish their exposure to political risk (1985:23). [See, for example, Theodore H. Moran, ed. (1981); or, Stephen J. Kobrin (1982).

Key to the discussion of political risk is the idea that specific firms are the best targets of nationalization, or, in special instances, particular sectors. Nationalization is more difficult to use as a general "cure" for the problems created by multinational presence in a diversified economy dependent on foreign investment in several sectors; an economy such as Canada's. Finally, authors such as Lipson (1985) and Wilkins (1974) have pointed out nationalizations have made certain countries more attractive as locations for natural resource investments -- those countries where a stable pattern of expectations has been built up as to their likely behaviour. As Lipson has written, "investors can neither foresee nor

Table 3.1: Nonresident Long-Term Investment in Canada,
Selected Years, 1900-1967 (Millions of \$C, constant \$:
1949=100)[a]

Year	Amount (\$) Owned by Resident Of			% of Totals		
	U.S.	U.K.	Other	U.S.	U.K.	Other
1900	435	2,720	36	13.6	85.2	1.1
1914	1,776	5,601	359	23.0	72.4	4.6
1918	2,264	3,790	249	36	60	4
1926	4,211	3,474	224	53	44	3
1930	6,189	3,673	249	61.2	36.3	2.4
(Direct)	2,647	521	55	26.1	5.1	0.5
(Port.)	3,542	3,152	194	35.0	31.1	1.9
1939	6,568	3,918	453	60.0	35.8	4.1
(Direct)	2,976	579	78	27.2	5.2	0.7
(Port.)	3,592	3,339	375	32.8	30.5	3.4
1945	6,653	2,333	469	70.4	24.6	5.0
(Direct)	3,072	464	81	32.5	4.9	0.8
(Port.)	3,581	1,869	388	37.9	19.7	4.2
1946	6,655	2,155	455	71.8	23.2	4.9
(Direct)	3,133	432	81	33.8	4.6	0.8
(Port.)	3,522	1,723	374	38.0	18.5	4.0
1950	6,364	1,701	355	75.5	20.1	4.2
(Direct)	3,329	455	79	39.5	5.4	0.9
(Port.)	3,035	1,246	256	36.0	14.7	3.2
1955	8,839	2,016	715	76.4	17.4	6.2
(Direct)	5,599	759	271	48.4	6.6	2.4
(Port.)	3,240	1,257	444	28.0	10.8	3.8
1960	13,061	2,624	1,669	75.2	15.1	9.6
(Direct)	8,241	1,199	615	47.4	6.9	3.5
(Port.)	4,820	1,425	1,054	27.7	8.2	6.0
1967	18,799	2,398	2,076	80.7	10.3	8.9
(Direct)	11,401	1,443	1,037	48.9	6.2	4.4
(Port.)	7,398	955	1,039	31.7	4.1	4.4

Source: Aitken et al., 1959:157,158; Gray Report, 1972:15.

[a] Constant dollar index constructed using: Canada. Dominion

CHAPTER THREE

CANADA AND THE INTERNATIONAL POLITICAL ECONOMY: CHANGING PATTERNS OF DIRECT FOREIGN INVESTMENT

Any state's attempt to regulate or restrict foreign direct investment potentially has consequences for both the domestic and the international political economy. The choice between such policy alternatives depends on existing perceptions of the international economic environment; state managers enact policy in response to an observed or anticipated change in the relationship between domestic actors and the extent of foreign direct investment. Chapter Two outlined some of the changes in the pattern of foreign direct investment, highlighting both the rapidity of change and its multi-dimensional nature. Chapter One outlined a model of state manager perception of change, and the significant role which classes or class fractions play in representing particular interpretations of international economic change to state managers. Perceptions do not always correspond to the reality of complex international economic conditions. It is through the articulation of the international economic environment in domestic class struggle, and in the challenge between these emerging perspectives and prior state knowledge (found in the state's participation in a defined international order) that state managers may be limited in their ability to

choose policy which responds to any sense of the "objective" changes of the international environment.

While we have already gone over a general theoretical review of the changing pattern of direct foreign investment, we have not yet defined the pattern of international investment in which Canada is, and has been, participating. In order to understand the perceptions of Canadian state managers in their desire to regulate foreign direct investment, and the relationship of these perceptions to the general pattern of direct foreign investment, it is necessary to introduce a discussion of the international context in which Canada has found itself, and how that context has changed. Through the detailing of this context, we can evaluate the relevance of state manager perceptions of the changing international environment, and better understand the way in which that environment was translated to them. The Gray Report, published in 1972, painted a picture of Canada's international position as a host to direct foreign investment, and it is the antecedents to this picture which we will initially discuss. Based primarily on 1967 statistics, the Gray Report was the most influential statement of the extent of foreign investment in Canada, and as such was widely debated in the country during the period surrounding the

creation of the Foreign Investment Review Agency. It helped considerably to shape -- but did not dictate -- the policy options of state managers, and the details it presented are a great part of the "picture" accepted by these managers. In order to situate the shaping of state manager perception, we will also discuss the nationalist and continentalist schools of thought which have dominated debates about the formulation of Canada's international economic policy.

We will then turn our attention to developments in the twenty years after the mid-1960s, the period during which FIRA was enacted and operated. We will demonstrate that Canadian state managers made certain assumptions about the nature and direction of foreign direct investment in the creation of FIRA -- in particular, that Canada had enough investment, that investment in Canada was of a branch plant nature, and that Canada could always continue to attract investment, no matter the policies which might be put into place to regulate it. An overview of specific investment patterns will allow us to evaluate the extent to which the processes outlined in the theoretical discussion of Chapter Two (globalisation of investment, alternatives to branch plant investment, adoption of flexible technologies making smaller production runs more viable)

were applicable to the Canadian case, and to assess the validity of Canadian state manager assumptions about foreign investment. Understanding changes in the international environment with reference to Canada will permit us to paint a picture of the Canadian "location" in international investment flows, against which we can assess the assumptions behind state policy.

HISTORICAL PATTERN OF FOREIGN DIRECT INVESTMENT IN CANADA

Foreign borrowing has defined the pattern of Canadian economic development. In the nineteenth and early twentieth centuries, Canada relied heavily on foreign portfolio investments, borrowing substantial sums on government account or guaranteed by governments. This foreign borrowing was undertaken in order to finance large scale infrastructural projects, particularly in railroad and canal construction, in the development of the western wheat economy, and in the financing of associated manufacturing (Levitt, 1970:60-62). Although most of this borrowing was in the form of debt securities (with the London bond market providing the main source of foreign capital), A. E. Safarian has noted that as much as \$140 million of a total capital inflow of \$850 million between 1870 and

1900 was in the form of direct foreign (equity) investment to Canada (1973:7). Franck and Gudgeon have further noted that most of the direct investment was by United States, rather than British, interests (1975:85) [11]. After 1900, the number of foreign-owned, largely American, manufacturing plants and subsidiaries in Canada increased rapidly, as did U.S. investment in Canadian primary resources. By 1913, direct investment represented over one-fifth of the total stock of foreign capital invested in Canada (Safarian, 1973:7).

While wars and depression slowed the flow of international capital, massive postwar foreign investment continued the century-old pattern of Canadian economic development. The growth of U.S. investment between 1918 and 1939 was slow, particularly as compared to the post-World War II period, but it was important. That investment was concentrated particularly in manufacturing and merchandising as the new mass-production techniques of consumer-goods industries were exploited -- and Canada was next door (Marr & Paterson, 1980:295). It is, in fact, impossible to study Canada's economic history without noting the degree of foreign ownership and control of its industry, which to this day remains considerably greater than in other developed economies (Feltham and Rauenbush, 1973;

Globerman, 1985; Safarian, 1983).

As it is today, direct foreign investment in Canada was dominated early by United States investors. In fact, most analyses of foreign direct investment in Canada are quick to note this, and point to Canada's close economic, geographic, and cultural ties to the United States as factors making research into the Canadian case particularly compelling (see, for example, Globerman, 1985; Safarian, 1983:14). Not only is Canada host to a large amount of foreign direct investment, but the majority -- near 80% -- of that investment is held by U.S. interests. A brief examination of U.S. investment in Canada prior to the debates about such investment characteristic of the late 1960s and early 1970s provides a context for the emergence of these issues, and helps to situate Canada within the international political economy.

The extent of U.S. investment in Canada, and the rapidity of its growth from the turn of the century through the post-war period is illustrated in Table 3.1. Of striking note is the enormous increase in U.S. direct investment during the years following the Second World War, increasing from over \$3.1 billion in 1946 to \$11.4 billion in 1967 (\$2.5 billion and \$17 billion in current dollars).

Table 3.1: Nonresident Long-Term Investment in Canada,
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(Port.)	7,398	955	1,039	31.7	4.1	4.4

Source: Aitken et al., 1959:157,158; Gray Report, 1972:15.

[a] Constant dollar index constructed using: Canada. Dominion

1949-1952. Ottawa: Queen's Printer, p. 14, 110-111; Canada.
Dominion Bureau of Statistics (1962). Prices and Price Indexes,
January 1962. Ottawa: Queen's Printer, p. 30; Canada.
Statistics Canada (1972). Prices and Price Indexes, July 1972.
Ottawa: Information Canada, p.54.

As the Gray Report on foreign direct investment points out, about half the increase in United States investment during this period was for the development of Canada's natural resources, reflecting the raw materials needs of U.S. investors for their processing and manufacturing plants in the United States (1972:14). As Melissa Clark-Jones has detailed, in 1952 the American state had directed its agencies to assure mounting supplies of materials and energy to meet the U.S.' economic and security objectives. The 1952 publication of the Paley Report (President Truman's Report of the President's Materials Policy Commission, named the Paley Report after its chair), saw Canada identified as an important source of "critical" raw materials in which the United States was not, or was no longer, self-sufficient. Further, Canada was attractive because it was a "Western Hemispheric nation" (and hence, strategically close by), and a "friendly" source country (Clark-Jones, 1987:12-21). This U.S. desire to expand its foreign investment in resource industries is clearly evident in the expansion of petroleum and mining investments in the post-war era. It is, moreover, echoed within Canada, where state managers perceived that Canada played an international role as the site of resources-based foreign investment.

The extent of U.S. direct investment into Canada in the post-war era also created expectations under which it was almost impossible for state managers not to believe that Canada could attract huge amounts of foreign investment regardless of the international competition. Other than resource-based investment, most of the remainder of the increase in U.S. direct investment was largely in manufacturing, whether for the start-up of new firms, the expansion of existing facilities, or the takeover of Canadian firms.

These figures are certainly instructive. We can better appreciate the process behind them, however, if we look more specifically at the types of economic activities being undertaken by U.S. investors in Canada. As R.T. Naylor (1975b) has documented, U.S. direct investment in Canadian industry -- both resource- and manufacturing-based -- began as early as the 1800s, before Canadian Confederation. In 1804, for example, the first Canadian paper mill was established in Quebec in a joint venture between Montreal financiers and New England paper mill interests (Naylor, 1975b:79). In the 1850s, American capital was involved in the financing of the Nova Scotia gold rush. United States capital was also involved, although minimally so, in the financing of the construction of the railroads, as well as in the

nascent Canadian lumber industry. The first American branch plant in Canada was a file factory at St. Catharines, Ontario, established in 1870 (Marshall et al., 1976:11). Investment patterns were such that, between 1890 and 1930, "the roots of foreign control of Canada's industrial structure were planted" (Stothart, 1987:33), a fact clearly reflected in the range and nature of the foreign (largely U.S.) firms which were then establishing plants in Canada.

To some extent, the roots of the resource-based investment were set before the Second World War as well. While large investment certainly had not taken place in the petroleum and natural gas industry (and did not until the oil field exploration at Leduc, Alberta -- see Aitken, 1967:217-8), other resource investments had begun. Marr and Paterson report that by the mid-1920s, for example, the Royal Commission on Pulpwood was raising concerns as to the proportion of forest wealth which had been effectively seconded to foreigners (1980:295).

Why did this U.S. business expansion into Canada occur so early in the history of the movement of firms abroad? Certainly, the largely receptive attitude of the majority of Canadian state managers and industry to foreign direct investment provided a climate attractive

to U.S. business interests. Foreign portfolio investment had helped to develop Canadian infrastructure and to maintain a high standard of living for Canadian settlers, and foreign investment was still seen as a positive feature in Canadian economic development. Canada's proximity, in light of early technical limits on intercontinental enterprise, also contributed to the country's attractiveness (Carroll, 1986:200; Franck and Gudgeon, 1975:85). This proximity proved particularly attractive in the post-war era as the United States became increasingly interested in Canada as a source of raw materials. As well, U.S. investment was attracted to the Canadian market by the imposition of the protective tariffs of the 1879 National Policy. Finally, and some would argue most importantly, the British Empire's network of trade preferences provided incentive to U.S. firms to gain and secure access to the Canadian market and thereby to the Imperial preferential trade system (Molot and Williams, 1984:82; Williams, 1983:57-8). However varied the reasons, Canada certainly occupied a place of privilege in the investment plans of growing U.S. firms. As Kari Levitt describes,

[d]irect American investment in Europe has concentrated on producing and selling manufactures in these markets; in the underdeveloped

countries of Latin America and the Middle East it has concentrated on extracting raw materials. In Canada we are in the unique situation of playing host to large American investments both in the resource and in the manufacturing sectors. As a result Canada has acquired markets for its industrial raw materials and has become a market for manufactured goods produced by American corporations located both here and the United States (1970:60).

We can gain valuable insight into Levitt's observation by examining the statistical profile of foreign investment by sectors (Table 3.2). These data indicates, as expected, that by 1967 the areas of greatest concentration of direct foreign investment were in manufacturing and natural resources; non-resident control of manufacturing was estimated at 57 percent by the end of 1967, at 74 percent in the petroleum and natural gas industries, and at 65 percent in mining and smelting. It is evident from the statistical picture that foreign ownership and control between 1926 and 1967 increased in manufacturing, oil and gas, and mining, but declined in utilities and railways. The prevalence of portfolio rather than direct investment in these sectors certainly "protected" them from a greater degree of foreign control, while Canadian policies designed to ensure sectoral protection of communications and transportation industries played a role in altering

ownership balances in these sectors.

Table 3.2: Non-resident Ownership and Control as a Percentage
of
Capital Invested in Selected Canadian Industries,
Selected Year-Ends, 1926-1967

Year	All Non-residents		U.S. residents	
	Owned	Controlled[a]	Owned	Controlled
Manufacturing				
1926	38	35	30	30
1939	42	38	34	32
1948	42	43	35	39
1954	47	51	37	41
1960	52	59	41	44
1967	52	57	44	45
Petroleum/ Natural Gas[b]				
1954	60	69	57	67
1960	62	73	53	64
1967	62	74	51	60
Mining/ Smelting				
1926	37	38	28	32
1939	40	42	31	38
1948	39	40	32	37
1954	56	51	48	49
1960	60	61	52	53
1967	61	65	51	56
Railways				
1926	55	3	15	3
1939	57	3	18	3
1948	45	3	21	3
1954	35	2	16	2
1960	26	2	9	2
1967	19	2	8	2
Other Utilities[c]				
1926	32	20	23	20
1939	27	26	20	26
1948	20	24	16	24
1954	16	11	14	10
1960	14	5	12	4
1967	19	5	18	5

Source: Gray Report, 1972:20; Aitken et al., 1959:159;
Safarian, 1966:14

[a] Foreign Ownership ratios measure equity and debt capital owned by non-residents as a percentage of total capital employed in the industries. Foreign Control ratios measure

non-residents in those companies whose voting stock is controlled by non-residents, all of which is taken as a percentage of the total capital employed in the industries. The ownership ratio for a particular industry will exceed the control ratio by the extent to which non-residents invest in companies they do not control, but will fall short of it by the extent to which residents invest in companies which non-residents control (see Safarian, 1966:13).

[b] Components of the petroleum and natural gas industry were included in other groups until 1954, particularly mining and smelting, although investments in exploration and development of petroleum by companies engaged principally in refining and production of petroleum products were included in manufacturing

[c] Utilities include air, road, water and urban transport, telecommunications, and hydro-electric utilities, as well as many of the large Crown Corporations.

The implications of many decades of eager encouragement of foreign investment in the days after Confederation are not to be understated. Although in the pre-World War I period, U.S. branch plants controlled only 10% of Canadian industrial capital (Williams, 1983:27), and although by 1930, foreign ownership of manufacturing assets had not yet exceeded 40% [with U.S. investment accounting for 82% of that total (Aitken et al., 1959:159)], such investment is crucial to our understanding of the nature of Canada's industrial structure. To that end, Stothart has detailed a list of those multinational enterprises which incorporated in Canada in the period prior to 1930. These include General Electric (1892), Westinghouse (1896), Otis Elevators (1902), International Harvester (1903), Du Pont (1910), IBM (1911), John Deere (1911), Ford (1911), General Motors (1918), Sperry (1919), Union Carbide (1922), RCA (1924), Chrysler (1925), Celanese (1926), Goodyear (1927), Ralston Purina (1927), Pratt and Whitney (1928), and General Goods (1929) (1987:33). As Glen Williams has pointed out, these firms operated in sectors showing the greatest industrial dynamism and technological growth, not only in Canada, but internationally (1983:27-8). Westinghouse and General Electric, for example, quickly came to dominate

industrial electrical equipment production in Canada before the first World War. Some of these firms invested in Canada through the takeover of Canadian firms -- a pattern which later caused concern. General Motors, for example, gained its Canadian branch by absorbing the McLaughlin Buick Company of Oshawa.

**Table 3.3: Non-Resident Ownership of Canada's
Manufacturing and Other Industries, 1967**

Manufacturing Industry	% Majority of Non-Resident Ownership as Measured by			
	Assets	Sales	Profits	Taxable Income
Food & beverages	31.2	27.2	30.1	32.5
Tobacco	84.3	79.9	82.7	83.3
Rubber products	93.1	91.4	90.0	88.4
Leather products	22.0	21.4	25.2	27.3
Textile industries	39.4	28.5	54.4	54.3
Wood	30.7	22.0	23.6	22.9
Furniture	18.9	15.6	20.8	23.2
Printing, publishing & allied	21.0	13.8	22.3	23.2
Paper & allied prods.	39.4	41.4	40.6	40.2
Primary metals	55.3	51.1	62.4	64.3
Metal fabricating	46.9	45.2	65.0	63.1
Machinery	71.8	72.6	78.9	88.3
Transport equipment	86.6	90.5	89.9	88.5
Electrical products	64.2	62.8	78.2	88.0
Non-metallic mineral prods.	51.5	42.3	47.0	53.1
Petroleum & coal prods.	99.5	98.9	98.6	99.4
Chemicals & chemical prods.	81.5	81.3	89.6	89.4
Miscellaneous manufacturing	53.9	51.2	72.1	72.6
Total--All Manufacturing	58.0	54.7	63.6	62.9
Total--All Mining	63.0	60.0	55.0	47.0
Construction	14.5	11.3	13.4	17.9
Transportation	8.9	11.3	26.5	25.6
Communications	1.0	1.1	0.5	1.1
Public Utilities	2.7	8.0	8.1	28.6
Wholesale trade	27.9	27.4	30.1	30.6
Retail trade	20.5	18.6	17.8	32.8
Financial industries	12.8	11.7	19.2	14.6

Source: Gray Report, 1972:21, 22.

By 1967, the die was clearly cast. A survey of manufacturing activities in Canada (Table 3.3) illustrates the extent to which Canadian economic activity had been penetrated by foreign interests. The level of non-resident ownership of Canada's firms had grown to such an extent that the Gray Report was forced to conclude that "the scope for further sharp increases in foreign control" had likely been reduced, since, for one, "the degree of foreign control of Canadian business in the economy is already very high", and secondly, "of the capital employed in Canadian controlled firms, about one-third is in government enterprises", and thereby protected (1972:16). The assumptions implicit in the creation of FIRA, however, suggested that Canada would continue to attract foreign investment no matter the circumstances.

As Table 3.3 indicates, non-resident ownership of Canadian industries was greatest in the petroleum and coal products industry, with figures approaching 100 percent ownership of assets, sales, profits and income. Within Canadian manufacturing activity, figures also exceptionally high (above 80 percent) included tobacco, rubber products, transportation equipment, and chemicals. Canadian ownership figures were also at less than 50 percent in primary metals, machinery, electrical

products, and non-metallic mineral products. The mining industry in general revealed very high ownership levels, at over 60 percent in both sales and assets. It is clear that the general argument of foreign penetration of the economic activity of Canadian manufacturing and resources industries can be borne out through statistical evaluation. Canadian ownership is highest in manufacturing endeavours such as furniture, leather products, wood, printing and publishing, and food and beverages, as well as in other industrial sectors from construction to financial industries. These 1967 data clearly support the contention that most investment, and by extension, most United States investment, was attracted to Canada as a source of raw materials and as a market for the products of its manufacturing subsidiaries.

Despite this early penetration of those manufacturing sectors which were crucial to the development of the newly-industrialized countries of the late nineteenth and early twentieth centuries, and despite the overwhelming penetration of Canada's resource industries, Canadian state managers did not feel the need to develop restrictive investment policies. Until the mid-1950s, there was effectively no debate as to the merits of Canada's open door investment

regime, a fact consistent with the prevailing and historical orientation of the Canadian business elite to foreign investment, and through existant structures of representation, the orientation of the Canadian state. Before turning our attention to the changing patterns of foreign investment, we will briefly examine the regulatory policies of the Canadian state in the pre-FIRA era, and review the main tenets of thought within Canada on the subject of foreign direct investment. Such a review will allow us to see more clearly the assumptions inherent in the specification of Canadian state policy.

Canada and the Regulation of Direct Foreign Investment

As Feltham and Rauenbush have discussed, expressions of concern about foreign investment can be found throughout Canadian history (1973:40). Yet, as Michael Bliss has pointed out, "[f]ew people in the half-century after Confederation questioned Canada's absolute reliance on foreign capital" (1970:33). The view, summarized in 1968 by an Ontario Minister of Trade and Development that "we'd still be chasing Indians if it were not for foreign investment" (cited in Williams, 1983:103) continues to be prevalent. On the other hand, it is also true that much has changed since an inter-war

Canadian Financial Post headline bragged; "Claim Tariff Brings Canada 90 New Plants: Government Points to Long List" (cited in Gilpin, 1976:269). Business International may have said it best in its February 19, 1971 story, headlining that "Canada Reacts Against Foreign Investors But Fears Losing Their Help." Underpinning this ambivalence was the Canadian state's historical understanding, well established through continentalist orthodoxy and the prevailing view of the Department of Finance, that foreign investment was crucial to Canada's economic development -- that without it, Canada would face calamitous balance of payments consequences.

Regulatory initiatives enacted prior to FIRA were characterized by a "key sector" approach to investment restrictions, occasionally coupled with tax incentives or restrictions, and the establishment of guidelines and regulations (see Appendix I). The key sector approach, most widely used, involves the identification of economic sectors for which national control is perceived to be desirable. In the 1880s, in the first such example, the Canadian state attempted to discourage American investment in the Canadian Pacific Railway. In 1904, this preference for non-American investors found legislative manifestation in the Railway Act Amendment,

which stated that a majority of the directors of any company receiving government aid for rail construction must be British subjects (Franck, 1976:57). Later regulatory and restrictive initiatives concentrated largely on ensuring majority Canadian ownership of transportation, communication, and financial networks in the country. This approach is consistent with that identified in Chapter Two as the one most widely applied by OECD countries. It was equally consistent with the desire for protection in the home market of some of Canada's largest firms (banks and financial enterprises in particular). Ironically, it is in measure through the protection from foreign ownership which had been applied by the Canadian state since 1913 that Canadian banks were able to gain the oligopolistic advantages which allowed them so quickly and early to become multinationals themselves.

Despite these few measures aimed at restricting particular sectors from foreign control (sectors in which the activities of Canadian capitalists were particularly concentrated), there was little general awareness of the problems and dilemmas which might be posed by the presence of a high degree of foreign investment in the Canadian economy. This, of course, is unsurprising given the dominance of the continentalist

orthodoxy -- an orthodoxy which we will review below. In the years up to 1930, for example, there was no clear identification of foreign investment as a factor which either encouraged, or retarded, Canadian economic growth (Stothart, 1987:33). In the years after World War II, U.S. investment to Canada rose quickly, but this increase coincided with a period of relative prosperity in Canada. It was difficult to be critical of the foreign investment which at least appeared to be related to the general prosperity, particularly given the fear that the post-war era would mean a return to the Depression which had followed the first war (Mackintosh, 1959:63). The Canadian ethos was in large measure the ethos of C.D. Howe: "what was good for business was good for everyone else and ... what was best for business was that it should be left alone" (Gwyn, 1985:64).

The increase in foreign control in the immediate post-war period provides an important backdrop against which the debate about the merits and costs of foreign investment was to begin. As Feltham and Rauenbush indicate, it is only in this post-war period that "entire industries, not just individual corporations, [became] subject to non-resident control" (1973:40). It is during this period that American investments, while significant since the 1920s, crossed a threshold of

concentration to become a source of public attention. Measured by assets, sales, profits, or taxable income, for example, we find that almost 90% of the manufacturing in the Canadian transportation industry was owned by nonresidents by the mid-1960s (due in large part to the activities of the "Big Three" car manufacturers in Canada), or that virtually 100% of the assets related to the production of petroleum and coal products in Canada were owned by nonresidents (see Table 3.3). This prominence provided a clear focus for those concerned about the consequences of a high degree of direct foreign investment.

There is little doubt that Canadian policy makers were aware of the likely foreign investment impact of their post-war policies. In particular, the 1947 Emergency Exchange Conservation Act, an import control policy, "was designed to encourage the substitution of domestically manufactured products for imported consumer goods, frequently through the establishment of a branch plant in Canada by the foreign manufacturer" (Wolfe, 1978:7). C.D. Howe and his key advisers, while they clearly wanted to stimulate the growth of manufacturing in Canada, also expected that these policies would attract foreign investors who would help them achieve their goal. Balance of payments considerations were of

foremost importance to these policy makers, who needed capital to finance the growth of the post-war economy. Howe in fact praised the extent of foreign investment in Canada after the import controls had been in operation for two years, saying in October of 1949 that; "Some 2,000 American companies and branch plants are now established in this country of which more than 1,000 are engaged in manufacturing. We hope that more American companies will avail themselves of the favourable conditions for investment in Canada" (cited in Wolfe, 1978:8).

The mid-1950s saw a diminution in the degree of enthusiasm for foreign investment in some quarters, however. Inflation had become a persistent problem. Questions were raised as to the wisdom of following a policy completely committed to liberalization in trade and all economic relations (the legacy of the costs of the Depression), and misgivings began to come to the fore as to the extent of United States control of Canadian industry (Mackintosh, 1959:64). In 1956, the political press was dominated by the Trans-Canada pipeline debate in the House of Commons, an episode which focussed public attention on foreign investment. This debate seemed to reflect the broader pattern of Canadian economic development; a cross-Canada pipeline

to bring western gas to eastern markets, heavily subsidized by the Canadian state, built by a U.S. firm. As Michael Bliss has written, calls of a sell-out to the United States were inevitable, for the picture painted, of "the government of Canada, and its American-born minister [C.D. Howe], apparently underwriting an American company's control of Canada's trans-continental gas pipeline" (1987:508) was a highly charged one.

After decades of warm reception to foreign investors, Canadians began to challenge the state's traditional open door policy. As we will see in Chapter Four, part of reason for this challenge lay in the rise of Canadian nationalism, espoused by members of the new middle classes. Both this nationalism, and in academic circles, the renewed focus on the study of political economy, owed a great debt -- whether explicitly or not -- to the arguments put forward by Harold Innis. It is to the outline of these nationalist beliefs, and to the continentalist position which underscored traditional Canadian policy, that we now turn our attention.

INNIS, MACKINTOSH, AND DIRECT FOREIGN INVESTMENT

In order to appreciate the reasons behind Canada's traditional "open-door" investment policy, and the historical understanding of its state managers as to the

Canadian location in the international economy, it is useful to outline very briefly the main tenets of the decades-old Canadian political economy debate. Melissa Clark-Jones (1987:222) has characterized this debate as one between the "anti-staples" nationalist school and the "pro-staples" continentalist school, intellectual traditions pioneered by H.A. Innis and W.A. Mackintosh, respectively. As is the case with many of the debates on trade and industrial life in Canada, these analytic traditions continue to dominate the discourse about the need for, and future role of, foreign investment in the development of the Canadian economy. Both traditions have been present in the formulation of Canadian economic policy, and have found adherents within the Canadian policy apparatus and amongst policy advisors [2]. Both traditions have not held equal sway in the determination of policy, however; as Rianne Mahon has pointed out, the state's representational structure usually favours a particular class or class fraction embodying a particular ideology or ethos. In this case, the continentalist school has been more successful in defining policy outcomes (see, for example, Melissa Clark-Jones' observation on resource policy, 1987). Authors such as Williams are most adamant in pointing to the importance of this debate for our understanding of

the contemporary Canadian political economy, arguing that "... a key to our national confusion, ignorance, and inactivity ... has been the dispute between the experts on the nature of the crisis [of industrial activity in Canada], its solutions, and even its existence" (1983:148).

Neither Innis nor Mackintosh specifically addressed questions of the impact of foreign direct investment upon Canada. Still, it is possible to gain some insight as to their position on the issue from their writings. Both Innis and Mackintosh begin their analyses acknowledging that staples production and export were crucial to the economic viability of the new Canadian colony. Innis, however, perceived that an excessive Canadian reliance on staples production and export would effectively create a staples "trap", reinforcing and eventually exacerbating the technological gap between Canada and its economically mature trading partners. Mackintosh, on the other hand, saw staples export as simply the first step along the path to Canadian economic growth. These differences are at the root of the different intellectual perspectives on the role and impact of direct foreign investment.

For Innis, the key to understanding Canadian political economy was found in the concept of the

technological gap. The North American settlers, Innis argued, in order to maintain the standard of living which they had come to expect from their European experiences, had to be able to trade with the European centres in order to obtain the goods they desired. The U.S., with a less hostile environment and a larger population was able to close the gap and produce its own manufactured goods. Canadian settlers were not so fortunate, and their reliance on natural resources as the goods of trade with the European parent countries only served to exacerbate the gap in manufacturing capacity. As Williams has described this process: "[t]rading Canadian resources for the manufactured goods of the centre had the long-term effect of stimulating the further specialization of production in each society. Thus, it became increasingly difficult for Canada to catch up with the centre of the world economy, leaving her ever more dependent on resource exports" (Williams, 1983:133). This dependence reflects the consequence of Innis' technological gap.

Innis clearly perceived that the decision to put in place the National Policy tariffs was the crucial one influencing the pattern of direct foreign investment, particularly American investment, in Canada. For him, the imposition of these tariffs and the securing of

Imperial preferences "compell[ed] the establishment of branch factories from the United States" (Innis, 1956:235). The tariffs had effectively precluded the possibility that Canada would become a significant exporter of manufactured goods, since they had only served to attract branch plants and capital equipment rather than stimulate the development of Canadian productive capacity. The presence of branch plants abetted by the tariff, furthermore, helped to ensure that the technological gap which characterized Canadian development relative to its economically mature trading partners would never be narrowed. Innis writes that the system of tariffs and imperial access

...proved enormously advantageous to American branch plants. Paradoxically, the stoutest defenders of the Canadian tariff against the United States were the representatives of American capital investors. Canadian nationalism was systematically encouraged and exploited by American capital (Innis, 1956:405).

Certainly, in the free trade debate of 1911, this was the case. The Canadian Manufacturers' Association, representing many American firms operating in Canada, coined the famous slogan "No Truck or Trade with the Yankees" in its pamphlets opposing free trade. Branch-plant managers expressed the fear that the deal could displace U.S. multinationals operating in Canada,

and could cost these managers their jobs (Gwyn, 1985:37). These fears were reflected in the nationalist rallying calls of the 1970s, as Chapter Four will detail, and yet were not reflected in the creation of FIRA.

Innis contended that the American branch plant presence in Canada made possible the "pull of raw materials and finished products in which depletion of American resources has been conspicuous" (1956:235). As Williams emphasizes, Innis clearly believed that the unrestricted inflow of U.S. capital into Canadian industry would only succeed in relegating Canada to de facto colonial status (1983:134). The United States would use Canada as a source of raw materials and of those manufactured goods determined by its needs and its corporate agendas. This "Canadian location" in the international political economy, defined as serving the interests of the American market, would mitigate against the development of a Canadian industrial strategy which would diminish Canada's technological gap. For Innis, therefore, the Canadian reliance on foreign investment would leave Canada forever vulnerable, particularly to the whims of American capital. This nationalist school of thought sends a cautionary message; while Canada may be attractive to foreign investors now, this may not

always be the case. A country heavily dependent on foreign investment is in a vulnerable position. As we shall see, while some were prepared to acknowledge Canadian vulnerability in the creation of FIRA, few questioned that Canada would continue to be attractive to foreign investors.

Mackintosh's expectation of the distribution of costs and benefits from foreign direct investment is widely divergent from that suggested by Innis. Somewhat akin to the later Rostowian approach to the analysis of economic development, Mackintosh argued that Canada would develop through a series of economic stages leading it to economic maturity. Such maturity would be evident "where economic expansion was in large degree self-sustaining and based on industrial rather than staples production" (Williams, 1983:132). Mackintosh identified the protective tariff as necessary to industrial development, acting to shield the era of industrial immaturity while fostering industrial growth.

For Mackintosh, industrial immaturity is characterized by continued dependence on staples as the focal point of economic production. Foreign investment, particularly the establishment of manufacturing branch plants, during this period is pivotal to economic growth, acting as one of the "life-blood[s] of the

pioneer economy" (Mackintosh, 1936:460). Foreign investment not only provides the possibility of industrial expansion for the developing economy, it creates its own demands by virtue of the necessity of its repayment. "As long as the capital imports are maintained a prosperity, real or fictitious, is apparent. But investment continues only in hope of ultimate gain" (Mackintosh, 1936:460). This necessity of repayment acts as a powerful stimulus to productive industrial activity, fuelling a cycle which pushes the economically immature country on to higher stages of economic productivity, and economic development. For Mackintosh, the process by which these "higher stages" are reached is never clarified; any form of economic activity generated by a reliance on foreign investment appears to be beneficial. The question of whether or not high concentrations of foreign investment would leave the Canadian economy vulnerable was placed on a back-burner; far more important was the observation that Canada needed foreign investment to develop economically. The belief that, whatever the cost, Canada needed foreign investment became clearly evident in the debates surrounding the creation of FIRA.

The combination of tariffs to protect industries in their infancy, together with an open investment climate,

has characterized Canadian economic development through much of its history, and reveals the extent to which a continentalist orientation to economic policy has prevailed in Canadian policy making. With the Canada-U.S. free trade agreement, continentalists deemed that Canada had achieved economic maturity, a point often echoed in the political debates which emphasized the competitiveness of Canadian industry. As Calvet and Crener, in their analysis of the Foreign Investment Review Agency, have contended;

[t]he openness of the Canadian economy to foreign investment, whether direct or portfolio, was the result of a long-lasting governmental policy which saw free trade as having detrimental effects on the infant Canadian industry. In contrast, the inflow of capital and labour was considered beneficial for the economic development of the country and was thus allowed unconditional entry (1979:416).

As Glen Williams has pointed out, it was not until the 1970s that the Innisian perspective began to contend seriously in policy formulation in Canada, as the economic crisis and the recessions of the era deepened. Until the late 1960s, in fact, "[s]ecure in the bosom of economic prosperity and its defence of the dominant economic order, the continentalist school faced little real challenge to its position as the official purveyor

of economic orthodoxy to Canada's state and business elites" (1983:149). A review of the changing pattern of foreign investment is helpful at this point for it leads us to question the assumptions of both the nationalist and the continentalist schools, and of the manner in which these have been translated through the Canadian state. In particular, we must examine some assumptions already evident; how attractive does Canada remain as a site for investment in a rapidly changing investment climate, and to what extent current investment takes place along a branch plant model. Policy based upon assumptions which are no longer valid is certainly limited at best.

CHANGING PATTERNS OF FOREIGN DIRECT INVESTMENT

Canada exists in a world in which not only the United States acts as a supplier of foreign capital. Although it is applicable to concentrate on the relationship between Canada and American capital in order to define the Canadian experience with foreign direct investment, such a discussion needs reference to the more general pattern of international capital flows -- particularly, as we have argued, in a period marked by considerable change in the motivations for, and manner of, foreign investment. In fact, the changing nature of those flows is part of the reason for the

Canadian state's failure to appreciate that Canada's position in the international political economy was changing, and that the changing role of the United States was at the centre of this re-evaluation.

The post-1960 period needs to be carefully examined; it is, after all, the period during which the impact and merit of foreign investment were seriously debated in Canada, resulting in the creation of the Foreign Investment Review Agency. It is also the period during which the Agency operated. Trends in foreign investment activity have been grouped into three distinct periods by organizations such as the OECD and the UNCTC: 1960-1973, 1974-1979, and 1980-1983 and beyond [3], and each of these will be considered in turn. Each period is so identified because it marks an important change in foreign investment trends. The 1960-1973 period was marked by a large increase in the flows of foreign investment internationally. This increase in global flows of investment had their impact upon the Canadian economy; witness for example the 30 percent increase in U.S. foreign investment to Canada between 1960 and 1967. These flows were motivated predominantly by the desire of firms to secure national or regional markets (branch plant investment), or to gain access to needed resources. This world-wide

increase in (particularly American) investment flows created circumstances under which individuals in many countries began to ask about the benefits and costs of foreign investment; we see here, as discussed in Chapter Two, the growth of regulatory mechanisms and nationalizations to deal with the perceived threat of multinational investment. Canada, of course, was not immune to these trends.

1974-1979 marked the slow-down of international foreign investment flows, and the deepening of the economic crisis of the international system. The economic crisis created the conditions under which multinationals began to concentrate on the development of new investment strategies, but also led states to continue to adopt measures to regulate or restrict the flow of investment. The effect of these parallel responses was that state managers were often reacting to the increase in investment of the 1960s at a time when both the pattern and extent of foreign investment had itself begun to change. The deepening of the economic crisis, with the attendant sluggishness of the world economy, brought about more competition for direct investment, and began to challenge the Canadian attractiveness to potential investors.

The period beyond 1980 witnessed the changing

position of the United States in the international political economy, its shift in location from a creditor to a debtor nation. At the same time, Canadian firms began to emerge as important foreign investors in their own right, joining a growing number of multinational corporations from the advanced and developing countries. Because of the deepening crisis, however, the 1980s also witnessed the entrenchment of new investment strategies, and the increasing competition between countries for foreign investment. As well, the 1980s have seen the change in focus of investment from a process conferring capital and productive capacity to one whose primary importance may well be the bringing of technology.

1960-1973

As the OECD has reported, the period ranging from the early sixties to the mid-seventies witnessed a rapid increase of international direct investment both in absolute terms and relative to the growth of other economic aggregates such as visible trade, domestic investment and GNP (OECD, 1981:6). As it had been throughout the latter part of the 1950s, international investment in the early 1960s was oriented towards developing sources of primary products and oil, many found in the developing countries. As a politically

secure location for investment, Canada was also at the forefront attracting these new investments. As Table 3.2, cited earlier, reflects, foreign ownership and control of these raw materials industries grew and was consolidated during the 1960s in Canada. This process reflected the U.S. perception (both state and industry) of Canada as a supplier of resources to the U.S. market, and reinforced the perception among Canadian state managers of Canada as a fundamentally resource-based economy. Later, direct investment in manufacturing began to assert overall dominance in direct investment flows among developed economies, although in Canada, half of the annual increase in the growth of the stock of foreign investment [which by 1973 stood at over \$(U.S.)33 billion; see Table 3.11] was accounted for not by actual capital inflows but by the reinvestment of retained earnings. Nationalists could point to this as evidence that Canada "had enough" capital.

Over the 1960 to 1973 period, the average annual growth rate of outward international direct investment flows from OECD countries neared 12 per cent a year, 50 percent greater than growth in average GNP during the same period, and roughly equalling the growth of international trade. Most of that investment was

directed toward other developed countries, with developing countries only accounting for between 25 and 30 percent of total flows of foreign direct investment throughout that period [4]. Existing multinational corporations expanded the size and the geographical range of their international investments, while national firms increasingly chose to multinationalize as well. The value of intra-firm trade began to increase substantially (reflective of new internationalization strategies), so that by the mid-1970s, imports by United States-based multinationals from their majority-owned foreign affiliates were close to 30 percent of total United States imports. In terms of total international trade (excluding the centrally-planned economies), intra-firm trade represented 22 percent of trade in 1966, and 25 percent in 1970 (OECD, 1981:7).

The United States, and to a lesser extent, the United Kingdom, were the major exporters of direct foreign investment in the period to 1973. While British firms tended to be engaged in primary production (usually in former colonies, such as Canada, with which they had established close economic ties as a result of previous portfolio investments), American firms were increasingly concentrated in sectors and industries which were characterized by intensive research and

development activities (including technologically sophisticated resource extractive industries). Not until the early 1970s did Germany and Japan begin to emerge as important sources of direct investment, helped by the appreciation of their currencies relative to the United States dollar.

Of great relevance to the Canadian foreign investment picture was the fact that United States investment was increasingly concentrated in Western Europe. After the Korean War, direct investment in primary sectors (particularly mining) began to grow less rapidly. In addition, as already suggested above, the establishment of the European Economic Community created incentives for investment within the Western Europe. A United States Senate investigation concluded that between 1966 and 1970, U.S. based multinationals had increased their share of manufacturing employment in six of the seven major hosts for American multinationals [5]. The only country in which there was a decrease in the proportion of manufacturing workers employed by U.S. multinationals was Canada, although this decrease was not accompanied by a lessening of U.S. ownership or control of manufacturing activities in Canada. The Senate Committee concluded that the drop in relative manufacturing employment by U.S. multinationals

operating in Canada "reflects the multinationals' shift of focus of their dynamic expansion away from Canada and toward the other areas, chiefly Western Europe" (cited in Laxer and Laxer, 1977:41). Reports of the Corporations and Labour Unions Returns Act (CALURA) support this finding, revealing that investments in manufacturing in Canada in this period (particularly after 1970) decreased, although figures on ownership and control did not. U.S. operations in Canada became increasingly concentrated in capital-intensive production, such as automobile production and oil extraction and refining. In 1971, for example, assets of foreign controlled manufacturing corporations grew at less than half the rate in 1970, and capital expenditures in manufacturing on the part of foreign firms declined 7% over their 1970 level, emphasizing a trend which was already becoming apparent (CALURA, 1971 Report:15). In contrast, investments in mining, petroleum, and service industries increased during the same period.

On the whole, though, through the 1960s and into the early 1970s, Canada remained a favoured location for investment (see Tables 3.1, 3.2, and 3.9, which reveal the increase in stock of direct foreign investment in Canada). Particularly in the early years of this

period, much foreign investment was still aimed at securing a national market or an unthreatened resource base. As a high-wage, western economy, Canada was an attractive choice for (particularly) U.S. investors, who could easily penetrate the market with their products. This is also the period, as we discussed in Chapter Two, when regulatory initiatives and nationalizations began to play a role in the investment calculations of MNCs. In Canada, where nationalizations (resource or otherwise) were not taking place, and rights of national treatment were largely respected, MNCs could find security in their resource investments -- and they did.

1974-1979

The latter half of the 1970s began to exhibit some rather dramatic differences compared to the investment patterns of the previous fifteen years, some the result of the worldwide economic recession. As well though, the different investment patterns were also reflective of changing technologies and multinational strategies. It is important to underline, before we detail these changes, that many of these were underway in the 1960 to 1973 period. However, it is only in the latter half of the 1970s that the aggregate effect of the changes began to be felt -- in Canada as elsewhere.

The most important consistent element of the 1974-1979 period was found in the weakening of most market economies of the developed world. [Canada, for example, had an average annual increase in consumer prices of 3.3% in the decade 1962 - 1972, rising to 10.8% by 1975, unemployment was increasing beyond the 8% mark for the period (from 5.3% in 1974 to 8.3% in 1978), and by the mid-1970s, Canada's rate of productivity growth was declining in absolute terms, as it was in most other advanced industrial countries]. With stagflation characteristic of most OECD economies, the annual growth in direct foreign investment decelerated quite sharply (OECD, 1981:12). Economic health was not helped by the oil crises which marked the middle of the 1970s. Direct foreign investment remained more buoyant than domestic investment, however, suggesting that multinational enterprises, as theory would indicate, were better able to adjust to new and largely unfavourable economic circumstances.

While the United States remained in this period the most important source of global direct investment, its share of the total of such investment fell noticeably. As a percentage of outward direct investment of 13 OECD countries, the share of the United States decreased from 60% in the 1961 to 1967 to approximately 30% from 1974

to 1979. With the United States as Canada's most significant foreign investor, this change in the relative global importance of the U.S. certainly had implications for the Canadian investment position. This relative decline was largely the result of the more rapid growth of direct investment from other countries, most significantly from West Germany, Japan and France. Canada also became a net exporter of capital during this period, beginning in 1977 and leading to a strong trend in capital exports (Statistics Canada, 1986:13). Despite this, and the concomitant decreased share of international flows of direct investment, Canada continued to retain the largest stock of foreign direct investment in the world, the overwhelming majority of which was United States-owned (OECD, 1981:24).

Numerous suggestions have been advanced to explain the change in the Canadian position to international creditor, among these, the fact that the Foreign Investment Review Agency was discouraging inflows of new investment. Other factors must be cited as well, however. In the June 23, 1975 budget, the withholding tax on medium- and long-term corporate obligations was suspended in Canada. This concession indirectly encouraged firms operating in Canada to meet a larger part of their capital requirements through medium- and

long-term debt instruments, and thus increased the attractiveness of the Canadian bond market to foreign firms. New issues of Canadian corporate securities sold abroad amounted to \$448 million in 1974, but to over \$1 billion in 1975 and to \$3.4 billion in 1976. These figures are reflected in Table 3.8, which reveals an increase in the sale of Canadian bonds to all buyers from 1974. The tendency to purchase Canadian bonds reflected a trend on the part of subsidiaries operating in Canada away from corporate borrowing from parents and affiliates abroad, and toward borrowing on the open market abroad -- and explains in part why foreign investment figures in Canada declined for this period, while ownership and control figures do not. Whereas borrowing from parent or affiliate firms is treated as foreign direct investment, however, borrowing in the open market is treated as portfolio investment. Changes in the pattern of financing contributed in that period to a decline in the flow of foreign direct investment to Canada (Gratton and Cusseau, 1978:19; Byleveld, 1982:14).

Additionally, from the mid-1970s there began a significant Canadian repatriation of foreign owned firms or assets, falling under the category of "irregular" or "non-recurring" transactions -- purchases which again

certainly affected the net flow of foreign direct investment into the country. In 1974, the Canadian government purchased De Havilland Aircraft from its British owners, and in 1976 purchased Canadair from the Americans. Petro-Canada purchased Atlantic Richfield Canada and Pacific Petroleum, while the Canada Development Corporation purchased the Canadian oil and gas assets of Tenneco, Inc., a U.S. company operating in Canada. As well, the Saskatchewan state expropriated some of the potash mines in the province.

During this period as well, the United States became a significant recipient of foreign direct investment, attracting almost 31% of the net international investment flows in the years 1974-1979, against only 2.6% in the 1961-1967 period. Given the near balance in capital flows between Europe and the United States, this increase in the share of the United States as host to foreign investment was not unanticipated. Most of the inflow to the United States (over two-thirds) originated with European countries, although with Canadian firms also growing to account for a significant share of this new direct investment to the U.S. The share of European countries as host to foreign investment flows had not changed significantly between the earlier and latter periods, despite the change in

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the status of the United States, although the average rate of growth of direct investment coming to Europe had declined as it had for the aggregate of all international direct investment flows.

Newly industrializing countries, among these, South Korea, Taiwan, Singapore and Brazil, began to attract significant international investment. The competitive advantage of the NICs in wage rates, and the growing experience of their labour force in industrial work has made these countries particularly attractive for the changing internationalization strategies of multinationals. We will recall from our discussion in Chapter Two that multinational corporations sought ways to increase their profitability during the economic stagnation in the western economies, and the pursuit of low-wage advantages was certainly an important means to this end. Largely as a result of the attractiveness of these countries, direct investment to developing countries sustained an increase in the 1974-1979 period in both current and real terms, 50 percent of the flow of investment coming from firms of the United States (OECD, 1981:15).

Direct investment continued to show remarkable stability in terms of sectoral distribution. Primary resource investments declined slightly in mining

activities, but remained stable or increased in petroleum industries (investment reflective of the uncertainty created by the oil shocks of the early and mid 1970s). Manufacturing investments increased relative to their total stock of investment abroad for the United States and Japan, while it decreased for Germany, replaced by increased investments in the service sector. The United States and the United Kingdom also increased slightly their share of service sector investments, while the Japanese share of service investments fell as Japanese firms began to engage in more manufacturing investment abroad.

While a general description of investment patterns in the 1974-1979 period may not appear to highlight significant changes, these become more apparent on second glance. The equalization of investment flows between Europe and the United States, for example, as well as increased Japanese investment in North America and Europe, can in part be attributed to a closing of the technological gap between the United States and its major economic competitors. As well, the increasing size and the securing of market position in home markets made it possible for many European and Japanese firms to contemplate investment abroad. This process of multinationalization would not have been possible in the

immediate post-war period, when home market reconstruction was the major preoccupation of any economic development plans. As Ozawa reminded us in Chapter Two, Japanese investment in other Asian countries was in part motivated by MITI's desire to exploit clean and high technologies at home, and to use foreign investment as a means to "houseclean" production in Japan. Shifting technological advantages have played a part however, for they appear to have lessened the enthusiasm of U.S. firms to undertake production in Europe rather than servicing European markets through exports (OECD, 1981:17). The increased competition among multinational corporations helped to create conditions under which firms began to seek ways to cooperate in order to control competitive economic circumstances. With a larger number of manufacturing multinationals, these cooperative arrangements have tended to be between firms of Europe, the United States and Japan (see, for example, Mytelka, 1987:60-68), rather than inclusive of Canadian firms. With most of these cooperative ventures at the technological frontier in knowledge-intensive industries, Canadian firms in general have not proven to be particularly attractive partners.

In addition, one feature of the changing investment

patterns appeared to be the increase in the number of small- and medium-sized firms participating in the foreign investment process. Beginning a trend which was to continue through the 1980s, smaller firms began to engage in direct investment abroad. Some of these firms responded to a growth in experience gained through exporting, behaving along the lines of Michalet's filiale-relais, engaging in direct investment as a next logical step to export activities. Canadian multinationals such as Northern Telecom and Moore Corporation became truly international during this period, with NorTel locating abroad to penetrate the U.S. market and yet continuing to internalize its firm-specific knowledge advantages, and Moore (the world's largest producer of business forms) breaking into the European market with the acquisition of the British-based Lamson Industries. For both firms, the small size of the Canadian market encouraged their move to multinationalization.

Since the early 1970s, but particularly through the second half of the decade, service industry investments have quickened. The most striking example of this phenomenon is the investment activities of banks, the 50 largest of which have increased their number of foreign affiliates by 60 percent between 1971 and 1976 (OECD,

1981:30). Banks have moved to follow their industrial clients, to keep their share of credit markets which have become worldwide with the growth of the euro-markets, and to strengthen their deposit base by gaining authorisation in a growing number of countries to attract deposits from host country residents (OECD, 1981:30). While foreign control of the Canadian financial industry is smaller than is foreign control of other Canadian industries due to protective sectoral governmental initiatives, 17 of the 35 largest insurance firms in Canada are foreign-controlled (including the U.S.' Allstate and Metropolitan Life, and the U.K.'s Lloyd's of London and Prudential). Even among financial industries, where Canadian banks are among the largest in the world, foreign-owned companies do play a role -- the Household Finance Corporation, or General Motors and Ford Motors Credit Companies, for example. Other service sectors which have shown remarkable growth in the latter part of the 1970s have been advertising, franchising, and international tourism, as well as specialized consulting (such as accounting services firms).

The growth in service sector investment has been most visible in Canada with the pressure brought upon the Canadian state to relax restrictions against foreign

banking activities, as well as upon the provinces to open insurance and securities markets to foreign investors. In large part, this pressure has come from Canadian financial firms fearing that their access to already penetrated foreign markets might be restricted by the failure of the Canadian state to provide reciprocal access to Canadian financial markets. Unlike some other Canadian firms, however, Canadian banks are not among the small- and medium-sized new international investors. As Moreau points out, Canadian banks make up five of the world's top fifty international lenders (Moreau, 1983:65).

Most importantly, perhaps, it is during this period that a change in multinational investment strategies began to be apparent. The latter half of the 1970s witnessed the decrease in numbers of wholly-owned subsidiaries, in part in response to the preference of developing states for joint venture investments with MNCs. The development of non-equity forms of investment; the provision of technology through patents, licenses or franchises (creating a relatively permanent link between the parent firm to the capital goods producers); the development of turnkey and buy-back arrangements; and the turn to a greater degree of international subcontracting, further revealed the extent

to which foreign firms chose to operate abroad through means other than traditional branch plant or subsidiary investment. In Canada, the number of licensing agreements (such as the one between Marsland and the Nippon Electric Coporations of Tokyo to produce optical charact r recognition (OCR) technology for the Canadian Post Office) and joint-ventures increased through the 1970s (Killing, 1978; Swedlove, 1978a,b). These new developments also signalled the importance of control, as opposed to ownership, in understanding multinational activities. While ownership may be completely absent in non-equity forms of investment, the MNC might continue to exercise control -- through the tight linking of the host country firm to channels it has organized and manages. As well, the MNC can exercise control through its ownership, or control, or mastery of the technology used. The OECD examination of investment patterns in this period importantly concluded that: "international direct investment through wholly-owned subsidiaries can no longer be thought of as the typical way of engaging in international business" (1981:33). These trends were underway when the Canadian state enacted legislation creating FIRA, but they were not clearly perceived by any one class, and thus not embodied in FIRA's mandate.

The new internationalization strategies were

evident in Canada in other ways as well. It is clear, for example, that U.S. subsidiary trade with their parents was on the increase. Between 1977 and 1982, sales to parent groups accounted for 73 percent of all foreign sales by U.S. subsidiaries in Canada (Rugman, 1988:3.11). Interestingly, sales to the parent group increased from a low of 45 percent as a percentage of foreign sales in 1964, while purchases from a parent group increased from 62 percent in 1964 to slightly over 70 percent in 1982 (Rugman, 1988:3.12). Increased sales to the parent group would seem to indicate that the degree of integration between parent and subsidiary has been increasing. Certainly, the growth of this intra-firm trade critically undermines the notion that U.S. subsidiaries in Canada are purely "branch plants", in place only to serve the Canadian market, and stands in contrast to what we will see was the perception of the Canadian state as it created FIRA.

It is in this period that we begin to assess the extent to which changing multinationalization strategies have implications for the Canadian location in the pattern of international investment flows. Most significantly, the motivations for new investment flows effectively situated Canada as a non-preferred investment location. The health (or lack thereof) of

the Canadian economy, as it was worldwide, did not serve as a magnet to new investment. Low-wage countries, particularly the NICs, began to attract investment in labour-intensive manufacturing industries. The OECD reported that NICs represented more than two thirds of the stock of international direct investment located in non-European, non-OPEC, non-tax haven developing countries in 1978 (OECD, 1981:18-9). Reclassification of foreign investor borrowing, and the effects of non-recurring transactions notwithstanding, the strong decrease in the expansion of foreign ownership in Canada in manufacturing industries (see Table 3.11) does point to a decrease in Canada's attractiveness as a location for manufacturing investment. Similar decreases in foreign ownership of resource industries, for which alternative investment locations cannot be so easily found, would appear to reflect the increased competition for investment among resource-endowed countries, sector-specific Canadian policies, and the collapse of the commodities market of the early 1980s.

The exception to this, of course, is to be found in the service sector. Many service industries retained the main features of branch-plant investment, that is, investment designed to gain access to a domestic market. Financial institutions, consulting firms, restaurants,

theatres, retail operations -- all engage in foreign investment in order to physically serve a local market. Ironically, precisely the high-wage nature of the Canadian market which would discourage the inflow or expansion of manufacturing investment was attractive to the expansion of service sector investments; a trend which continues to this day. Unquestioning conceptions of a Canadian economy always attractive to investors could no longer be sustained by the trends of this period, however.

1980-1983

It has been argued (UNCTC, 1985) that the main influence on foreign direct investment during the 1980s has been the unsettled international economy. The most serious recession since the 1930s has been followed by an uncertain and uneven economic recovery. The historically high interest rates in the early years of the decade, and the substantial exchange rate movements and fluctuations have not helped create an atmosphere of investment security. The rebound in economic activity for its part was concentrated in the United States and in a few countries in South and East Asia, and there continued to exist concern as to the long-term stability of a U.S. recovery based on expansive fiscal policies at

the cost of major and persistent trade imbalances.

The early 1980s, through the final years of the operation of the Foreign Investment Review Agency, saw the deepening of some of the trends begun in the 1974-1979 period. In particular, the deceleration of the rate of increase of foreign direct investment flows appeared to have continued from the earlier period, as did the greater buoyancy of international over domestic investment. Also consolidated was the reversal of the United States and Canada in their positions as capital importers and exporters; the United Nations Centre on Transnational Corporations called this reversal the "major recent change in the measures of the relative importance of foreign direct investment" (UNCTC, 1985:20). Comparative distributions of outward and inward direct investment flows among OECD countries illustrate this point most effectively, as seen in Tables 3.4 to 3.7.

**Table 3.4: Outward Direct Investment Flows:
Percentage Distributions among 13 countries**

	1961-1967	1968-1973	1974-1979
Australia	0.7	1.4	1.6
Belgium-Luxembourg	0.3	1.4	2.5
Canada	2.3	4.5	6.2
France	6.9	5.2	7.8
Germany	7.2	12.5	17.0
Italy	3.6	3.3	2.0
Japan	2.4	6.7	13.0
Netherlands	4.4	6.8	9.6
Norway	0.0	0.3	0.9
Spain	0.0	0.3	0.6
Sweden	2.0	2.4	3.7
United Kingdom	8.7	9.1	9.2
United States	61.1	45.8	29.3

Source: OECD (1981), p. 40

**Table 3.5: Outward Direct Investment Flows:
Net Percentage Distributions on Global Basis**

	1975-1979	1980-1983
Australia	0.6	1.8
Austria	0.3	0.8
Belgium-Luxembourg	2.3	0.4
Canada	6.4	13.4
Denmark	0.6	0.8
Finland	0.3	0.9
France	8.1	14.7
Germany	12.5	15.5
Italy	1.8	6.2
Japan	19.2	34.5
Netherlands	8.4	8.9
New Zealand	0.1	0.5
Norway	0.6	1.3
Portugal	0.6	1.3
Spain	0.5	1.6
Sweden	2.6	4.1
United Kingdom	8.7	14.6
United States	27.0	-20.0

Source: OECD (1987), p. 12

Table 3.6: Inward Direct Investment Flows:
Percentage distribution among 13 countries

	1961-1967	1968-1973	1974-1978
Australia	15.6	12.9	9.5
Belgium-Luxembourg	4.5	6.1	9.4
Canada	16.2	12.1	3.2
France	8.2	8.2	15.2
Germany	21.3	16.4	14.7
Italy	11.5	8.3	5.0
Japan	2.0	1.7	1.2
Netherlands	4.7	8.5	6.0
Norway	0.8	1.4	4.1
Spain	2.7	3.7	3.7
Sweden	2.4	1.7	0.5
United Kingdom	9.7	7.4	6.1
United States	2.6	11.4	26.7

Source: OECD (1981), p. 41

Table 3.7: Inward Direct Investment Flows:
Percentage Distributions

	1975-1979	1980-1983
Australia	2.9	4.9
Austria	1.0	0.9
Belgium-Luxembourg	7.6	4.8
Canada	2.4	-3.1
Denmark	1.6	0.3
Finland	0.3	0.0
France	14.0	7.9
Germany	8.1	4.8
Italy	4.1	3.1
Japan	2.0	2.5
Netherlands	5.4	4.0
New Zealand	0.6	0.4
Norway	3.2	1.3
Portugal	0.5	0.5
Spain	5.5	5.8
Sweden	0.5	0.6
United Kingdom	6.3	6.3
United States	28.9	52.6

Source: OECD (1987), p. 13

As these tables illustrate, the traditional distinctions between home and host countries have become at least blurred, and sometimes reversed. Canada is now an important home country [6], as are Japan, the Federal Republic of Germany, and France. In fact, the UNCTC speculated that, by 1987, Japan had become the largest single source of FDI outflows (UNCTC, 1988:2). The United States is now by far the most important host economy, attracting 52.6 percent of global foreign investment in the period between 1980 and 1983. Table 3.8 illustrates more starkly the processes underway in Canada. From this table it can be seen that while Canada has become an international creditor in terms of direct foreign investment, it has also become an attractive site for portfolio investment. In part this is the natural outcome of the high interest rate policy of the early 1980s; portfolio investments also increased dramatically in the United States, for example. Canada was also uniquely attractive for portfolio investment because of the comparatively secure interest rate remuneration of its bond market [7]. As pointed out earlier, as well, reliance on portfolio loans also reflected a changing tendency of firms operating in Canada toward the financing of their operations through borrowing on the open market. The United States,

however, clearly became the dominant host country for current investment flows. Despite this, in terms of investment stocks, the United States is still the dominant home country, while Canada remains a major host country.

Table 3.8: Canada's International Investment Position,
1970-1986 (Millions of \$)

Canadian Claims on Non-residents, Net Flows			
Year	Canadian Direct Investment Abroad [1]	Portfolio Securities Foreign Bonds	Foreign Stocks
1970	- 315	- 20	+ 90
1971	- 230	- 25	+ 221
1972	- 400	- 28	+ 272
1973	- 770	- 48	+ 118
1974	- 810	- 19	+ 67
1975	- 915	- 60	+ 42
1976	- 590	+ 57	+ 20
1977	- 740	- 21	+ 244
1978	-2,325	- 49	+ 75
1979	-2,550	+ 31	- 613
1980	-3,150	- 68	- 115
1981	-6,900	- 31	+ 8
1982	- 875	- 234	- 309
1983	-3,400	- 451	- 825
1984	-2,950	-1,359	- 784
1985	-5,100	- 750	- 563
1986	-4,521	- 182	-2,230
1987	-6,300	- 892	- 888
1988	-7,897	- 78	-1,006

Canadian Liabilities to Non-residents, Net Flows			
Year	Foreign Direct Investment in Canada [1]	Portfolio Securities Canadian Bonds	Canadian Stocks
1970	+ 905	+ 572	- 79
1971	+ 925	+ 233	- 125
1972	+ 620	+ 1,380	- 24
1973	+ 830	+ 577	+ 13
1974	+ 845	+ 1,866	- 139
1975	+ 725	+ 4,406	+ 87
1976	- 300	+ 8,636	- 56
1977	+ 475	+ 5,280	- 105
1978	+ 135	+ 5,267	- 271
1979	+ 750	+ 3,552	+ 523
1980	+ 800	+ 3,461	+1,490
1981	-4,400	+11,504	- 629
1982	-1,025	+11,964	- 308
1983	+ 300	+ 4,780	+ 912
1984	+1,700	+ 7,832	+ 152
1985	-2,950	+11,095	+1,551
1986	+1,550	+22,588	+1,912
1987	+4,750	+ 6,774	+6,649
1988	+4,881	+16,135	-2,338

Tables 3.9 through 3.12 paint a picture of inward and outward investment flows and stocks among selected OECD countries. These tables reveal that despite a considerably reduced inflow of investment into Canada, and a significant increase in outflow, the stock of foreign investment in Canada has continued to grow. This, of course, is due to the role of reinvested earnings in expanding investment, not included in the investment flows picture for Canada. The United States, in particular, relies heavily on reinvested earnings to expand investment; 60 percent of U.S. direct investment outflows in the 1975-1982 period were accounted for by reinvested earnings (OECD, 1987:28).

In the 1980-1983 period, the trend of increasing investment to developing countries levelled off, and then fell off dramatically by 1983. Latin American countries in particular, crippled by the growing debt crisis and persistent exchange rate fluctuations, were unsuccessful in attracting foreign investment through this period. Investment which might have been directed to Latin America in an earlier period continued to flow to South and East Asian, and non-Latin American NICs. Investment in African countries appeared to show a moderate increase in the early 1980s, but this was in large part due to larger investments in oil projects in

Nigeria, Cameroon, Egypt and Tunisia, which had the effect of skewing the figures on investment for the continent as a whole. Other African countries, however, saw a retrenchment of rather limited investment inflows, coinciding with severe economic difficulties (UNCTC, 1985:28). In fact, the 1980s witnessed the decline in Africa's share of worldwide inward DFI stocks by one half (UNCTC, 1988:25). As we would expect, the concentration of investment activity took place between European, U.S., and Japanese firms.

Table 3.9: Inward Direct Investment Flows:
1970-1983 (Millions US \$) [a]

	1970	1971	1972	1973	1974
Australia	572	746	770	132	268
Austria	97	80	78	107	171
Belgium-Lux	320	449	402	706	1,073
Canada	867	916	626	830	864
Denmark	105	127	164	213	357
Finland	18	24	31	16	41
France	626	528	687	1,125	1,847
Germany	421	912	1,507	1,585	1,970
Italy	603	524	624	629	604
Japan	94	210	169	-42	202
Netherlands	537	591	604	846	968
New Zealand	31	110	72	61	75
Norway	64	94	121	209	346
Portugal	27	52	76	96	103
Spain	222	202	276	390	358
Sweden	107	83	70	61	81
United Kingdom	438	650	260	955	1,411
United States	1,030	-175	380	1,890	3,695
	1975	1976	1977	1978	1979
Australia	541	-42	453	439	575
Austria	98	106	127	158	194
Belgium-Lux	922	793	1,116	1,295	1,006
Canada	713	-304	447	118	640
Denmark	267	64	76	57	634
Finland	68	58	47	34	27
France	1,457	1,051	1,765	2,445	2,722
Germany	849	1,329	1,210	1,329	733
Italy	631	94	1,136	510	362
Japan	167	196	224	236	524
Netherlands	976	354	357	667	1,287
New Zealand	141	35	105	28	90
Norway	215	373	766	423	401
Portugal	102	62	60	66	78
Spain	307	222	606	1,166	1,398
Sweden	78	4	81	69	111
United Kingdom	815	464	851	1,038	1,089
United States	1,414	2,697	2,142	5,314	7,921

Table 3.9 (continued)

	1980	1981	1982	1983
Australia	596	1,794	1,965	1,305
Austria	240	320	205	223
Belgium-Lux	1,453	1,352	1,390	1,271
Canada	684	-3,670	-730	162
Denmark	217	-40	135	64
Finland	28	17	-14	16
France	3,327	2,426	1,563	1,733
Germany	1,026	1,680	1,236	1,562
Italy	587	1,146	636	1,190
Japan	300	432	1,006	1,153
Netherlands	1,959	1,407	585	683
New Zealand	247	44	98	119
Norway	60	681	442	261
Portugal	158	176	145	144
Spain	1,493	1,710	1,788	1,627
Sweden	249	181	184	52
United Kingdom	4,305	723	552	1,656
United States	11,741	21,635	16,254	10,813

[a] Excludes reinvested earnings except for Austria, Denmark (1970-73 and 1982-83), Finland, Italy, Japan, Netherlands, Norway, Portugal, Spain and Sweden.

Source: OECD, 1987:60

Table 3.10: Outward Direct Investment Flows:
1970-1983 (Millions US \$) (a)

	1970	1971	1972	1973	1974
Australia	123	60	109	33	208
Austria	12	36	26	36	21
Belgium-Lux	157	181	148	172	372
Canada	302	228	404	770	828
Denmark	29	53	147	98	108
Finland	73	44	66	23	22
France	376	399	594	935	781
Germany	687	792	1,272	1,331	1,469
Italy	112	403	214	256	200
Japan	904	858	2,338	3,494	2,395
Netherlands	552	500	734	904	1,714
New Zealand	11	6	8	-	13
Norway	32	32	-	50	148
Portugal	10	3	13	43	36
Spain	43	25	56	52	85
Sweden	213	176	265	294	432
United Kingdom	537	848	679	1,913	1,696
United States	4,413	4,441	3,214	3,195	1,275
	1975	1976	1977	1978	1979
Australia	87	126	173	135	73
Austria	29	56	85	83	82
Belgium-Lux	150	293	354	362	1,119
Canada	900	598	696	2,038	2,178
Denmark	79	191	161	20	193
Finland	26	31	73	63	125
France	1,428	1,712	1,198	1,794	1,973
Germany	1,557	1,937	2,206	2,908	3,909
Italy	348	159	551	168	544
Japan	3,280	3,462	2,806	4,598	4,995
Netherlands	1,649	1,122	1,513	1,747	2,348
New Zealand	9	18	25	12	40
Norway	171	193	125	65	44
Portugal	6	5	2	6	-12
Spain	91	54	116	101	133
Sweden	437	366	738	418	606
United Kingdom	646	1,241	1,034	2,781	2,993
United States	6,196	4,253	5,497	4,713	6,258

Table 3.10 (continued)

	1980	1981	1982	1983
Australia	259	283	547	415
Austria	100	207	152	189
Belgium-Lux	62	30	-77	358
Canada	2,694	5,756	770	2,191
Denmark	324	151	80	160
Finland	131	142	234	261
France	3,138	4,615	3,063	1,699
Germany	3,772	3,356	3,098	2,996
Italy	754	1,404	1,025	2,126
Japan	4,693	8,931	7,703	8,145
Netherlands	3,268	874	1,935	1,542
New Zealand	47	39	14	368
Norway	254	183	305	354
Portugal	14	18	9	18
Spain	311	271	509	244
Sweden	626	854	916	1,060
United Kingdom	3,912	6,271	1,514	735
United States	2,205	-3,354	-11,131	-4,809

[a] Excludes reinvested earnings except for Austria, Denmark (1970-73 and 1982-83), Finland, Italy, Japan, Netherlands, Norway, Portugal, Spain and Sweden.

Source: OECD, 1987:58

**Table 3.11: Inward Stock of Foreign Direct Investment:
1970-1983 (Millions US \$)**

	1970	1971	1972	1973	1974
Australia	5,887	6,605	7,696	9,026	9,586
Austria	784	1,025	1,098	1,350	1,710
Canada	26,130	27,941	29,781	33,012	36,708
Denmark	920	1,234	1,505	1,858	2,458
Finland	117	143	173	204	239
Germany	-	-	-	-	-
Japan	-	-	1,645	1,602	1,867
Netherlands	-	-	-	7,508	9,573
Portugal	-	-	-	-	313
United Kingdom	11,439	13,678	13,637	17,346	22,104
United States	13,270	13,914	14,868	20,556	25,144
	1975	1976	1977	1978	1979
Australia	9,330	9,229	9,059	10,119	11,194
Austria	1,810	1,992	2,379	2,895	3,266
Canada	36,786	39,943	39,915	40,683	46,451
Denmark	2,458	2,686	2,876	3,350	4,172
Finland	292	397	427	480	533
Germany	-	26,891	29,600	36,622	40,581
Japan	2,084	2,208	2,229	2,841	3,422
Netherlands	10,027	11,868	13,579	16,529	19,806
Portugal	303	303	283	294	329
United Kingdom	22,512	21,609	27,244	33,982	46,777
United States	27,662	30,770	34,595	42,471	52,260
	1980	1981	1982	1983	
Australia	12,663	15,415	16,313	15,813	
Austria	3,165	2,896	3,164	3,432	
Canada	51,592	56,097	56,287	59,924	
Denmark	4,193	3,370	3,507	3,571	
Finland	540	501	416	396	
Germany	36,630	33,147	31,963	32,903	
Japan	3,270	3,915	3,998	4,364	
Netherlands	19,943	18,991	18,469	18,847	
Portugal	424	474	390	292	
United Kingdom	60,009	54,333	48,682	48,795	
United States	93,046	107,590	123,590	135,313	

Source: OECD, 1987:63

Table 3.12: Outward Stock of Foreign Direct Investment by
Country of Origin 1970-1983 (Millions US \$)

	1970	1971	1972	1973	1974
Australia	596	649	802	983	1,180
Austria	-	-	-	-	339
Belgium-Lux	2,223	2,404	2,552	2,724	3,096
Canada	6,119	6,524	6,745	7,868	9,292
Denmark	217	373	588	735	923
Finland	131	174	238	274	316
France	6,909	7,306	7,899	8,833	9,615
Germany	-	-	-	-	-
Italy	-	2,319	3,345	3,190	3,519
Japan	-	-	2,574	4,546	17,227
Netherlands	-	-	-	15,595	18,905
Sweden	2,194	2,370	2,635	2,929	3,361
United Kingdom	21,348	23,446	25,305	26,860	30,494
United States	75,480	82,760	89,878	101,313	110,078
	1975	1976	1977	1978	1979
Australia	1,169	1,249	1,343	1,615	1,706
Austria	303	-	-	-	547
Belgium-Lux	3,246	3,539	3,893	4,255	5,374
Canada	10,356	11,386	12,344	13,847	17,145
Denmark	914	1,160	1,355	1,534	1,776
Finland	318	356	397	471	626
France	11,193	12,842	13,841	15,729	17,712
Germany	-	18,416	22,228	28,831	35,320
Italy	3,299	3,362	4,137	4,767	5,852
Japan	8,322	10,313	11,958	14,329	17,227
Netherlands	19,092	20,442	24,525	30,176	36,890
Sweden	3,798	4,164	4,902	5,320	5,926
United Kingdom	30,421	32,897	37,244	50,536	67,481
United States	124,050	136,809	145,990	162,727	187,858

Table 3.12 (continued)

	1980	1981	1982	1983
Australia	2,225	2,459	2,858	2,937
Austria	529	636	677	794
Belgium-Lux	5,436	5,466	5,389	5,747
Canada	21,598	27,436	27,546	28,795
Denmark	2,065	1,991	2,072	2,232
Finland	731	786	869	1,067
France	20,810	25,392	28,236	29,935
Germany	37,955	39,218	39,851	42,201
Italy	6,972	7,378	8,116	8,501
Japan	19,612	24,506	28,969	32,178
Netherlands	39,930	38,806	37,986	38,900
Sweden	6,552	7,406	8,322	9,382
United Kingdom	77,869	83,736	86,677	87,106
United States	215,375	228,348	221,512	226,117

Source: OECD, 1987:64

As in the 1974-1979 period, foreign investments were increasingly undertaken by small- and mid-sized firms. By 1981, for example, these smaller firms (with less than 500 employees) accounted for 38% of Canadian foreign investments (OECD, 1987:22). In addition to trends mentioned earlier, continued poor economic performance into the early 1980s of firm home countries encouraged some companies to seek greener pastures in international investments. As well, the diffusion of new technologies allowed smaller firms to compete in sectors or industries where size was not a prerequisite to entry. In this respect, the continuing decline of primary resource investment, and the increase of manufacturing and service sector investments, would seem to be aggregate trends pointing to the likely success of smaller firms. Countering this trend to smaller firm size, however, it is important to point out that increased costs and risks evolving out of a high-technology focus to production may favour larger firms, better suited to making necessary adjustments and spreading risks (OECD, 1987:23).

The 1980s have also seen the increasing importance of firm acquisition or firm expansion as forms of foreign investment, rather than the establishment of new investments. To some extent, this is a function of the

maturity and experience of existing investments; local knowledge makes the task of identifying potential acquisitions or of expansion easier. It is also a function of R & D costs outstripping amortization possibilities because of the number of competitors in the market, which leads to takeovers and mergers (Mytelka and Delapierre, 1988). The uncertain economic climate of the 1970s and early 1980s has also made these forms of investment attractive for firms intent upon avoiding all risks possible. This is consistent with the expanding pattern of non-branch plant forms of international investment, which continued throughout the early 1980s, and which were attractive for risk avoidance reasons as well.

Perhaps most importantly, however, we must reflect upon that aspect of foreign investment which is not so easily mirrored in foreign investment figures. As we discussed earlier, the development of non-equity forms of investment played an ever greater role during this period. Buy-back arrangements, international subcontracting, the provision of technology through patents, licences or franchises, as well as the growth of strategic partnerships between firms (involving knowledge production and sharing agreements) have signalled a change in the nature of foreign direct

investment away from capital flows. Strategic partnerships, at the leading edge of new technological developments, do not necessarily involve equity at all, and yet surely effect the transfers of technology which states have accepted as one of the benefits of foreign investment. These new forms of investment, when the focus of the Canadian state in the creation of FIRA was primarily on capital as reflective of investment, suggest that such an Agency was far too limited in its mandate.

Trends in Canada also reflected the trends mentioned earlier in terms of sectoral investment patterns. Service sector investments began to assume more of the stock of foreign investment in the country, and the United States, as elsewhere, was responsible for an increasingly smaller (though still by far the largest) percentage of the total stock of foreign investment. These trends are illustrated in Table 3.13.

Table 3.13: Stock of Foreign Direct Investment in Canada:
Selected Year ends, 1966-1984

All non-residents

	1966	1969	1972	1975	1978	1981	1984
Manufacture[a]	41.5	41.1	40.4	40.7	42.0	38.9	39.5
Petroleum/ mining[b]	38.3	37.5	36.3	34.7	32.2	34.4	31.7
Services/ other[c]	20.2	21.4	23.3	24.6	25.8	26.7	28.8

U.S. residents

	1966	1969	1972	1975	1978	1981	1984
Manufacture[a]	43.5	43.6	42.8	42.9	45.9	32.5	43.8
Petroleum/ mining[b]	39.6	38.7	37.8	35.6	31.4	33.7	31.3
Services/ other[c]	16.9	17.7	19.4	21.5	22.6	23.8	24.9

U.S. % of total DFI	81.2	81.6	80.5	80.4	79.5	78.4	76.3
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Source: Calculated from statistics found in Statistics Canada (1981). Canada's International Investment Position for 1977 Ottawa: Supply and Services Canada, pp. 82-85, and Statistics Canada (1986). Canada's International Investment Position 1981 to 1986 Ottawa: Supply and Services Canada, pp. 54-57.

[a] Manufacturing includes the following industry classifications: vegetable products, animal products, textiles, wood and paper products, iron and products, non-ferrous metals, non-metallic minerals, chemicals and allied products, other manufacturing.

[b] Includes petroleum and natural gas, mining and smelting.

[c] Includes utilities, merchandising, financial services, and other enterprises.

Foreign investment trends over the last twenty five years provide concrete illustration of the extent to which multinational strategies have been changing. Where market penetration and security of market access were once the keys to the firm's motivation to invest abroad, these realities are no longer the sole considerations. Cheap labour, and less costly factor assets in general (from energy sources to lax anti-pollution legislation) began to play a role in determining the location preferences of firms, particularly as they adopted internationalization strategies based on the fragmentation of the production process. The desire to internalize knowledge assets also encouraged firm movement, while the desire to reduce some risks and costs have contributed to the creation of joint ventures and partnerships between firms, or with governments. Partnerships between firms may not involve the transfer of equity, and yet they are certainly part of a foreign investment process. Furthermore, there appear to be different processes at work governing manufacturing, resource and service sector investments, with the latter most likely to be taking place along branch plant (domestic market oriented) lines. The days of the wholly-owned subsidiary producing for the host country market no

longer characterized multinational activity, however, at least not in the manufacturing sector.

These changing aspects of multinational investment, and their reflection in the aggregate picture of international investment patterns, did not occur simply because multinational firms concluded that these were ways to "build the better mousetrap". Rather, the firms were responding to the challenges posed by the economic crisis as it deepened during the 1970s, as we saw in Chapter Two. Their ability to adapt lends credence to the OECD conclusion that multinational investment is less susceptible to international or national economic upheavals than domestic investment. As these economic upheavals challenged multinationals, firms have altered their investment strategies, and created new international patterns of foreign direct investment.

The capacity of the firm to adapt has posed particular problems for Canadian policy formulation, however. Where once state managers could assume that U.S. firms would continue to invest hugely in Canada, this was no longer an undisputed question. The United States itself became the magnet for international investment, and far more direct investment has been flowing out of Canada to the U.S. than was the case in reverse. Furthermore, analysts have suggested that

those manufacturing industries in Canada in which foreign investment has penetrated most deeply -- that is, those manufacturing industries in which Canada has proven to be most attractive -- are precisely those industries in which multinational firms are least likely to invest: cars, petrochemicals, and pharmaceuticals (Cook, 1984:1B1). These industries are now mature, and not on the forefront of dynamic new investment projects, unlike industries such as electronics or computers. As a small economy adjacent to a far more powerful market, hindered by high production costs, a well known deficit in research and development programs, and lagging behind in technological trade, Canada does not present itself as the obvious choice for setting up an advanced electronics plant.

The assumptions of branch plant investment, and national attractiveness, held by the state managers in the creation of FIRA, were severely challenged by an examination of the international pattern of foreign direct investment. Screening for the transfer of capital and the establishment of subsidiary operations is limiting if the most dynamic forms of investment did not involve the transfer of equity or the creation of new productive operations. National attractiveness was compromised in a climate of worldwide competition for

investment in all three of manufacturing, resource and service industries. Perceptions of Canada as a market to service the United States (producer of raw materials, consumer of manufactured goods) are subject to change in the face of the growing influence of Canadian multinational corporations. Chapter Three has highlighted an overview of the manner in which Canadian state manager assumptions were challenged by the changing pattern of foreign investment. Chapter Four discusses more precisely the manner in which these assumptions about Canada's location in the international political economy came to be held despite the evidence of this discussion about changing forms of international investment.

ENDNOTES

- [1] See Mira Wilkins' studies (1970, 1974) for an excellent review of the reasons and the circumstances which led American firms to choose direct investment as their preferred form of overseas investment.
- [2] For example, the Science Council of Canada is often characterized as representing the tenets of the "nationalist" school, whereas the Economic Council of Canada is the standard bearer for the continentalist orthodoxy (See Williams, 1983:149).
- [3] Trends beyond 1983 remain largely speculative, in part due to the problems involved in collecting and comparing international data. Kinniburgh and Ribeiro (1986) point out that however difficult it may be to obtain data on foreign direct investment stocks and flows across countries, it is even harder to find data on other activities of multinational corporations. A large part of this difficulty stems from the fact that statistics on direct investment are primarily collected for reasons other than to examine the activities of international firms (such as recording capital inflows and outflows for balance-of-payments purposes).
- [4] The exception to this trend, a decrease to 5 percent of total direct investment flows in 1974, was the result of major divestments of the petroleum sector in the wave of nationalisations of oil-exporting countries (UNCTC, 1983:27).
- [5] The U.S. Senate Committee on Finance investigated U.S. multinational activities in Canada, the United Kingdom, Belgium-Luxembourg, France, West Germany, Mexico and Brazil.
- [6] The figures for the 1980-83 period are, however, exaggerated by the impact of the Canadianization provisions of the National Energy Program.
- [7] Interest returns on Canadian bonds are set and guaranteed at the time of purchase, while in other industrial countries rates are subject to yearly fluctuations. Bond issues are thus a more secure and conservative investment in Canada, while they will not likely pay higher interest than at issue,

they will not pay lower rates either. This feature has been particularly attractive to Japanese investors seeking to securely invest the returns of a persistent trade surplus (Personal interview, Investment Canada, 1987).

CHAPTER FOUR

CANADA AND FOREIGN DIRECT INVESTMENT: STATE ACTION AND THE SEARCH FOR KNOWLEDGE

We know now of the existence of two main approaches to economic thought in Canada, one of which was concerned with the consequences of a high level of foreign direct investment in the Canadian economy. We also know of the extent of foreign investment in the country since its earliest days. Given this, it is now necessary to ask why concerns about foreign investment only became clearly apparent in the late 1960s and early 1970s. What caused state managers to move from a largely open door investment policy? How and why did they begin to change their evaluation of the benefits of foreign investment? These questions define the task of this chapter.

In order to answer these questions, we will chart the changing view of foreign direct investment within Canadian policy making circles, both at a political and a bureaucratic level. This tracing of views will focus upon four key dimensions which play a role in the Canadian foreign investment debate. These dimensions include, first, the extent to which the Canadian economy is "capital poor" or suffering a capital shortage (usually presented in terms of balance of payments needs); second, the issue of the extraterritorial

application of host country laws to home country subsidiaries; third, whether Canada would continue to be attractive to foreign investors; and fourth, the consequences of foreign investment for Canadian development. The choice of these dimensions was determined by their importance as issues in the series of royal commissions, public policy statements, committee reports, and public testimony undertaken between 1955 and 1974 in order to resolve a growing public concern over foreign investment. They reflect the points of debate over the issue of foreign direct investment in Canada, and their introduction into the debate gives focus to our task of determining the source and manner of state manager learning.

In charting movement along these dimensions, we will rely upon two broad categories of explanatory variables, both of which derive from our theoretical framework as defined in Chapter One. The first category of explanation is to be found at the level of the international system. We will recall, for example, that the international norms governing the freedom of investment were beginning to show signs of fraying, and as such were politicizing the issue of foreign investment internationally. Even as early as 1950, the United Nations Economic Commission For Latin America

(ECLA) had begun to raise questions about the unfettered investment activities of multinational corporations and their impact on economic development. Within this international context, concerns were raised domestically about the pattern of foreign direct investment in Canada. Within this context as well, the policy actions of the United States government were particularly relevant, for they represented not only the views of Canada's largest foreign investor, but also the perspective of a system hegemon interested in maintaining liberal investment norms.

The second category of explanation is at least equally important. We will be focussing upon the role of various class actors in Canada -- particularly the growing new middle classes -- in interpreting the changes in the international economy, and in presenting these views to state managers. These class agents are the filter between the international economy and state managers. State managers are not driven to respond to concerns which have not been identified or given a domestic political focus. It is expected that charting the impact of both the international economy and class actors upon state managers will allow us to explain changing views along the dimensions we have previously identified.

FOREIGN INVESTMENT AND THE CANADIAN STATE: FROM GORDON
TO GRAY

The Gordon Report

The Gordon Royal Commission on Canada's Economic Prospects was charged to report on "the probable economic development of Canada and the problems to which such development appears likely to give rise" (Gordon Report, 1957:3). The Gordon Report marked the first official statement in Canada which pointed to foreign investment as a likely source of potential problems for the Canadian economy. Gordon's own convictions on the subject were known; as the chairman of the executive committee of the Canadian Institute of International Affairs, he had submitted a draft article for the International Journal on the problem of Canada's economic future and the growth of foreign control of the economy. That draft article, in fact, had provided the genesis for the creation of the Royal Commission (see McCall-Newman, 1982:27; Wolfe, 1978:16). What is of interest to us here is to identify the assumptions toward direct foreign investment present in the Final Report.

A Preliminary Report was presented to Cabinet in December, 1956, and became public the following month to considerable controversy (although the provisions

which caused the greatest controversy were not those related to foreign investment, but one paragraph which suggested that generous assistance should be provided to Maritimers "who might wish to move to other parts of Canada where there may be greater opportunities"). Seen by C.D. Howe as "some of the greatest rot he had ever heard" (Smith, 1973:44), the Report was taken as an implicit criticism on many fronts of Liberal government policy. By the time the Final Report was released a year later, its time had effectively passed (Smith, 1973:35-50). The Conservative Party had formed the new government, and Gordon himself was relegated to being put down as "that Toronto taxidermist" by Diefenbaker (Gwyn, 1985:65). The Final Report is the most useful here, however, for it provides a far more detailed analysis into the basis of recommendations present in the Preliminary Report.

The first comment on foreign investment which is made in the Final Report concerns the Canadian relationship with the United States, the primary source of direct foreign investment. The Report, in trying to forecast Canadian investment twenty five years into the future (1981-82), concluded that "the external capital that will still be required will be supplied by United States residents, we should imagine; and United States

ownership and control of a number of our largest and fastest-growing industries will be even greater than it is today..." (Gordon Report, 1957:12). These comments were re-emphasized further in the Report, with the Commission arguing that "there seems little reason to expect that the current trend towards greater United States control of some of our fastest growing industries is likely to be reversed unless there is a change in present corporate practices or government policies" (42). Moreover, the Commission writes that Canada:

"has always welcomed the investment of foreign capital", and that this welcome has been helped by a favourable "investment climate"; "a long tradition of freedom for the flow of capital and income across its borders"; "a long working history of orderly and responsible government"; "a hard-working people with a strong desire for material advancement, a skilled labour force, a well developed educational system, adequate transportation and other social-capital facilities, reasonably stable economic and social conditions and positive encouragement by all levels of government..." (1957:385).

What are we to conclude from these observations? Certainly there seems an implicit assumption that Canada's attractiveness to United States investors specifically and foreign investors more generally is unlikely to change. These conclusions do not address the possibility of other countries coming to represent a

more attractive location for investment. United States investors are not expected to limit their investments, or to divest them. Canada's attractiveness is not under question in the 1950s. This conclusion is hardly surprising; we will recall the extent of U.S. investment in Canada during this period, and the rapidity of its growth.

Among its many conclusions, the Gordon Commission suggests that the Canadian state adopt a far more interventionist stance with respect to foreign investment, and a more nationalist stance to support Canadian businessmen. The Report argues that Canada has gained considerably from the presence of foreign investment: "[t]he increase in ... investment in Canada, accompanied as it has been by new technology and managerial skills, has clearly resulted in a faster rate of economic growth than would otherwise have been possible" (1957:41). Nevertheless, the Report does outline areas of potential conflict between Canadian interests and those of foreign investors. These include: the search for markets for Canadian products and plans for the expansion of Canadian operations, intra-firm trade which might lead to pricing discriminatory to the Canadian subsidiary operation, sourcing restrictions, export market restrictions, and

an unprofitable "dry run" mentality in wage negotiations between a foreign parent and its Canadian worker (Gordon Report, 1957:390-1). The identification of these problems is consistent with a branch plant view of the structure of Canadian industry; foreign control might in effect truncate the range of activities which would normally be performed by a Canadian firm.

In this, the Gordon Commission was revolutionary. While moderate in its recommendations, the identification of potential conflicts between Canadian and foreign interests implied serious criticism of the pattern of Canadian economic development and expressed serious concern about the magnitude and effects of foreign investment in Canada. It clearly painted Canada as a branch plant economy, which in itself was not a new observation (C.D. Howe himself acknowledged without apology that Canada was characterized by branch plant manufacturing). What was new was that the Report identified negative consequences from such a pattern of development -- particularly the limited export markets and the restrictions to domestic sourcing. It recommended that the Canadian state take action to increase Canadian ownership of Canada's economic concerns, and to limit or ameliorate the areas of potential conflict between Canadian interests and those

of foreign investors. It did not question the benefits conferred upon the Canadian economy by foreign investment in the first place; while the Report was a nationalist critique, it was very much influenced by the concerns of continentalist thought. In fact, the Report argued that the Canadian state should seek more portfolio investment rather than direct investment; control was the only problem associated with a foreign presence. While the Gordon Report set the tone for a debate which was to go on for another fifteen years, it did not have any immediate impact, or, with the election of the Diefenbaker Conservative government in 1957, any official acceptance [1].

The Gordon Report gave the Canadian state the first glimpse of a new way of interpreting its position in the international political economy. Written at a time when the Canadian economy was experiencing massive postwar inflows of direct investment in both manufacturing and resource industries (see Table 3.2), Gordon raised the first early questions as to the consequences of this pattern of economic growth. The Report suggested that Canada, the dynamic industrial country of C.D. Howe, might in fact be losing out in its relationship with the world economy.

Despite the tremendous contributions
which foreign capital -- and the

management and technological skills and the access to markets that has come with it -- has made and will continue to make to the development of our country, we do not believe Canadians will cease to be concerned about this matter unless something is done to make Canadian voices more strongly and effectively heard in some vitally important sectors of our economy in which non-residents exercise a large measure of control.... [T]o do nothing would be to acquiesce in seeing an increasing measure of control of the Canadian economy pass into the hands of non-residents and to run the risk that at some time in the future a disregard for Canadian aspirations will create demands for action of an extreme nature (Gordon Report, 1957:399).

Wrapped into this picture of potential doom was an evaluation of why Canada was attractive to foreign, particularly U.S. investors -- an evaluation largely coincident with the pattern of foreign investment in the 1950s. Manufacturing and resources are identified as the two sectors of greatest penetration. The Gordon Report acknowledges that while profitable exploration has guided the investments of U.S. firms in Canadian resource industries, more important has been "the desire to develop and guarantee sources of supply of materials in which the United States ... needs are, or promise to be, greater than can be supplied from existing sources. In certain cases the United States Government has encouraged direct investment in Canada in connection

with its programme of stockpiling strategic metals" (Gordon Report, 1957:387).

Investment in manufacturing, on the other hand, is simply seen as the choice of an efficient means to supply the Canadian market. The tariff is held responsible for the extent of the penetration of the manufacturing sector (Gordon Report, 1957: 397). Canada is both the "hewer of wood and drawer of water" to the U.S. resource needs, and an affluent market, similar to the U.S., in which manufacturing profits can be easily made. Because the Gordon Report recognized the branch plant nature of the manufacturing investment in particular, it acknowledged that it would be difficult to alter the balance of ownership -- particularly since the expansion of existing investment "has been financed in large measure from retained profits and depreciation allowances" (Gordon Report, 1957:42). With this acknowledgement, the Commission implicitly stated that foreign investment was not repeatedly bringing in new capital, all the while arguing that "Canada has never been able to provide enough capital from its own resources to finance the growth and development of the country" (1957:380). Even five years later, with greater concern about the implications of foreign investment in Canada, Gordon continued to hold that

foreign investment was necessary for balance of payments reasons (1961:57-8).

The Gordon Report clearly painted a picture of Canada as a branch plant economy, and yet did not question Canada's attractiveness as a site for investment. Its view of Canada's location within the international economy (as a satellite of U.S. interests and needs) contrasted quite sharply with the picture of a continentalist path to development, where foreign investment, through the necessity of its own repayment, provided Canada the means to achieve full development. Foreign ownership, rather than being an engine for economic prosperity, is identified by the Gordon Commission as congruent with lack of Canadian control over its economy. This is not an admission of long term economic vulnerability as a result of foreign investment, or indeed, even a statement that Canada no longer required foreign capital. Rather, the Gordon Report only sounded a cautionary note about the potential consequences of foreign control.

The Gordon Report, as we have already implied, was largely ignored. It could hardly have been any other way. In many respects, the warnings about the potential consequences of foreign investment made little sense in a Report whose main thrust was to argue that Canadians

were rich, and in twenty five years likely to be richer, and that foreign investment was high and in twenty five years likely to be higher. Gordon himself was certainly concerned with the implications of foreign control; but the broad outlines of the Report read as praise to the continentalist solution. It is no wonder that C.D. Howe denounced the report; if his policies encouraging foreign investment had caused the extent of such investment to grow while the economy had also grown, what was the logic of suspending the "formula" for economic success?

We have argued that the state turns to domestic paths to knowledge at times when change seems to be breaking down the accepted norms of international exchange. The release of the Gordon Report did not coincide with the most intense of the Third World nationalizations which were to come through the 1960s (Kobrin, 1980), and by the time these did come about, the impact of the Report had passed. State managers learned that they did not need to alter their strategy. As we shall see, there was little domestic pressure for them to do so, and the international investment climate -- with Canada continuing to attract significant foreign investment in both manufacturing and natural resources (Table 3.2) -- only served to reinforce existing beliefs

In an open investment policy. Still, it is useful to assess whether there were any signs of broader public frustration with the problem of foreign direct investment, for these would have the potential to develop into the classes or fractions which might later emphasize the Report's assumptions to state managers. Which areas of domestic concern can be found, beyond Gordon's own agenda, which led the Gordon Commission to investigate the consequences of foreign investment on the Canadian economy? Three problems can here be identified. To begin, complaints had arisen that U.S. branch plants in certain sectors were operating with special advantages over their Canadian counterparts. In particular, this was the view of the oil industry, where the U.S. had implemented a program of tax concessions to encourage American firms to explore for oil and gas at home and abroad. Canadian tax laws, for their part, gave each new site of exploration (foreign or Canadian) a three year period of exemption from taxation, and provided generous depreciation and depletion allowances. Canadian firms criticised the "bonus" tax position in which U.S. firms found themselves (with concessions from two governments) as unfair to their interests (Mackintosh, 1959:66; Gordon Report, 1957:387-8).

The U.S. temptation to use Canada as a testing

ground for labour negotiations was of particular concern to labour in the automobile industry. Writing in this period, Mackintosh speaks of the "resentment which Canadians feel when their automobile industry becomes a testing ground for the vastly more important United States negotiation between the motor companies and the United Automobile Workers" (1959:66). The Gordon Commission suggested that when the Canadian branch of an international union was represented by its U.S. directors, and the Canadian subsidiary was represented by U.S. management, "suspicion may well arise that the negotiators are more interested in setting precedents for impending wage negotiations in the United States than they are with the immediate problems of the Canadian subsidiary and its employees" (1957:391). In fact, in 1956, the United Automobile Worker (UAW) established the principle that any Canadian contract package "should bear a strong resemblance to the American" (Crispo, 1967:199), a factor seen as limiting the degree of Canadian autonomy in its wage negotiations with the same management.

Finally, the simple fact that heavy patterns of U.S. investment and geographic proximity create an interdependence of policy was a source of frustration to some, including business interests involved in specific

projects and Canadian policy makers. These projects had the tendency to become involved in American sectional politics [2]. U.S. investments and the political interests behind these were played out by parochial interests in Congress, and resulted in delays and frustrations which angered Canadian interests involved in these projects.

Gordon himself was ideologically motivated, however, and domestic bases of support for his position should not be overstated. When in 1963, following the return of the Liberal party to power in Ottawa, Finance Minister Walter Gordon presented a budget based in part on the recommendations of his earlier report, his repudiation seemed complete. Within five days, in response to business and governmental outcry, Gordon had to withdraw the most contentious of the budget's proposals: a 30 percent "takeover tax" to be levied on the value of shares of Canadian firms sold to non-residents. Canadian business raised its severest criticisms around what it perceived as a nonsensical way of doing business. Whatever the costs of foreign investment to the Canadian economy (and these were still seen as largely negligible), they were not worth the risk of cutting Canada off from the capital it was perceived to so badly need.

The only exception to this rule was in the cultural industries. Walter Gordon had introduced a measure disallowing advertising in foreign-owned newspapers and periodicals as a tax deduction in his Budget. This measure was not new; it had also been introduced under the St. Laurent government in an effort to bolster the sagging fortunes of the Canadian magazine industry (see Appendix I). Gordon's proposal was accepted, although, because of strong U.S. pressure, Time and Reader's Digest magazines were exempted (Newman, 1968:224-6). Gordon himself recalled that the source for this proposal came from Canadian newspaper publishers, some of whom "were concerned that control of the press might be lost to Canadians" (1977:205). An identifiable group of Canadian publishers, interested in maintaining their livelihood, appeared to have given credibility for moves restricting foreign investment in this one specific sector.

The more general concerns which did exist in Canada were heated by the bilateral context of the 1960s. These years began the process of fundamental readjustment in the global economy; a shift focussed upon the weakening position of the United States within that economy. It is around this changing U.S. international position that concern for the Canadian

global location did develop -- and it is the fact of readjustment in the U.S. hegemonic position (and many would contend, the beginnings of hegemonic breakdown) which began to once again place international economic policy on the agenda of state managers. The growing competitiveness of manufactured exports from Western Europe and Japan challenged the United States' international trade position. More than exports, however, we will recall that both Europe and Japan were beginning to develop their own MNCs interested in investing abroad. U.S. firms now had competition for their international investment position. Furthermore, the growing U.S. involvement in the war in Vietnam placed burdens upon the U.S. state to finance that investment, and the consequences of its so doing fueled domestic inflation. Together, these trends placed pressure upon the U.S. balance of payments position, creating large increases in the current account deficit. As well, multinational firms began to define new strategies of investment; in particular, the trend toward the internationalization of production.

Signs of these pressures were evident as early as July 1963, when the Kennedy administration proposed to Congress the levying of an interest equalization tax, which would equalize the cost of domestic and foreign

borrowing in order to discourage further international borrowing in the United States (Bothwell et al., 1981:319-20). The Canadian state was able to secure an exemption from the tax measures but in return, pledged not to increase its reserve holdings of U.S. dollars. The conditions thus placed upon Canadian monetary policy were to prove limiting. For most of 1963 and 1964, the American bond market was virtually closed to Canadian borrowers. Had it not been for the unexpected and large purchases of Canadian wheat by the Soviet Union, the Canadian balance of payments position would have been precarious at best.

In 1965, the United States government released guidelines again targetted at resolving balance-of-payments difficulties. This time, the guidelines hoped to reduce the flow of U.S. direct foreign investment, and speed the repatriation of profits by American owned businesses operating abroad. The guidelines were interpreted to be largely voluntary, and the Canadian state chose to react to them with the publication of its own voluntary guidelines, the 1966 Winters "Guidelines of Good Corporate Citizenship". The Canadian reaction stands in sharp contrast to the Australian response, where the publication of the U.S. guidelines was met with the first measures to regulate

inward foreign direct investment (see Mytelka, 1986:150). In many respects, the United States was itself violating the terms of the international norms which it had been instrumental in maintaining. While the U.S. state expected other countries to support the rights of the investments of U.S. firms abroad, they themselves were attempting to disrupt those investments. As systemic hegemon, U.S. policy makers clearly believed that the "rules of the game" -- even its own rules -- were for others. In 1968 the U.S. guidelines were further strengthened to demand that American-owned firms repatriate 30 percent of their earnings. The Canadian state once again had to seek exemption from U.S. rules, as within days, "there was an unexpectedly large transfer of funds from American-owned firms back to the United States" (Bothwell, 1981:321). When in late 1968 there was severe speculative pressure placed upon the Canadian dollar, the Bank of Canada had to turn to Washington to seek an exemption from its earlier exemptions in order to allow Canadian foreign reserves to rise (and thus attempt to curb growing inflationary pressures).

The picture of Canada's "monetary mandarins" making repeated pilgrimages to Washington, hat in hand, in order to seek the authority to deal with Canada's own

monetary and fiscal problems, seemed to capture some of the consequences of a high degree of foreign investment. The Gordon Report had attempted to introduce concern about the potential effect which foreign investment was having upon the Canadian capacity to control its own economic development and to determine its own economic direct. While a coherent social force had yet failed to materialize critical of foreign investment, a general unease was building up around Canadian ties to the United States. This unease was crucial; without it, it is doubtful that the new middle class would have been able to influence state manager assumptions about foreign investment in Canada. Murray and LeDuc, for example, report on the enormous increase in positive responses to Gallup polls questioning whether there is "too much U.S. influence in the Canadian way of life": from less than 40 percent in 1961 to almost 55 percent in 1966 (1982:218). In the late 1960s, the Cabinet responded to some of these concerns, and undertook a comprehensive study of foreign investment. Walter Gordon was asked to return to the Cabinet as a Senior Minister without Portfolio, and in return for his acceptance, he appointed Mel Watkins to head a task force of university professors to investigate the effects of foreign investment, among other influences,

upon the structure of the Canadian economy. The task force included such scholars as foreign investment specialists Stephen Hymer, Abraham Rotstein, and A.E. Safarian.

The Watkins Report

The Watkins Task Force presented its Report, Foreign Ownership and the Structure of Canadian Industry, to the government on January 12, 1968. It presented a similar picture of foreign investment in Canada as had the Gordon Commission, arguing that the depletion of resources in the United States had inexorably "pulled Canada into the American orbit" (Watkins Report, 1968:16), limiting the Canadian capacity for independent decision makings and creating an "inferiority" in the Canadian firm, which as a branch plant was protected "from the stiff winds of international competition" (17-27). The Watkins Report did diverge widely from the Gordon submission in its focus on the extraterritorial application of foreign (predominantly American) laws as the "political" (versus the economic) manifestation of direct foreign investment. The issue had only received limited coverage in the Gordon Report, but in many respects seemed to formed the thrust of the Watkins Report. It

stressed that "[f]oreign control means the potential shift outside the country of the locus of some types of decision-making. The extent to which decision-making within the host country is eroded varies with circumstances, and basically depends on the power of the foreign firm and its government relative to the government of the host country" (1968:27). We see here one of the first lessons learned -- as a result of U.S. attempts to disrupt its foreign investments throughout the 1960s.

The issue of extraterritoriality points in detail to one of the larger problems of the Watkins Report. Mel Watkins' letter formally submitting the report to Walter Gordon includes the clause that the report "represents a consensus of our views" (1968). A consensus of views among economists subscribing to such radically different interpretations of the costs of foreign investment as Hymer, Watkins, and Rotstein (Rotstein, in fact, became one of the founders of the Committee for an Independent Canada), on the one hand, and Safarian on the other, must have been difficult to achieve, at best. Extraterritoriality is the one issue upon which both more radical and classical economists could find themselves in agreement. Unsurprisingly, therefore, the task force found that of the six major

issues facing Canada as a result of foreign investment, "[t]he most serious cost ... results from the tendency of the United States government to regard American-owned subsidiaries as subject to American law and policy with respect to American laws on freedom to export, United States anti-trust law and policy, and United States balance of payments policy" (Watkins Report, 1968:360). Within the context of the difficulties experienced by Canadian policy makers and firms when their range of actions was restricted under U.S. balance of payments provisions or the Trading with the Enemy Act, extraterritoriality took on particular relevance. Submissions made two years later by Abraham Rotstein and A.E. Safarian before the Standing Committee on External Affairs and National Defence reveal this same assessment of the core of agreement. Rotstein, for example, testified that,

The crux of the issue ... lies neither in the economic cost of exports which have been foregone, nor whether American anti-trust law has had "good" or "bad" effects on the Canadian industrial structure. (My own view is that they inhibit substantially a major program of rationalization of Canadian manufacturing which is urgently needed) [emphasis added]. The central issue is the intrusion of American jurisdiction in Canada through the agency of the American subsidiary. (Rotstein, 1970:9:57).

It is interesting to note that Rotstein's own observation of some of the structural consequences for the Canadian economy which have developed as a result of foreign direct investment are in his testimony given second string to the legal and political dimensions of extraterritoriality.

In his testimony before the same committee, Safarian also refers to his conclusions as a member of the Watkins task force. Unwilling to blame any perceived negative economic consequences of foreign investment upon the multinational firm (rather, he lays the blame at the feet of inappropriate Canadian industrial policies), Safarian suggests that governmental intervention in Canada's political affairs through the extraterritorial application of home country laws is unacceptable. In fact, he contends that there is substantial "danger to the future of national policy-making if the principle of unilateral extension of foreign law and policy to subsidiaries ... [is] not strenuously challenged" (1970:10:86).

The implications of a consensus report formulated by individuals representing both nationalist and continentalist views effectively were that the report would be a muted evaluation of the costs of foreign investment, certainly more muted than Watkins own

personal views. For the authors of the Watkins Report, the new realities brought by the multinational corporation were to be accepted as a new economic "fact of life" (1968:355), actors creating a new international economy of which Canada was a part. Foreign investment was described as rather inevitable, something which would naturally accrue to Canada, and the responsibility of the Canadian state lay in collecting information about it, and controlling the multinational firm if and when it followed the laws of its parent state over those of the host country (Canada). Critical of MNCs in its demand that more information be collected about their activities (the Watkins Report acknowledged that the state had little knowledge about the activities of multinationals, and on that basis, could not effectively formulate policy), the Report nevertheless continued to paint foreign investment as a relatively benign force. Canada needed foreign investment, would continue to attract it, and the state needed only to learn more about it in order to control it -- knowledge in itself being a form of control. The branch plant economy was an acceptable form of economic development, and state managers needed only to be better informed in order to control some of its excesses.

The Watkins task force was, however, the first to

recommend the creation of a special agency to coordinate Canadian policies dealing with multinational enterprises. Canadian policy had to "come to terms" with the multinational firm, and accept that foreign investors had penetrated the Canadian economy. The Report does not even address the issue of Canada's attractiveness as a location for investment; it has been, is, and will continue to be, we are told, and we must simply accept it (1970:355). It sums up this non-issue by stating that "[f]oreign ownership and control are presently pervasive in Canada and are likely to remain so" (Watkins Report, 1970:361). The branch plant economy is seen as another fait accompli, but its most negative consequences are associated with extraterritoriality, and not with the truncation of Canadian economic development.

The primary function of the agency recommended by the task force, then, would be to collect information about multinational activity in Canada, protect Canadian interests, and encourage Canadian participation in the country's economic growth. All three functions were seen as a way to address the concerns over extraterritoriality. The Watkins Report did recommend the establishment of a Canada Development Corporation, which would provide pools of capital permitting

Canadians to keep national firms under Canadian control. The Corporation was not to be a force in the repatriation of foreign assets, but only a means of assembling Canadian capital to permit a Canadian presence in the economy. This Corporation would act with a view to improving Canadian management skills, increasing local research and development, and expanding exports (Watkins Report, 1968:411-2) -- addressing only in passing some of the concerns of the branch plant economy.

For the Watkins Report, therefore, Canada was attractive to investors, was a branch plant economy complete with the attendant costs, had to accept that these trends would continue, but needed to stop the extraterritorial application of U.S. law. Interestingly enough, the question of Canada "needing" foreign investment doesn't appear; it is as though the pervasiveness of the investment process has made the issue moot. Finally, it is also interesting to note that the Watkins Report turns to the evaluation of policies in other countries -- France, the United Kingdom, and Japan -- to determine the nature of potential Canadian policy responses to the challenges of direct foreign investment. Such evaluations only served to emphasize the extent to which the principle of

national treatment was not being applied in other countries, focussing attention on the uncertainty of the norms governing international investment.

As was the case with the Gordon Report, the Watkins Report did not have an immediate, or, in the short term, significant impact on the formulation of state policy. It was either disowned or ignored by those members of the Pearson Cabinet in search of the Prime Minister's job, and its suggestion that an agency monitor the activities of foreign investors was rejected as too interventionist (Smith, 1973:348). Its liberal orientation to foreign investment was unlikely to stir public reaction against an imminent threat. Canadian state managers did, in 1971 create a Canada Development Corporation along the lines of that suggested by the Watkins Report, but only because it was to be a developmental agency (encouraging Canadian investment) rather than one which would encourage the repatriation of assets (see Tarasofsky, 1987, for a complete discussion). The only immediate response of any note was the election campaign strategy of Tommy Douglas and the NDP. Douglas urged the adoption of the measures in the Watkins Report during the 1968 federal election campaign -- but the issue did not prove important enough to encourage other parties to discuss it.

Despite the failure of the Watkins Report to have an immediate impact upon public policy, the general concerns over the extent and nature of foreign investment in Canada did not diminish. In fact, these were at the same time being critically addressed within the intellectual community. The problem of foreign ownership was defined as an important factor limiting a state's autonomous decision-making capacity -- along the lines of the Watkins Report -- but it was also seen to create serious structural problems within a host economy. This intellectual turn to "dependency theory" had its origins in the radical structuralism of Raul Prebisch's The Economic Development of Latin America and its Principal Problems (1950) and ECLA (the United Nations' Economic Commission for Latin America), Paul Baran's Political Economy of Growth (1957), a neo-Marxist analysis which profoundly guided Andre Gunder Frank's seminal essay, "The Development of Underdevelopment" (1966), and, in Canada, Kari Levitt's Silent Surrender: the multinational corporation in Canada (1970). Kari Levitt's book was both "intellectually intriguing and politically momentous" (Carroll, 1986:5). It provided ideological direction and theoretical coherence to nationalist movements and movements on the political left, such as the Waffle.

Additionally, as the most coherent statement of the era of a Canadian Marxist school of political economy, Levitt's book set "the terms of reference for a considerable volume of critical scholarship on Canadian political economy that emerged in the ensuing decade" (Carroll, 1986:5). A measure of Levitt's critiques had already been foretold in the publication of the Gordon and Watkins Reports, and were to echo through the next two governmental investigations.

Levitt challenged the passive acceptance of the branch plant economy by pointing out that through this economic arrangement, it was no longer in the interests of the economically powerful in Canada to be nationalists. Branch plant economic development had resulted in an industrial structure marked by low rates of research and development, little domestic sourcing, few exports, and an industrial decision making centre located in another country (Levitt, 1970, 116-56). Prosperity comes more easily to a Canadian capitalist class allied to the American empire, she argued, and if national autonomy and indigenous control are thereby sacrificed, no tears are shed. Levitt pointed to the convergence of interests between the Canadian capitalists and the American interests they represented through the branch plant economy, and saw this

relationship as bringing the greatest of the costs associated with foreign investment -- the loss of any desire to be nationalist among the Canadian capitalist class. Levitt acknowledged that there had grown up a Canadian indigenous capitalist class, but saw the post-war era as the period of its "silent surrender". In fact, she argued that "[t]he most serious consequence of the bias towards imports resulting from branch-plant economy in Canada is the discouraging effect on Canadian entrepreneurship.... The more market demand is shaped by metropolitan corporations, the more restricted becomes the area in which independent Canadian enterprise and innovation can operate" (Levitt, 1970:126). For Levitt, the problems of foreign direct investment were structural, and not simply related to the extraterritorial application of U.S. laws.

Standing in contrast to Levitt's observations of a surrendering capitalist class, studies of the activities of Canadian multinationals (firms which in the 1960s included the Canadian Pacific Railway Co., the Steel Co. of Canada, Algoma Steel Corporation, Seagrams, and the International Nickel Company, among others) concluded that in 1966, Canada placed sixth among capital exporting countries, a position which remained the same in 1971 (Niosi, 1985:44). This placed Canada in league

with France, Switzerland and the Netherlands, countries with an acknowledged independent capitalist class. As we will see, however, the concentration of activity of indigenous Canadian capitalists was not in the manufacturing sector which captured most of Levitt's attention.

Levitt's intellectual concerns were the prevalent ones, however, and they were not operating in a Canadian ivory tower. As LeDuc and Murray have pointed out, "the first [comprehensive] Canadian policy initiatives to restrict foreign (particularly American) investment and to reduce Canada's trade dependence on the United States coincided with a sustained shift of public opinion in a direction increasingly critical of the Canada-U.S. relationship throughout the late 1960s and early 1970s" (1984:131). As they discuss, while in 1956 (during the Gordon Commission hearings), 27% of the Canadian population agreed with a Gallup Poll statement that there was "too much U.S. influence in the Canadian way of life": by 1974 the numbers had increased to 57% (LeDuc and Murray, 1984:132). Even the Financial Post published a laudatory essay praising Walter Gordon as a hero, and asking; "why won't Ottawa do something, before it's too late?" (Ross, 1970:7). Criticism of Canadian policy founded on the continentalist orthodoxy of the

Department of Finance was growing.

Canadian concerns about the pervasiveness of American values and products, reinforced by the concurrent struggles in the United States to redefine the American way of life, began to be reflected in increasing worries about the extent of foreign ownership of the Canadian economy. The growing concern was beginning to take shape in political activism. In September 1969, the Waffle Manifesto was unveiled at an Ottawa press conference. The Waffle movement, a wing of the NDP led by such notable figures as James Laxer and Melville Watkins, called for "economic independence" for Canada. Canada was to throw off the yoke of the American Empire through the adoption of socialist policies, among which nationalization was to be a key instrument. The consequences of Canadian state inaction were to be most severe; the Waffle's analysis, pinned to the de-industrialization thesis, suggested that the "strategic aim" of United States government policy was to "shift manufacturing and jobs to the U.S." with obvious consequences for future employment, economic security, and quality of life for Canadians (Laxer, 1973:9).

The assumptions of the Waffle explicitly rejected the rosy picture of Canada's attractiveness painted by

the Gordon Report and assumed by the Watkins task force. The developing internationalization strategies of U.S. firms were likely, in the assessment of the Waffle, to bring about the movement of U.S. subsidiaries in Canada to low-wage locations. The Waffle was among the first public groups to recognize that manufacturing production for a national market might no longer be the norm of foreign investment. The Waffle was also the first significant political organization to grapple seriously with the problem of foreign ownership, its critique founded in a rejection of capitalism. The relative, although short-term, success of the Waffle within the NDP (attracting the support of one-third of the delegates at the October 1969 convention despite the opposition of "virtually every high ranking spokesman in the party" (Resnick, 1977:230) attests to the growing public attention to, and concern over, Canada's economic destiny.

In September 1970, a more centrist organisation, the Committee for an Independent Canada, was formed under the honorary chairmanship of Walter Gordon. The CIC called, as its first statement of purpose, for the Canadian state to "implement policies designed to increase the proportion of Canadian ownership, including the establishment of a federal agency to supervise the

conduct of foreign-controlled operations in Canada, and in particular any new takeovers". As Resnick has pointed out, despite their important ideological differences, "the Waffle ... and the Committee for an Independent Canada ... have been emanations of the class whose interests were directly linked to the existence of a vigorous nationalist state" (1977:170). Both groups were dominated by members of the new middle class -- self-employed or salaried professionals, many working for the state, for universities, in schools, in research institutes -- groups who had come "into their own" with the "fantastic take-off of the state sector and of higher education in the 1960s" (Resnick, 1977:167), and whose career future often depended on the expansion of that state sector. Within the Waffle, for example, 21 percent of its members were students, 8 percent teachers, 10 percent university professors, and 19 percent professionals. James Laxer and Mel Watkins, its main leaders, were from this same class. Within the 120-member steering committee of the CIC, 32 were academics, 10 students, 10 journalists and broadcasters, 6 politicians, and 25 were professionals, many of these writers and artists. Walter Gordon, the honorary chairman, was the only representative of the dominant capitalist class.

We have already identified the new middle class as an important agent for change in the foreign investment debate. George Ross, examining the case in France, makes the point that just as with the capitalist class, the new middle class is composed of fractions. The first is a private sector new middle class, which is "rewarded from surplus value accumulated in the very organizations where it works and from the very work processes in which it participates" (1978:178). It tends to identify its interests with the success of the firm, and to be strongly aware of the differences which separate it from labour. As such, the private sector new middle class tends to identify with a capitalist understanding of the world (Ross, 1978:178). This fraction of the new middle class was not the one spearheading change in Canada's foreign investment policy.

The second fraction, the public sector new middle class, tends to have a different political perspective. As public sector intellectual workers, they "obtain their surplus-derived benefits indirectly, not through involvement in production or distribution, but from the state, which drains the necessary funds through taxation" (Ross, 1978:179). Public sector is here broadly defined, and includes, among its most prominent members, teachers and academics. The political agenda

of this class is not defined in terms of a direct relationship to capital, but rather in terms of its "proprietary interest in the state, believing it to be "its" state" (Ross, 1978:179). This was certainly the case in Canada, where members of the new middle classes encouraged the expansion of the Canadian state. Mel Watkins, for example, regarded the "steady expansion of Canadian public ownership" as the "means by which we can halt and reverse American economic penetration". Robert Page, an academic and 1974-5 chairman of the CIC, echoed these views, predicting greater public ownership in Canada to combat "geography and the power of transnational corporations" (Cited in Resnick, 1977:167). The public sector new middle class had an even more compelling interest -- an economic one -- in asserting its "ownership" of the state. The expansion in social spending in the 1960s had not only subsidized the education of many in this class, but had provided them with jobs after graduation, whether as teachers in a greatly expanded public university system, or as state officials administering the programs of the equally expanded state.

The new middle class in Canada is further divided, however, with regional states capturing the proprietary ambitions of many. The public sector new middle class

of most interest to us in this analysis is the one based predominantly, although certainly not exclusively, in Central Canada -- largely in the region between Montreal and Southern Ontario. There are a number of reasons why this is the case. To begin, by the early 1970s, the concern of the public sector new middle class in Quebec was focussed almost exclusively on the national ambitions of the province, and not on the comparatively trivial issue of foreign investment. The state which the Quebec new middle class defined as "its" state was the Quebec state.

As to the West, Pat Marchak has made the important point that patterns of concentration in manufacturing activity in the Montreal/Southern Ontario triangle have influenced the development of viewpoints different from those in the far more resource dependent West (1980:19). As we will see in more detail, most of the major criticisms of foreign investment brought by the representatives of this fraction of the new middle class related, as Levitt's own work did, to manufacturing investment. This is not to say that members of the public sector new middle classes of the West were not interested in the issue of foreign investment, rather, it serves to underline the extent to which the main political concerns of groups like the CIC and the Waffle

were rather more Ontario centric than broadly "Canadian".

That writers, artists and intellectuals should have been involved in these political movements calling for a diminished foreign economic presence in Canada is hardly surprising, given the extent of the revulsion against the American involvement in Vietnam that swept the intellectual communities of most Western countries. The American involvement in the Vietnam war, and Canadian complicity through arms sales, gave impetus to calls for a Canadian move away from the Quiet Diplomacy of the Merchant-Heeney Report toward the statement of an independent foreign policy. While we can only speculate, it seems unlikely that in the absence of a general concern about U.S. activities the non-partisan Committee for an Independent Canada could have gained such prominence as a voice for the Central Canadian new middle class. Against this backdrop, however, the ideas advanced by the political movements of the new middle class could be played out, and could find an audience. In 1975, for example, one of the best-selling books in Canada was a study of Canada as an American satellite: Walter Clement's Canadian Corporate Elite (Marchak, 1980:26).

What did the new middle class introduce to the

debate about foreign investment in Canada? We have seen in the Gordon and Watkins Reports that concerns were already being raised as to capital shortage in Canada, extritoriality, and Canadian attractiveness as a site for investment. While the Gordon Report tried to suggest that there were negative consequences to a pattern of development characterized by heavy reliance upon foreign investment, his views were largely ignored, and the Watkins Report accepted the branch plant economy. More than any other group, the political representatives of the new middle class placed the issue of the negative impact of the branch plant economy for Canadian economic development on the public agenda.

The Wahn Report

In 1970, the Standing Committee on External Affairs and National Defence of the Canadian House of Commons (SCEAND), under the chairmanship of Ian Wahn, heard testimony on the nature of Canada-United States relations. This report, prepared at the instigation of the parliamentary committee rather than the government, reflected the mounting concerns about the U.S. foreign investment presence in Canada.

The Wahn Report solicited briefings from a number of commentators on the Canada-United States

relationship; among them, John Holmes (Director, CIIA), John Deutsch (Principal and Vice-Chancellor, Queen's University), Claude Ryan (Editor, Le Devoir), and Lester B. Pearson. To define their perspective on economic relations with the United States, in particular on the problem of foreign investment, they solicited the advice of Abraham Rotstein and A.E. Safarian. Rotstein concentrated his presentation on the necessity of finding a *modus vivendi* between the state and the multinational corporation, a relationship which he clearly perceived as being at least potentially antagonistic (1970:9:53). The large oligopolistic multinational, he argued, is not the most efficient method of allocating resources, and this fact alone may justify the intervention of the state in its operations. In fact, Rotstein referred to French regulatory policies which tried to restrict foreign investment in order to manage the structure of the French economy. Rotstein then returned to the "minimum common denominator" between the continentalist viewpoint and the nationalist one, and called for the establishment of an agency which would at least deal with the question of extraterritoriality.

Safarian, in a far more technical analysis, praised the multinational as being no better and no worse than

any domestic firm. Rather than seeing potential for conflict between the state and the multinational corporation, Safarian argued that benefits from foreign investment were largely the same as those from domestic investment (1970:10:77), although the Canadian state did need to develop tax policy which would allow it to gain access to the profits of the multinational firm.

Canadian policies have been at fault, however, and these need to be rectified. "In brief, we have emasculated the multi-national firm by our policies and have dissipated much of its potential benefit in an inefficient structure of much manufacturing industry" (1970:10:82). The Canadian state -- whose policies regarding matters such as combines, research aids, taxation and management development had created an inefficient industrial structure in Safarian's analysis -- did have a role to play in restructuring the Canadian economy, and could be interventionist in so doing. State interventionism was not to be a comment on the multinational firm, in fact, the one major conflict as a result of foreign investment was a state to state one, involved in the extraterritorial application of home country laws.

Other briefs before the Wahn committee suggested different perspectives. George Ball, the former U.S.

Secretary of State, introduced the notion of the truly global multinational corporation, with behemoths "rang[ing] the world ... with substantial flexibility on the basis of business decisions made less and less in terms of national markets and increasingly in terms of the world economy" (Ball, 1970:8:7). Ball did scowl at the United States tendency to engage in the extraterritorial application of its laws, in large part because this was an unjustified tampering with the functioning of the market. Robert Fowler, President of the Canadian Pulp and Paper Association concurred with Ball's perspective, and argued that restrictions against foreign investment should not be enacted in Canada for fear that recriminations would face Canadian firms on the verge of participating in multinational investment (1970:11:11). In the event of the imposition of regulatory initiatives, Fowler argued that U.S. investors might well say: "There are plenty of other more agreeable and exciting places in the world we can go. From now on, we will treat Canada as an uninteresting place for development, like say Utah in our country, or northern Ireland" (1970:11:19). Although speaking in terms of potential retaliation, Fowler suggested that Canada might not always be attractive to foreign investors. This lack of

attractiveness, however, would not be as a result of changing international investment patterns, but as a consequence of a "misguided" decision by the Canadian state.

Finally, W. Earle McLaughlin, Chairman and President of the Royal Bank of Canada, testified against the prevalent, though often unstated, assumption, that Canada needed foreign investment for balance of payments reasons. "The greatest single reason that Canada has a "chronic" deficit on current account is that she has a "chronic" surplus on capital account. And the reason she has a "chronic" surplus on capital account is that private foreign investors like what they see in Canada and invest their funds here." (1970:15:6-7). Canada did need foreign investment to sustain economic growth by McLaughlin's calculations, however. For his part, McLaughlin also criticised the negative implications of extraterritoriality.

Several assumptions are apparent in these testimonies before the Standing Committee. Among them, we find the notion that Canada did not need foreign investment for balance of payments reasons, but did need it for future economic growth. We also discover that, for two economists, state intervention in the economy is reasonable -- whether to guard against the ills of

branch plant investment, or to rectify errors of past state policy. We know that, for all representatives before the committee, state intervention would be legitimate in the face of questions of extraterritoriality. The fact of Canada's branch plant status is never questioned by these critics, and only two suggest that multinational firms may be moving away from this form of investment, with uncertain implications for Canada.

In the Eleventh Report of the Standing Committee on External Affairs and National Defence Respecting Canada-U.S. Relations, we see many of these viewpoints echoed and assumptions adopted. The SCEAND Hearings represent the first time members of the government have directly investigated the issue of foreign investment, making the assumptions of the report all the more important for our understanding of state manager learning. In the matter of balance of payments problems and extraterritoriality, the committee accepted wholly the views of Earle McLaughlin, quoting from him at length (1970:16-20). Canada might need foreign investment for economic growth, but it did not need it for balance of payments purposes, and should never find itself in a position where this would be so. At best, therefore, the Canadian need for foreign investment was

deemed to be ambiguous.

The Wahn Report reacted most strongly, however, to the presentations, explicitly or implicitly made, of the Canadian economy characterized by a branch plant structure. Whereas the Watkins Report was bound by the necessity of producing a consensus view among economists, the Wahn Report, drafted by bureaucratic managers, reflected the political calculation that the consequences of branch plant investment were to be found in more than the extraterritorial application of home country laws. Threats that multinationals might divest from Canada did not mean that Canadian legislators should ignore the concentration of foreign direct investment in the country, but rather, that they should encourage Canadian ownership, and review foreign investment applications. Both Rotstein and Safarian, from different perspectives, had accepted the legitimacy of an interventionist state -- one in order to control MNCs, the other, in order to correct past state errors. To the Standing Committee, it seemed that the consequences of branch plant investment needed an interventionist state whatever the goals of policy.

The Wahn Report argued that, in particular, "the major deficiency in Canadian policy with respect to foreign ownership has not been its liberality toward

foreign investment but the absence of an integrated set of policies with respect to it" (Wahn Report, 1970:45), taking the same line as the Watkins Report on this score. To that end, the committee gave serious attention to the proposal that a Canadian Ownership and Control Bureau should be set up to monitor or control the flow of foreign investment to Canada, thus continuing the theme of the Watkins Report for the creation of some type of agency. The Bureau would have a monitoring and enforcement role (and as such, be far more interventionist than the agency suggested in the Watkins Report), identifying and gathering information about the activities of foreign-owned firms operating in Canada, developing code of conduct guidelines for the economic activities of these foreign firms, and ensuring their compliance with these guidelines.

Further, however, the Wahn Report proposed that the Bureau should play a role in screening new investment to Canada. Whereas the major concern of other Reports was to monitor exsistant investment in Canada, SCEAND recommended that, in addition, new investment come under the scrutiny of the Bureau. Specifically, the Report suggested that the Bureau examine "all applications for new foreign investment in Canada with the intention of determining whether or not the proposed products could

be more advantageously manufactured under licence by Canadian controlled corporations. If the Bureau determines that this is the case, it should make vigorous efforts to have such arrangements effected" (Wahn Report, 1970:50). The powers of the Bureau of Ownership and Control, despite the Wahn Report's basic assessment that foreign investment had been a positive force in the economic maturation of Canada, were to be far reaching and potentially highly restrictive. The consequences of branch plant investment, identified particularly in the report as a lack of research and development, were not to be left undisturbed, although as much as possible, attempts to Canadianize industry in Canada should be positive (incentives to Canadians), rather than negative (sanctions on foreign investors).

The Wahn Report clearly reflected Gordon's concerns about the branch plant status of the Canadian economy, and recommended that active measures be taken to ensure that Canadian firms develop their own export and research capabilities -- two of the consequences identified as associated with the branch plant. The Wahn Report does implicitly accept the notion of Canada's attractiveness to foreign investors, however. We see a new set of assumptions in play here, those echoed by the CIC and the Waffle; Canada had a serious

concentration of foreign investment in some sectors, and this concentration should be balanced by some Canadian ownership. It was no longer a question of Canada being able to attract investment -- this was taken for granted -- but that Canada may have too much investment. Like the Watkins Report before it, and despite testimony which suggested it, the Wahn Report did not question whether established patterns of branch plant and resource-extractive investment were changing. Rather, the Report reacted to an existing situation, without wondering whether it could change independent of state policy.

Before SCEAND had brought down its recommendations, the Trudeau government had already established its own task force to bring forward proposals on foreign investment for governmental consideration. Headed by Herb Gray, a Cabinet Minister without Portfolio (and a supporter of the Committee for an Independent Canada), the task force reflected rising pressures placed upon Cabinet by the nationalist wing of the Liberal party, as well as by the successes of the NDP in focussing attention upon the issue. Gray's public interviews emphasized the extent of Canadian concern over foreign ownership, saying, for example, that "[e]ven out West ... the businessmen I have met are worried about too

much foreign ownership and control" (Baxter, 1970:5). Trudeau, himself no fan of nationalism, acknowledged at the November 1970 Liberal party convention that "Canadians have become a lot more nationalist economically than they were before." With polls revealing a growing anti-American and nationalistic sentiment among the Canadian population, with lead articles in national magazines such as Maclean's proclaiming in February 1970 that "Maclean's wants to fan the flames of what we take to be the heartening surge of a new Canadian nationalism" (Tower, 1970:1), with political movements coalescing around the issue of foreign direct investment in Canada, with an international climate characterized by the United States' involvement in Vietnam and troubled by the domestic consequences of that action, with other industrial states taking action to regulate the flow of foreign investment, the Canadian state responded by acknowledging that foreign investment was a serious issue. As Franck and Gudgeon have remarked, "the summer of 1970 marked the last phase of research, exploration and hortatory exercises. The time had come for full-scale government involvement in investment regulation" (1975:102).

The major federal political parties certainly

responded to the birth of this Canadian nationalism, responses reflected by changes in party platforms. Nationalism had long been the political stance of the New Democratic Party; at the 1961 party convention, a resolution was adopted which called for a "break [in] monopoly control over Canadian industry and resources", particularly in industries dominated by foreign-owned firms (Fayerweather, 1974:184-85). While the NDP as a whole did not support the tenets of the Waffle Manifesto, by 1970 the party did advocate the screening of industry takeovers by foreign investors, and the development of strict rules regulating the expansion of foreign-owned corporations in Canada. On the opposite end of the political spectrum, the Progressive Conservative Party of Canada did not concern itself with any discussion of foreign investment until 1969, a point at which public debate of the issue made it difficult to ignore. Foreign investment was certainly not an issue for the Conservatives in the 1968 federal election (see Meisel, 1972), unlike the NDP. While there was no unanimity within the party as to the direction which should be taken by foreign investment policy, key speeches by leader Robert Stanfield indicate a general orientation in favour of nondiscrimination against foreign firms, subject to a key sector exception

(Fayerweather, 1974:183). The party came to favour policies which would ensure a greater degree of Canadian control of industry, although it continued to prefer the "building up [of] Canadian firms, disclosure by foreign firms, and requiring Canadian participation on boards of directors" (Fayerweather, 1974:184) rather than the creation of a screening agency which might restrict the inflow of foreign capital.

The Liberal Party of Canada began a divided journey to foreign investment regulation with the position that "[t]he government should take steps to encourage greater ownership of the economy, without discouraging foreign investment" (Party convention, 1966; cited in Fayerweather, 1974:178). By 1970, the winds of nationalism were clearly blowing through the party; MP Alastair Gillespie (another public supporter of the CIC) produced an industrial policy report which called for 50 percent Canadian ownership and government screening of foreign takeovers in the area of resource development; the Wahn Report, supported by the Liberal majority on the Commons Committee, was released; and Herb Gray began work on his report on foreign investment, indicating at least a Liberal acknowledgement of a national concern over foreign investment. In November 1970, the Liberal party convention supported resolutions calling for the

screening of all foreign investments, and the creation of special classes of voting shares to permit majority Canadian control of foreign-owned firms (Fayerweather, 1974:180). For all three parties, the questions surrounding foreign investment centered around control over the Canadian economy. Foreign investment was seen in terms of the capital which it brought, and most often accepted as necessary capital.

With public attention already sensitized to levels of foreign ownership and control in Canadian industry, the media coverage of a number of takeovers and takeover attempts into the early 1970s lent credence to cries for investment regulation. The state, both provincial and federal, did act, but it is instructive to note that what was being "done" was the selective intervention in sectors in which the interests of Canadian capital already supported protection; publishing, resources and financial industries. In 1969, Royal Securities was acquired by Merrill Lynch, Pierce, Fenner & Smith, Inc., and in 1970, Ryerson Press was bought by McGraw-Hill. The takeover of Royal Securities prompted a study of the securities industry and the imposition of restrictions by the Ontario government on foreign ownership of securities firms. The Ryerson Press takeover, and public reaction to it, set the scene for the

intervention of the Ontario government against the U.S. purchase of McClelland and Stewart Limited. On an ad hoc basis, the federal state intervened to prevent the sale of a number of large Canadian interests; the sales finance corporation Traders Group in 1969, Denison (uranium) Mines in 1970, and Home Oil in 1971. These interventions led Franck to assess that; "aroused public sentiment concerning alienation of such visible Canadian businesses, have made any such acquisitions [of large Canadian firms] virtually untenable" (1976:59). As Michael Bliss has complained:

[b]y the late 1960s and early 1970s the concern about foreign investment, which was continually being stimulated by media publicity of dramatic American "takeovers" of Canadian companies, was often expressed in popular fears that the country was being sold out to the Americans. Unless something was done soon, the argument went, the Americans would own everything and Canada would disappear (1984:7).

In many respects, the seminal event confirming the Canadian wariness of its close ties with the United States, and thus of the level of foreign investment in Canada, came on August 15, 1971. Signalling the final gasp of the Bretton Woods agreement, U.S. President Nixon announced that convertibility of the U.S. dollar into gold or any other reserve asset was to be suspended. Further, and all in response to the growing

balance of payments difficulties, Nixon enacted tax legislation aimed at encouraging American corporations to make future investments in new productive facilities in the United States, rather than abroad. U.S. firms increasing their capital investments at home would receive tax cuts through the introduction of a seven percent tax investment credit. In addition, the Domestic International Sales Corporation (DISC) was created, encouraging U.S. multinationals to shift already existing production in branch plants abroad back to the United States. DISC was to achieve this by allowing exporting U.S. firms to write-off fifty percent of the taxes on their foreign sales. Measures such as the DISC lent support to the Waffle claim that the drive to de-industrialize Canada was a strategic aim of U.S. government policy, and to the claim of the CIC, the Watkins and Wahn Reports, that efforts of the Canadian state should be directed towards increasing Canadian participation in, and control of, the economy. Despite its attempts, the Canadian state was unable to secure exemption from the U.S. measures.

The actions of the American state effectively signalled the breakdown of the post war hegemonic world economic order. The United States was changing the rules of the game, and in so doing re-politicizing

economic questions, and forcing state actors to reassess their country's status within the emerging economic system. For Canadian state managers, not only had the Canadian state lost control of some of the levers of independent action as a result of Canada's economic penetration by multinational firms, but the special relationship with the United States which could buy Canada exemptions from the more painful consequences of this interdependence with American policy had been ended by the Nixon administration. Information as to Canada's apparent dependent status was now not only coming from Canadian interest groups; it was being reinforced by unilateral decisions of the U.S. government to change the rules of the world economic game from which Canadian state officials could not secure exemption.

The concerns of the new middle classes were, as we have seen, particularly successful in defining the state's emergent understanding of the foreign investment issue. Their concerns, however, did not imply social unanimity. As suggested earlier, the position of Canadian capitalists in the late 1960s and early 1970s was, in many respects, an ambiguous one. The creation of the Export Development Corporation in 1969 (offering foreign investment insurance to Canadian firms) and of the Canadian International Development Agency in 1970

(with a Business and Industry Division to encourage Canadian firms to invest abroad) reflected the interests of capital for some state support. These same business interests, however, tended to oppose any move toward regulation of foreign investment in Canada by the Canadian state. Canadian capitalism was witnessing the emergence of a number of Canadian-owned multinational firms and banks, whose corporate view was opposed to interference with the free movement of capital into or out of Canada. For Robert Bonner, President of MacMillan-Bloedel in the early 1970s, those seeking to restrict investment flows to Canada were "dilettantes who espouse the narrow nationalisms of the separatists and the neurotic left", acting without recognition that cutting Canada off from the "free flow of capital" would guarantee Canada only high unemployment (cited in Resnick, 1977:152). Foreign multinationals operating in Canada were just as opposed; W.O. Twaits, Chairman of the Board of Imperial Oil, dismissed nationalist worries by asserting that: "[s]overeignty should never be of real concern to Canadians since assets by foreign-owned firms are resident in Canada" (1972:29/6).

The Canadian Manufacturers Association and the Canadian Chamber of Commerce, as increasingly vocal representatives of the interests of business in Canada,

were on the frontlines of opposition to legislation restricting foreign investment (Gray Report, 1972:302-04). The CMA and the Canadian Chamber, speaking for the interests of foreign-owned corporations as well as Canadian-owned firms, many of them multinationals in their own right, reacted against any regulatory expression of Canadian nationalism. Canada was part of an international economy, and should not seek to cut itself off from it [3]. The Canadian Chamber was of the opinion that "short-term political considerations [were] being given priority over long-term national interests" in governmental moves toward regulatory legislation (Wolff, 1973:31/5), while the Canadian Manufacturers' Association believed that "Canada should continue to enjoy foreign investment" (Stevens, 1973:34/7).

The division of Canadian capitalists into "camps", big versus small, was not a black-and-white issue. Some members of the big business community offered reserved support for nationalist aims (J.H. Moore of Brascan [4], David Kinnear of T. Eaton Company, for example), while some smaller businessmen disavowed any nationalist ideals. These groups were not inclined to object to state support for Canadian firms, but did not want any intervention which might affect the activities of

multinationals in Canada. Even Richard Thomson, president of the Toronto-Dominion Bank, while rejecting regulatory legislation, contended that "Canadians are concerned about domination of our economy by outsiders -- mainly American -- and with good reason I question whether Canada will be able to compete in manufactured products without bringing genuinely Canadian products and processes into the world market" (1972:10).

The Gray Report

Divisions between the interests of most capitalists and the growing class of Canadian professionals, reflected within the Liberal party ethos of "more Canadian control, but not at the expense of foreign investment", came to the fore with the debate in the Liberal party surrounding the release of the Gray Report. The Gray Report was not a report per se; it was not commissioned by the government for public debate. Over 400 pages in length, the report was produced for consideration by Cabinet as a Memorandum entitled "Domestic Control of the National Economic Environment: The Problems of Foreign Ownership and Control", and was presented to Cabinet in May 1971. Undoubtedly the most comprehensive study of foreign investment in Canada,

Prime Minister Pierre Trudeau hedged on the question of its public release. Media reports in fact indicated that the divisions within Cabinet had led it to decide against publication of the Report (Canadian Forum, 1971:8). Despite, and perhaps because of, this, the Report was leaked, and The Canadian Forum, in its December 1971 issue, reprinted an abridged version of the confidential document.

The Gray task force (for want of a better term) differed substantially in its purpose from those of Wahn, Watkins or Gordon. While the other reports sought to influence policy, Cabinet had asked Gray to develop policy (Confidential Interview, senior Liberal party official, September 1989), spurred by public reaction to the growing number of high profile takeovers of Canadian firms. The process of compiling the Report also differed from the others in that the committee drafting it did not seek submissions from various interest groups. Rather, Gray, acting in his capacity as Government Minister, seconded people from government departments (primarily Finance, and Industry, Trade and Commerce), and hired others as contract researchers. The committee expanded and contracted as necessary during the research and writing process, and it did at one point include in excess of eighty people. Among

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them was Joel Bell, who chaired the Working Group on Foreign Investment from 1970 to 1973, and later went on to become the Senior, and then the Executive, Vice-President of Petro-Canada.

Certainly far-reaching, the Gray Report recommended the creation of a foreign investment review agency which would scrutinize all foreign takeovers of Canadian firms, all new investments, and the unrelated expansions of foreign-controlled companies already established in Canada [5] (Gray Report, 1972:463-471). Also recommended for screening were licensing arrangements, joint venture agreements, and management contracts between foreign firms and Canadians business interests (Gray Report, 1972:468-69) [6]. This aspect of the Gray Report, while not enacted into the mandate of the Foreign Investment Review Agency, does reflect some of the changes beginning to take place in the international political economy, focussing, as we will recall from Chapters Two and Three, on what were then very new adaptation strategies by multinational firms. As well, the Report addressed issues which were still new to the discussion of foreign investment: transfer pricing, intra-firm trade, and sourcing, as well as implications of foreign investment for foreign and cultural policy. The Report revealed a very sophisticated understanding

of foreign investment. While the Report was published with the caveat that "it is not a statement of government policy nor should it be assumed that the government endorses all aspects of the analysis contained in it" (1972:v), subsequent governmental policy initiatives make clear its validity as "primary travaux preparatoires (Franck and Gudgeon, 1975:102).

The central message of the Report was an important one: that national governments must screen closely the activities of foreign firms in their domestic environments since global firms plan on a world-wide scale. This was not the same argument as the one being presented by the Waffle, that MNCs were themselves global. It reflected, however, the contention that foreign subsidiaries in Canada were subject to the planning decisions of a non-resident owner. The report paints a picture of a Canadian economy characterized by truncated subsidiaries or miniature branch plant replicas (neither engaging in R&D), resulting in part as a consequence of Canadian tariff policy. Multinationals move abroad, for the Gray Report, because they wish to secure an export market -- they are the filiale-atelier (1972:414). Although the Report mentions the possibility of rationalization (defined in terms resembling world product mandating), it suggests that

even if the Canadian state were to offer subsidies, such rationalization would not occur in the absence of reduced tariff barriers. Additionally, the Report argues that Canada's attractiveness as a location for resource extraction has been the result of its ability to provide a secure and ample supply of resources, and for U.S. firms, of geographic proximity. Such firms seldom process the resources in Canada, however, because of the comparatively higher cost of manufacture in Canada, and because resource investment is often a backward linkage for firms already engaging elsewhere in the processing of resources (Gray Report, 1972:413). While certainly a more comprehensive analysis than that conducted by the Gordon Commission, the Gray Report came to substantially the same conclusions; Canada's economic development can be described as relying on foreign branch plants and foreign resource needs. The Canadian location in the international economy is to supply a market for foreign goods, and the resources to produce those goods. Furthermore, the Gray Report does not suggest that any of these features is likely to change -- implying that the Canadian economy will remain as attractive to investors as it always has (although it may be saturated in terms of the amount of investment it can continue to absorb). The conclusions of the Gray

Report were clearly consistent with the viewpoint argued by the Committee for an Independent Canada.

The Gray committee perceived its mandate fairly narrowly. The question of whether Canada needed, or could attract, foreign investment was moot. The issue was to determine whether foreign investment had had a positive or negative effect on Canadian economic development. Issues which had been important for other committees, such as extraterritoriality, were of less concern to Gray. Extraterritoriality was a negative consequence of DFI, and as such, was a second order problem to the issue of positive or negative effect. It is clear from interviews of political and bureaucratic state managers that Gray himself understood the committee's work as focussed only on evaluating the merit of the criticisms of the branch plant economy put forward by groups such as the Waffle and the CIC. When asked which source most influenced the committee, a senior Liberal party official could only recall Kari Levitt's Silent Surrender -- although this same official was quick to point out that this did not imply that the committee accepted the book's thesis (Confidential interview, September 1989).

If Gray himself had "learned" of the negative consequences of foreign direct investment, as a

political leader with roots in the Ontario middle classes, what of the bureaucrats who participated in and consulted with the Gray task force? Were any particular interests being represented there? Again, interviews indicated that both the Departments of Finance, and Industry, Trade and Commerce raised the issue of the potentially negative consequences for balance of payments of regulating foreign investment. These arguments were dismissed by political staff as "second best" arguments, which did not address the very real negative effects of foreign investment. While it is clear why officials of the Department of Finance would present a balance of payments argument, it is not so clear why those same interests would be expressed by officials of ITC. The answer is to be found in the historical evolution of the department, which had to then (despite a brief separation of Trade and Commerce from Industry, creating two departments in the mid-1960s) always emphasized the interests of trade (particularly resource exporters) -- with its balance of payments implications -- over those of industry (see Williams, 1982:118-9 for a good overview).

The Gray Report reflected some of the same convictions as the Wahn Report about the Canadian "need" for foreign investment. We can see the extent to which

bureaucratic input on this point was a second best argument in the Report's conclusions. It bluntly assessed that there was no obvious balance of payments reason for foreign direct investment (1972:83), and that in fact, a further inflow of capital from abroad "will contribute nothing to economic development unless it serves a particular need for capital that cannot be fulfilled in Canada perhaps because of sheer magnitude, or because it is accompanied by some other element that is of particular value to the economy -- new technology, for example" (1972:84). The Gray Report came closer than any other official statement to asserting that Canada simply had enough foreign capital, and could afford to be "selective in determining what type of foreign capital will be allowed to enter" (1972:84). Canada could be selective, of course, because it would remain attractive to foreign investors. In the recommendation for a screening agency, bureaucratic inputs were important in maintaining some of the traditional liberalism of the investment norms, however. While Gray was most impressed by the development of regulatory policies in France (see Mytelka, 1986, for an elaboration of these), bureaucratic officials insisted that any regulatory process adopted by Canada be far more transparent (Confidential interview, senior Liberal

party official, September 1989).

Even though the Gray Report comes closest to acknowledging that other forms of investment -- other than branch plant and resource-extractive -- exist, it does not attempt to redefine foreign investment to include non-equity forms of international cooperation. It could not have been expected to do so, of course; as we saw in Chapter Two, firms adopted strategies such as strategic partnering in knowledge intensive production in the later 1970s, although capital sharing joint-ventures, which the Gray Report does acknowledge, had been under way for at least two decades (see Mytelka, 1987b:10). Processes taking place almost simultaneously in the pattern of international investments, however, have implications for the conclusions of the Gray Report, particularly its suggestions with regard to the lack of Canadian research and development.

In sum, therefore, in the Gray Report, we see the crystallization of a series of assumptions about the nature of foreign investment in Canada and Canada's position in the international economy. Their genesis is clearly found in the political convictions of the new Ontario-centric middle class. Canada had enough foreign investment. Canada was attractive to foreign investors.

Canada was a branch plant economy. Gray's recommendations for regulation flowed quite naturally from these assumptions.

CREATION OF THE FOREIGN INVESTMENT REVIEW AGENCY

By May 2, 1972 the Trudeau government was compelled to release the complete version of the leaked Gray Report, Foreign Investment in Canada, and two days later, presented to the House a proposal for a foreign investment screening agency in the Foreign Takeovers Review Bill (Bill C-201). The Takeovers Bill was a considerably watered down version of the recommendations of the Gray Report, intending to screen only foreign takeovers of existing Canadian businesses for their benefits to the Canadian economy. Gray's proposals for the screening of all new foreign investment plans, and the more radical suggestion for the monitoring of existing foreign investments in Canada were not accepted. Further, to signal that this was to mark the extent of government intervention in foreign investment decisions, Prime Minister Trudeau announced to the House of Commons that the bill was the sole piece of legislation in this area being considered, and not part of a larger package (Franck and Gudgeon, 1975:106).

Despite relatively rapid passage through Committee

(accepted June 22, 1972), the Takeovers Bill died on the order paper. The Liberal Government effectively found itself in a no-win situation. The Bill, designed to appease the concerns of the strong nationalist movement, only fuelled those worries. Franck and Gudgeon argue that the leaking of the Gray Report gave time to nationalist groups to read and digest its essence, and develop expectations about the direction of future government policy. The tabling of the far more moderate Bill C-201 thus sparked opposition from the nationalists who had come to expect a comprehensive strategy to repatriate the Canadian economy (1975:106).

Our purpose here, though, is to assess the process of state manager learning, and the failure of Bill C-201 provides us with a unique opportunity to do so. Full hearings were held before the Standing Committee on Finance, Trade and Economic Affairs of the House of Commons, and these hearings provide us with an opportunity to assess directly the kind of information -- assumptions and perceptions of direct foreign investment -- being presented to state managers. Jean-Luc Pepin, at the time Minister of Industry, Trade and Commerce, presented the bill to committee as a "means of safeguarding Canadian interests in the area of foreign investment" (1972:17/11). A general screening

device, Pepin argued, would not deter investment as significantly as a key sector policy, and it was not in the interests of the government to "eliminate or strongly decrease foreign investment", since particularly in manufacturing, foreign investments offered considerable advantages as well as disadvantages (1972:17/11-12).

The Committee for an Independent Canada, representing, as we have argued, the views of the largely Central Canadian, nationalist, new middle classes, objected strenuously to the bill. Edwin Goodman, Chairman of the Committee, argued that "the procedures outlined in the bill will not be of any substantial assistance in increasing the country's control of its economy and is totally inadequate even to check the constantly increasing control of the economy by foreign investors" (1972:20/30). Goodman went so far as to call the bill a "mockery" (20/31), a "zero", a "nothing", a "farce" and a "laugh" (20/33), arguing that it would do nothing to stem the expansion of foreign investment in Canada. Other members of the Committee for an Independent Canada -- Walter Gordon (Honourary Chairman), Mel Hurtig (co-chairman), Barbara Daprato (executive director), Jack Biddell (treasurer), and Robert Page (chairman of the Peterborough branch) spent

the morning of June 13, 1972 testifying before the Standing Committee and trying to make clear their opposition. The CIC clearly rejected the concerns of the Waffle that Canada might be a pawn in a U.S. de-industrialization strategy, arguing instead that the tide of foreign investment was likely to continue unabated if stringent controls were not brought in. Canada was attractive to investors, and would remain so.

Additionally, the CIC clearly reflected the assumption that Canada was a branch plant economy, and had suffered dearly for the privilege. An impassioned Mel Hurtig listed some of the problems to come from this form of economic development:

the drain of funds, the stifling of Canadian development in certain areas, what the Gray Report calls truncation, the dependency that results to the Canadian economic system, the vulnerability and all these things that are the direct results of so high degrees of foreign equity investment in Canada [sic] (172:20/41).

Finally, the CIC clearly believed that Canada not only had enough foreign investment, it had too much -- and that this "too much" had turned elements of foreign ownership into foreign control (Hurtig, 1972:20/40).

Capital held a different view. The Canadian Manufacturers' Association argued that foreign investment was needed to fuel growth and prosperity in

Canada. Foreign corporations were seen to be "providing jobs for many hundreds of thousands of Canadians ... paying taxes to the tune of many hundreds of millions of dollars ... contributing mightily to both our economic growth and our national standard of living", and were no less than "the very lifeblood of a host of cities and towns across Canada" (Flintoft, 1972:22/48). Bill C-201 was so inoffensive, however, that the CMA was low-key in its opposition, declaring the bill to be "moderate" (Flintoft, 1972:22/49), although not recommended. The Canadian Chamber of Commerce, for its part, refused to make any general comment about the desirability of the bill in its submission, choosing instead to argue technical points about the definition of criteria for proposed acquisitions, or for the determination of non-eligible persons (Canadian Chamber of Commerce, 1972:22/82-85).

The Canadian Labour Congress, for its part, sided most closely with the CIC (although it was never prepared to make its case as strongly), arguing that "[a]fter two years of intensive study by its own task force, it is no exaggeration to say that this government policy does not even begin to deal seriously with the question of foreign ownership and control of the Canadian economy" (Canadian Labour Congress,

1972:21/37)). The CLC clearly argued that Canada now had enough foreign investment; in fact, that the benefits of past investment had brought Canada to a stage of economic maturity that would let it continue to grow without foreign assistance.

In the evaluation of Bill C-201, the sternest opposition came from nationalist forces, and not from groups representing the interests of Canadian capital. The strongly held view that Canada had too much investment articulated in the lengthy CIC briefing contrasted with the CMA's assertion that Canada needed investment, but the proposed review policy was tolerable. It is interesting to note that neither state managers -- bureaucrats or politicians -- nor representatives of social groups or classes discussed the fact that flows of manufacturing investment in Canada, as we saw in Chapter Three, had begun to decrease, and that, furthermore, such investment was beginning to concentrate in capital-intensive industries. No mention was made as well of the increase in investment in resource-based industries. That there was little discussion of this was not surprising; it was only 1972, the trend had hardly been established, and the Gray Report with its 1967 data was for most commentators the latest update of the investment

situation in Canada -- and it did not show that patterns were changing. These parallel trends were to pose problems for the Agency, however.

Additionally, of course, provincial reaction was a significant factor; while concern over foreign investment was high in Ontario [7], Manitoba, Saskatchewan, and British Columbia, Atlantic Canada, and to a lesser degree Quebec and Alberta, had expressed serious reservations to any federal policy which might limit the flow of foreign investment to their regions [8]. The Maritime provinces in particular argued that the bill was some form of Central Canadian "plot". "To be blunt, it seems as if certain segments of opinion in Central Canada, having achieved the benefits of industrialization for themselves, now wish the Atlantic Provinces to forego the industrialization they never had in the interests of maintaining an ill-defined Canadian economic independence" (Weymen, 1972:20/10).

In early June, the Committee for an Independent Canada petitioned the members of the House of Commons to toughen the takeovers bill with limitations not only on new investment but with provisions to repatriate foreign branch plants operating in Canada. The CIC once again stressed the equation between foreign ownership and control of the Canadian economy. This action was held

responsible for a public split in the Liberal party; by the second week of June, thirteen Liberal backbenchers, led by Mark MacGuigan, broke with party ranks on the issue and "called for much stronger and comprehensive controls" (Cunningham, 1972:5). In the face of an October 30 election, the Takeovers Bill was set aside for the new Parliament.

On January 24, 1973, the minority Trudeau government introduced Bill C-132, the Foreign Investment Review Bill. Introduced by Alastair Gillespie, Minister of Industry, Trade and Commerce, and a member with excellent nationalist credentials, the Bill was a strengthened version of its predecessor. It not only was to review takeovers of Canadian firms, but new investment proposals, as well as expansion by foreign businesses operating in Canada into areas unrelated to their existing activities. These changes were not only the result of the appointment of a more nationalist minister (Gillespie replaced Jean-Luc Pepin, who had been considered pro-business in the portfolio). The new situation in Parliament, with a Liberal minority dependent upon NDP support to remain in power, certainly altered the immediate political balance. Franck and Gudgeon argue as well that the heavy electoral losses of the Liberal Party convinced Trudeau that "economic

nationalism was a major force", if not throughout Canada, then in Ontario, where the Liberals had performed particularly poorly (1975:107'. The lesson learned seemed to be that foreign investment had to be discouraged in a manner more decisive than that implied by Bill-201, in the context of balancing the pressures coming from nationalist concerns with the laissez-faire preference of big business groups.

A summer of hearings before the Standing Committee on Finance, Trade and Economic Affairs saw the presentation of negative assessments by both nationalist and business groups. The strengthening of the bill, however, brought with it stronger opposition from business groups, and more moderate criticism from the CIC and CLC. The Canadian Chamber of Commerce, for example, concluded that "Bill C-132 should not be proceeded with in its present form", although it did significantly acknowledge the need for a mechanism which could prevent or limit foreign investments contrary to Canadian interests or objectives (Wolff, 1973:31/6). The Canadian Manufacturers' Association, for its part, was concerned with the future administration of the bill, and continued to emphasize the view that foreign investment was needed in Canada (Stevens, 1973:34/7). Ironically, the CMA argued that foreign investment

provided just those things -- research and development, technology, management skills, and export markets -- whose lack thereof had been identified in every task force report as the consequence of a high degree of foreign investment. Clearly, the CMA stood in strongest opposition to the assumptions that Canada had enough foreign investment, or that foreign investment had truncated Canadian economic development along a branch plant model.

Bill C-132 was approved by the House of Commons on 26 November and received Senate approval and Royal assent on December 12 1973. The first phase of the Foreign Investment Review Act came into effect by proclamation on April 9, 1974. The Foreign Investment Review Agency was born, with a mandate to review investment proposals related to the acquisition of existing Canadian businesses by foreign interests (the second phase, which reviewed proposals to create new businesses in Canada, either by new investors or by foreign interests already operating in Canada in an unrelated line of work, came into effect on October 15, 1975). On that same day, the Agency, created as anticipated in large part out of existing industrial expertise and administrative units within Industry, Trade and Commerce, received its first application for

approval of a takeover (Munton and Poel, 1978:232).

FIRA: INSTITUTIONAL STRUCTURE AND IMPLICIT ASSUMPTIONS

Schultz, Svedlove and Swinton (1980) have written perhaps the definitive assessment of FIRA as a bureaucratic structure. We will here briefly review some of their main arguments before entering into a discussion of the assumptions embedded within the Foreign Investment Review Agency. After all, the agency did not exist apart from its institutional location, and that role has implications for our assessment of the manner in which the state incorporated assumptions about Canada's place in the pattern of international investment flows.

It is important to note, first, that FIRA's role was to be completely advisory; officials would make their recommendation to the responsible Cabinet Minister, who would then advise the Cabinet. Schultz, Svedlove and Swinton have suggested that this was in order to closely supervise the politically contentious responses to foreign direct investments (1980:23-4). Other than its advisory role, it must be mentioned the FIRA was effectively politically isolated. As a stand-alone agency (rather than a part of Industry, Trade and Commerce, as had been envisaged in Bill C-201),

the resolution of the foreign investment question would have a high profile. Furthermore, as Shultz, Swedlove and Swinton have pointed out, a stand-alone agency had the distinct political benefit of acting as a "lightning rod drawing criticism away from the the real decision-makers, the Government, by becoming itself the central reference point in debates on the policies and process for reviewing foreign investment" (1980:21). As a small stand-alone agency, without the resources of the much larger departments, FIRA was institutionally subordinated, depending upon the information and evidence of the mainstream departments in order to come to its investment recommendations.

In addition to its marginal political location and its institutional subordination, FIRA was clearly limited as a nationalist tool by the stipulation of classes of investment which it could and could not review. As Molot and Williams have argued, FIRA was not to review "the most obvious means by which foreign control of the economy continues to grow, namely expansion, by subsidiaries, of existing plant capacity as well as their movement into areas of "related" business" (1984:89). The implications of not reviewing this investment were substantial; by the early 1970s, reinvestment of earnings from existing operations,

coupled with their borrowings from Canadian investors, accounted for roughly three-quarters of the increasing annual growth of foreign-held business assets (See Tables 3.7 and 3.9).

In preparing its recommendations for the Minister and Cabinet, FIRA's mandate provided for an evaluation of eligibility, of control, and of business "relatedness". FIRA was to review investment proposals involving more than \$250,000 in assets, and \$3,000,000 in annual revenues. The specification of these very low threshold figures effectively did not act to limit cases which would be subject to review, although it can be speculated that such low figures provided the Liberal government with further evidence, when such was needed, of its commitment to the regulation of foreign investment in Canada (Confidential interview, Investment Canada, Winter 1988). Once the dollar figure was met, FIRA further selected for review only those investment proposals made by non-eligible persons -- that is, citizens of foreign countries who were not Canadian landed immigrants, or if landed immigrants, had held that status for more than six years without becoming Canadian citizens. A corporation was deemed to be non-eligible if more than 5 percent of its voting shares were owned by a single non-eligible person, or if 25

percent of the voting shares of a publicly-traded company (40 percent in a private company) were owned by non-eligible persons in the aggregate (Gillespie, 1973:26/10). The Act recognized that the achievement of these percentages did not necessarily signify that a corporation was under foreign control, but placed the burden of proving otherwise upon the corporation rather than the government.

Acquisition of control, in the case of a takeover (mandated by the first phase of the Act to come into effect), was assumed to have happened if a non-eligible person or firm acquired more than 50 percent of the voting shares of a Canadian corporation, or substantially all of the property used in carrying on a business in Canada. Acquisition of less than 5 percent of the voting shares of a public corporation, or 20 percent of the shares of a private corporation, was not deemed in itself to be the acquisition of control of the corporation, and therefore was not subject to review. Acquisition of between 5 and 50 percent of the shares of a public corporation (or between 20 and 50 percent in the case of a private corporation), according to Gillespie's presentation to the House Committee on Finance, Trade and Economic Affairs, "raises a presumption that control has been acquired"

(1973:26/12). This presumption was open to rebuttal, but the burden of proof again rested with the corporation. The issue centred around the question of the non-eligibility of the person(s) seeking to make the acquisition, and proof as to eligibility would constitute rebuttal of the presumption of the acquisition of control.

Finally, when the investment review dealt with a new investment proposal rather than a takeover (phase II of the Act), the Agency needed to make a determination of the relatedness of the proposed business venture to the current economic activity (if such existed) of the firm submitting the application. If the firm was seeking expansion into a related business activity, the investment proposal would not be subject to review. Five separate factors were to be used in the determination of relatedness, including; vertical integration, direct substitutability, similarity of technology or production processes, output of research and development, and placement within the same governmental Standard Industrial Classification. To meet the criterion of relatedness, and thereby to obtain exemption from review, a firm needed only to fulfill one of these factors (Abdel-Malek and Sarkar, 1977:38).

Once reviewable investment proposals had been

identified, FIRA's mandate was to determine if investment plans were likely to be of "significant benefit" to the Canadian economy. While control of Canadian industry by non-residents had been assessed as the key problem, significant benefit was to be the method of solution. The Act itself acknowledged this. Its preamble officially states that it was enacted "in recognition by Parliament that the extent to which control of Canadian industry, trade and commerce has become acquired by persons other than Canadians and the effect thereof on the ability of Canadians to maintain effective control over their economic environment is a matter of national concern..." (s 2.1). In response to this national concern, the Act sought to ensure that acquisitions and new business investments (including expansion into unrelated areas of current business) would only occur if these had been deemed to be or "likely to be of significant benefit to Canada" (s 2.1).

Significant benefit was to be assessed by an evaluation of the potential contribution of a particular foreign investment proposal to the Canadian economy in a number of areas; including prospects for increased employment; the extent of new capital investment; the extent of resource processing; the utilization of Canadian parts, components and services; the

maximization of exports from Canada; the maximization of sourcing from within Canada; Canadian participation as shareholders, directors, or managers; the effect of the investment on productivity, industrial efficiency, technological development, product innovation, and product variety in Canada; the likely beneficial impact on competition; and the compatibility of the proposed investment with industrial and economy policies (Pryde, 1984:181-91). These criteria of significant benefit reflect precisely the concerns of the branch plant economy. They underline the extent to which the state had accepted the diagnosis of Canada's position in the international economy, rather than, for example, underlining the more conservative (or pro-business) concerns evident in the Watkins Report over the extraterritorial application of foreign laws. The criterion of "significant benefit" itself was widely decried by business and opposition members as being "an intrusion into the normal economic decisions of a company" and thus "open to abuse" (Ruben, 1973:30/58), "largely subjective," as well as "fuzzy and ill-defined" (Schultz, Swedlove, and Swinton, 1980:27-8). Gillespie in fact acknowledged that the guidelines were general, but argued that, through the experience of specific cases, a body of more precise guidelines would be built

up. The Minister conceded that he hoped eventually to be able to publish these resulting guidelines (Gillespie, 1973:26/7). Despite the recognition that "significant benefit" could prove unclear for those administering the guidelines, Parliament made no attempt to make the criteria more specific.

FIRA embodied selected aspects of the perception of Canada's position in the international economy contained in the government reports on the problem of foreign direct investment. On the one hand, state managers continued to be disposed toward foreign investment; the agency was hardly restrictive in scope given that it did not regulate the expansion of existing investments (despite the Gray Report's assessments that most growth in foreign investment in Canada was occurring through the reinvestment of earnings). The state had, however, accepted a notion of its position as the recipient of truncated and miniature replica investment, and as a location in which resource extraction was conducted without any attendant processing. FIRA's criteria of benefit reflected the state's perception of its place in the global economy. New investors were to be encouraged to process resources, to maximize exports, to pursue backward and forward linkages in Canada, and to conduct research and development activities. Existing

investments, however, were to be largely left untouched; which was only a partial response to the branch plant critiques of the Gray Report and the CIC.

FIRA was widely criticised: for its failure to regulate all foreign investment (existant as well as incoming); for its placement of the burden of proof of criteria such as eligibility and control, or significant benefit, on the applying firm rather than the government; for its failure to come to grips with the problem of extraterritoriality which had been addressed by Reports starting with Watkins [9]; for its failure to provide any mechanism for disclosure of the reasons for acceptance or rejection of an investment proposal; for the vagueness of its guidelines and the resultant perception of the possibility for abuse; and for its insistence that significant benefit, rather than likely detriment, form the basis of the guidelines which would determine a proposal's acceptability. These criticisms were primarily made by representatives of Canadian capital, the Canadian Manufacturers' Association and the Canadian Chamber of Commerce. Neither of these organizations, as we have detailed, were as vociferous in their opposition to review provisions as the CIC was in defending a broader interpretation of them, and the criticisms of Canadian capital in the early days of FIRA

continued to be muted. It is only necessary to examine the criticisms directed toward the new Agency, however, to realize the extent to which this was truly a regulatory tribunal born of compromise.

The creation of FIRA, while certainly a symbol of the nationalist cause in Canada, did not in fact represent a true break with the continentalist orthodoxy which had governed economic planning throughout most of the previous century. FIRA's intent was never to restrict investment coming to, or expanding within, Canada. The Agency embodied in its legislative mandate a positive orientation to the presence of foreign investment in the country. It welcomed such investment, seeking only, through negotiation with the investing firm, to secure greater benefits for the Canadian economy. It neither sought to restrict, nor monitor, foreign investment in a manner which would have satisfied either the Committee for an Independent Canada, or the (by then disbanded) Waffle. It underlined a clear belief that Canada would remain as attractive to foreign investors as it had always been -- and that the state could afford to negotiate with investors without affecting its attractiveness.

The creation of the Foreign Investment Review Agency represented, in the end, a new assessment by

Canadian state managers of Canada's location in the pattern of direct foreign investment. While foreign investment was seen to be a positive force, its benefits were no longer unquestioned. The legislation had firmly identified Canada as the recipient of branch plant investment, with its negative as well as positive consequences. With a strengthened mandate (over Bill C-201), FIRA also re-emphasized state manager assumptions that Canada would continue to be attractive to new investment; attractive enough that prospective investors would be willing to submit to a regulatory process. Of course, this assumption was helped by the growing regulatory recourse to which other states had turned in their resolution of foreign investment problems (see Safarian, 1983, for example). Finally, in its choice of a regulatory framework, state managers implied that Canada had enough foreign investment -- that it did not need to curry favours for additional investment dollars.

We will recall that Chapter One argued that state managers would turn to domestic interpretations of their country's location within the international economy when the international norms governing economic transactions began to breakdown, and thus become re-politicized. As well, we argued that state managers could gain such

interpretations from extra-bureaucratic sources of information, as well from traditional bureaucratic sources. It is interesting to note, for example, that the Department of Finance provided the main evaluation of foreign investment as necessary for balance of payments reasons (Schultz, Swedlove and Swinton, 1980:19), an evaluation which was not represented in any of the Reports completed on the issue of foreign investment, or in any of the concerns raised by representatives of Canadian capital. Of the interpretations presented to Canadian state managers, FIRA comes closest to articulating the assumptions of the Committee for an Independent Canada, and through it, the nationalistic (Ontario) new middle class. State managers did not reflect those assumptions as in a mirror, however; the limits of the historical position of the Canadian state as a capitalist state made it difficult to adopt the extensive regulatory initiative proposed in the Gray Report and supported by the CIC.

The difficulty with the creation of the Agency, of course, was that investment patterns were beginning to change -- as we noted earlier. Responding to the Gray Report and the CIC's diagnosis of the branch plant problem, state policy was now best suited for the negotiation of a new, more innovative, manufacturing

branch plant. Unfortunately, manufacturing investments to Canada were decreasing in favour of expanded resource investments, and manufacturing investments were becoming more concentrated -- exacerbating, and not resolving, the problem of lack of Canadian economic control. These problems were probably unavoidable, for these trends were occurring simultaneously with the creation of the Agency. Still, they point to the root of some of the problems with FIRA.

Learning does not occur in a vacuum, no more for state managers than for anyone else. The adoption of the Foreign Investment Review Agency in response to new interpretations of Canada's position in the global economy did not signify that the issue was dealt with, that state managers would never be challenged to "learn" even newer interpretations. As we have suggested through this chapter, and as we have clearly seen in Chapters Two and Three, ever changing international investment strategies were inevitably going to be represented anew to state managers. Chapter Five will detail the process of re-interpreting Canada's international investment location in the post-FIRA era.

ENDNOTES

- [1] This is not to say the Diefenbaker was unsympathetic to nationalist concerns. Diefenbaker was in fact suspicious of the extent of Canadian links to the United States, and focussed a good deal of his election campaign on expanding trade with the United Kingdom at the expense of Canadian trade with the United States. As with Mitchell Sharp's Third Option, however, Diefenbaker was not able to translate his preferences into concrete policy initiatives, and trade links between Canada and the United States continued to grow.

- [2] Projects included the development of the St. Lawrence, the development of hydroelectric power in British Columbia, the exploitation of resources in the Yukon, and the distribution of western oil and gas.

- [3] Philip Resnick has provided a tongue-in-cheek, yet insightful, assessment of the precise "place [of] the Canadian big bourgeoisie, indigenous and branch-plant ... in the international capitalist economy" in his reporting of the caption accompanying a picture published in the CMA's resume of its 100th annual meeting in 1971. "When the President of the United States, Richard M. Nixon, came to New York City in December 1970 to speak to the National Association of Manufacturers, CMA President A.G.W. Sinclair was seated fifth on the President's right" (Resnick, 1977:154-5).

- [4] Moore's enthusiasm for measures to return business operating in Canada to Canadians was certainly very public. As Courtney Tower reported for Maclean's, Moore "talks of foreign firms siphoning off profits that should feed Canadian social needs, of talented Canadians leaving communities when the challenges are moved south. Moore would like frankly tough policies against foreign ownership, as well as incentives and protection for Canadians" (1970:5). Philip Resnick has questioned Moore's nationalism, however, remarking that Brascan's "track record in Brazil was substantially worse than that of most multinationals in Canada" (1977:156).

- [5] The Report rejected the review of new investments by foreign firms operating in Canada into current economic activities -- such as additions to

capacity. It rejected such review because it would interfere with a firm's use of retained earnings, would represent a fundamental change in the "rules of the game" of doing business in Canada, would politicize the market by introducing government's administrative judgement, would potentially create problems in relations with foreign governments, and could, over the long-run, "make Canada a less attractive location for investment" (Gray Report, 1972:470). Review of investments by an existing foreign-controlled firm into a new line of business was recommended because such investment "has almost all the characteristics of a new investment by a foreign controlled company not yet established in Canada" (Gray Report, 1972:471).

- [6] The Gray Report also provided suggestions as to the factors which a review agency would need to take into account in making its recommendations on investment proposals. These factors included the nature of the investor's product lines; the nature of the relationship (particularly managerial) of the subsidiary to its parent and its other international affiliates; the nature of the technology to be employed; the plans for research and development and product innovation to be conducted in Canada; export markets available to the Canadian subsidiary operation; plans for sourcing within Canada; plans for subsidiary expansion; plans for the hiring of Canadian managers and employees, and the appointment of Canadian directors; the source of financing; the opportunity for equity participation by Canadians; and the degree of processing of resources to be done in Canada (Gray Report, 1972:455-56).

- [7] The Select Committee on Economic and Cultural Nationalism of the Ontario Legislative Assembly had in fact presented its own report on the questions of foreign investment, recommending, among others, that measures should be taken to control the sale of Canadian firms "where no public benefit would result from foreign ownership" (Fayerweather, 1974:174).

- [8] Stevenson's survey of provincial elite (governmental) attitudes reveal that support for foreign ownership restrictions varied across provinces. Support for restrictions, with note of government in power, was divided as follows:

Newfoundland (PC)	23.5%
Prince Edward Island (L)	33.3%
Nova Scotia (L)	22.2%
New Brunswick (PC)	15.0%
Quebec (L)	31.8%
Ontario (PC)	62.2%
Manitoba (NDP)	73.9%
Saskatchewan (NDP)	75.8%
Alberta (PC)	40.7%
British Columbia (NDP)	75.0%
(Stevenson, 1974:640)	

The Atlantic provinces, as well as Quebec, expressed worry that restrictions against foreign investment would affect job creation prospects in their regions. By 1974 however, Quebec had conducted its own report calling for guidelines and restrictions upon foreign investors (Rose, 1974). Ontario, as the centre of both the Waffle and the CIC nationalist movements, had clear interests in restrictions (despite a Progressive Conservative government). Manitoba, Saskatchewan, and British Columbia, with the NDP in power, had governments long committed to measures for the Canadianization of the economy. Alberta's opposition to regulations was tempered by its own desire for high local content levels (Molot, 1984:174).

- [9] Perhaps ironically, the Canadian Labour Congress placed most emphasis on the failure of the Agency to deal with concerns over the extraterritorial application of foreign -- virtually exclusively American -- laws through subsidiary firms operating in Canada (Macdonald, 1973:35/4). The CLC thereby shared the one concern most consistently mentioned by pro-business analysts (Safarian, for example); the one major problem with foreign direct investment was not the structural problems which it might create in a host economy, but rather the difficulty which might through it be encountered as a result of the application of home country laws. This critique was completely consistent with the continentalist perspective on foreign investment.

CHAPTER FIVE

FOREIGN DIRECT INVESTMENT AND THE CANADIAN STATE: POLICY-MAKING INTO THE 1980S

On June 6, 1985, the Canadian House of Commons passed the Investment Canada Act, and replaced FIRA with a new Agency. Less than ten years after FIRA had come into full operation, it was no longer part of the Canadian political landscape. The continentalist political agenda of the Mulroney government appeared to have overcome the nationalist values which gave rise to FIRA. This chapter will argue that the change to an "investment promotion" agency from a regulatory one in fact predated the Conservative Party victory of 1984 and the subsequent creation of Investment Canada. The FIRA of 1984, an agency which by then had undergone a number of revisions, was not particularly different in tone, if somewhat more stringent in guidelines, than the new "Open for Business" Investment Canada. Making this argument, however, requires that we continue to trace factors which influence state manager learning, for it appears that the nationalistic political leaders of the Liberal Party learned much the same information with respect to foreign investment as the most continentalist Conservatives.

Through the whole debate on foreign direct investment in Canada, two things stand out as

particularly noteworthy. To begin, the debate proceeded very much under the assumption that the established pattern of investment in Canada -- resource-extractive and manufacturing branch plant -- would never change. After decades of this form of investment, this failure to consider that new realities might be emerging may not be so surprising. Still, the only official discussion of the changing patterns of investment already underway in the global economy took place in the Gray Report, which acknowledged that some multinationals were "rationalizing" their subsidiaries, but which commented that Canada could not expect this process to change the nature of investment in Canada, given the presence of the Canadian tariff. As we know from Rugman's 1987 study of inter-firm trade in Canada, by the mid-1960s Canadian subsidiaries were already becoming integrated with parent production in the United States; at least some of these were doing more than supplying the home market. The only other source of sustained criticism of a stagnant view of Canada's location in the international political economy came with the deindustrialization thesis promoted by the Waffle, which while wholly unsuccessful politically, did recognize the emerging internationalization strategies of multinational firms. When considered in a global

perspective, FIRA reflected a preoccupation with investment patterns of the 1950s and 1960s rather than the emerging patterns of the 1970s, a reality which these last two chapters will begin to explore.

The creation of FIRA, as we have seen, had much to do with the perception, filtered through the new middle class, and predominantly held by political state managers such as Herb Gray and Alastair Gillespie, that there were negative consequences to a branch plant pattern of economic development. The process which led to the creation of Investment Canada, however, at least implicitly questioned the importance of that view. Emerging through the transition from FIRA was a new view -- one which focussed on Canada as home to competitive multinationals rather than as host to branch plant subsidiaries. Once again, we will find our explanation for this transition not only in agency but in state manager learning by examining both the international system and the role of domestic class actors. In particular, we will focus on the rise and changing nature of Canadian (MNC) business interests, which occurred both in response to changes within the Canadian economy and within the international economy. This change in the role of Canadian capital, along with emerging MNC strategies as discussed in Chapter Three,

fundamentally altered Canada's location within the pattern of international direct investment flows. As well, we will look at the reasons for the decline in the Ontario-centric new middle class as a force cohesive enough to sustain national concerns about foreign investment and political concerns about the negative consequences of the branch plant economy.

This examination of the broader structural factors influencing state manager learning is not intended to deny the importance of the political in shaping decisions. We have already discussed the difference in learning between political and bureaucratic state managers, with the latter more likely to develop a long-term (and organizationally contingent) view of the "national interest", and the former more likely to respond to societal pressures which do not find representation in bureaucratic structures. We have already seen this process at work in the FIRA decision, with political leaders such as Herb Gray and Alastair Gillespie more sensitive to the concerns of the new middle class, and Departments such as Finance and Industry, Trade and Commerce more responsive to their traditional concerns about balance of payments. A focus on structures, though, makes the argument that the narrowly defined political (which political party is in

power, for example) is not as decisive for questions like direct foreign investment as are underlying domestic and social changes, and the relationship of the Canadian economy to the global pattern of direct foreign investment.

FIRA: CRITICISMS AND COMMENTARY

It is unsurprising, in an Agency which reflected the branch plant assumptions of the Central Canadian new middle class, watered down by the concerns of capital and the insistence on transparency by bureaucratic state managers of Finance and ITC, that FIRA was not widely praised. Detailing the reactions of both the Committee for an Independent Canada and representatives of Canadian capital provides us with information as to the nature of each group's assumptions about Canada's place in the world economy, and allows us to trace the influence of each upon the evolving interpretations of Canadian state managers. Also important to note, however, is the fact that FIRA was simply not an issue on the public agenda -- a point of some significance in and of itself. Let us examine both these phenomenon.

The Foreign Investment Review Agency was perceived to be an unsatisfactory government initiative by both business interests and the economic nationalists of the

Committee for an Independent Canada -- the central Canadian new middle class. As we began to trace in Chapter Four, the business community, while privately critical, publicly acknowledged the right of the Canadian state to legislate the regulation of direct foreign investment. Some business leaders even went so far as to accept that "[t]here will be times when the interest of the subsidiary will differ from that of the parent" (Thomson, 1972:10). Even U.S. business interests, testifying before a committee of the U.S. House of Representatives in anticipation of the Foreign Investment Review Agency, commented that there could be "great advantages for American businessmen to have an organization to which they could address themselves, from which they can receive authoritative advice to help decide whether they want to do business in Canada" (Thomson, 1971:39).

Even prior to the enactment of the FIRA legislation, we can note capital's distance from the issue. In March of 1973, for example, the Canadian Chamber of Commerce and the Canadian Manufacturers' Association put together a compendium of business viewpoints on national industrial strategy, submitted to Alastair Gillespie, the Minister of Industry, Trade and Commerce, and the minister who introduced the FIRA

legislation. The compendium included eleven briefs from separate business organizations to the Minister, as well as an industrial overview discussion from the CMA and the CCC. The briefs were from groups as diverse as the Canadian Export Association, the Mining Association of Canada, the Pharmaceutical Manufacturers Association of Canada, and the Machinery and Equipment Manufacturers' Association of Canada. They represented sectors dominated by Canadian firms (such as the Air Industries Association of Canada) as well as by multinationals (Pharmaceuticals, the Electronic Industries Association of Canada). They represented manufacturing, service, and resource industry groups. Interestingly, only one association (the Air Industries Association) made any mention of the issue of foreign ownership and of state interest in the regulation of foreign investment, and then only to say that its brief would not deal with the issue, but that it acknowledged that the government was concerned (Canadian Chamber of Commerce, 1973:51). In Gillespie's response to the compendium, delivered in a speech to the CMA's annual meeting in June 1973 (precisely when the committee hearings into Bill C-132 were taking place), the specific issue again does not emerge. Gillespie does cite as a target of industrial development the government's commitment "[t]o provide

for greater domestic control of the Canadian economy and its future industrial development of Canadians for Canadians" (1973b:4), but no mention is made of the soon-to-emerge FIRA.

In part, this lack of attention may be attributable to FIRA itself. FIRA's mandate was so vague that business leaders could contest the philosophy of state intervention, but were hard-pressed to identify the likely damaging consequences of the Agency. Of equal importance, there is no evidence that business was prepared or able to offer a view of Canada's location in the pattern of foreign investment which fundamentally challenged the branch plant contention of the new middle class. The greater part of business briefs on Bill C-132 ask for clarification -- how to define significant benefit, or non-eligible persons -- rather than for justification. Because of this vagueness as well, particular segments of capital were unlikely to identify any features of the initiative which they could wholeheartedly support. A lukewarm response was the state's best case scenario with FIRA. The nationalist movement, for its part, was not as content to adopt a similar "wait and see" attitude to the Agency.

The Committee for an Independent Canada was intent upon strengthening the provisions of the Foreign

Investment Review Agency. As John Trent had testified before the House of Commons Finance, Trade and Economic Affairs Committee's hearings on Bill C-132, the Committee for an Independent Canada could only support the bill with grave misgivings. "We would support the passage of this bill as a small step toward Canadian economic independence rather than have no legislation at all," Trent argued, but the bill is itself too weak and is "unaccompanied by the positive measures for the stimulation of Canadian enterprise which our Committee has long maintained must accompany efforts to control foreign investment" (1973:34/49). The CIC's newsletter, The Independencer, put the case more strongly, asking if Bill C-132 was nothing but a smokescreen designed to prevent the Canadian public from perceiving that "no determined effort" was being made "to achieve a reasonable degree of economic autonomy for Canada" (The Independencer, July 1973:1).

In order to help redress some of the perceived inadequacies of the legislation, the C.I.C. was championing a document before the Liberal caucus outlining a strategy to achieve 75 percent Canadian ownership of all foreign-owned companies within a decade. For the CIC, there was a straightforward assumption that Canadian ownership would imply greater

control over the economy, and that control could not be achieved without ownership. As we argued in Chapter Two, however, the equation is not always that simple; multinational firms can continue, through licensing arrangements, through their monopoly of marketing information, through their control over export markets, to exert control even without ownership.

In fact, the Committee for an Independent Canada increasingly identified ownership and control as synonymous concepts. The state should, in effect, begin to nationalize foreign firms in order to transfer these to Canadian ownership. If ownership of branch plants and resource companies were transferred, Canada would de facto have a mature, industrial economy. For the Committee, the key problem was one of independence; a branch plant structure meant that decision-making had been shifted "outside this country to the head offices of these multinational corporations" (Rotstein and Lax, 1972:x). Most accepted Walter Gordon's contention that there should be a gradual process of "buying back" ownership, and therefore, control, particularly of the larger foreign firms operating in Canada (Gordon, 1972:72).

Despite efforts to encourage the Liberal Party to promote strategies of Canadianization, Mel Hurtig, as

co-chairman of the CIC, was clearly discouraged by what appeared to be the real limits to which the Liberal party would adopt the cause of economic nationalism.

"All the evidence suggests that the faction supporting the plan [for 75 percent ownership of the Canadian economy] is losing the struggle going on within the party" (Partridge, 1974:1), a pattern which had been apparent in the nature of the debate within caucus over any regulation of foreign direct investment, which was consistent with the traditional laissez-faire market orientation of the Liberal party, and the pro-business orientation of the Departments of Finance and Industry, Trade and Commerce. The screening of new investment or of the acquisition of Canadian companies could be tolerated out of political necessity, but proposals to nationalize existing foreign investment went much further than that.

The summer 1974 election did little to convince anyone that foreign investment review should be strengthened. Only rarely did coverage of the election lament the lack of attention paid to the issue of foreign investment.

For the second time in twenty-one months a federal election will be held apparently without the issue of foreign ownership considered a priority by any of the four party leaders. Just as no other nation in

the world would have tolerated the sellout of the country as Canadians have, similarly no other country would allow their politicians to so completely abdicate their responsibilities. Sadly, despite all of our activities to date, "silent surrender" still best describes Canada in 1974 (Mel Hurtig, as cited in Fulford, 1974:8).

Robert Fulford, editor of Saturday Night magazine, felt compelled to decry the failure of economic nationalism in Canada. "Behind us are millions of words, hundreds of articles and speeches, dozens of books, and ... what?," he wrote. "A mainly useless piece of legislation..." (1974:8). The nationalist movement spearheaded by the new middle class interests of Central Canada may have created a "certain change in national mood" (Fulford, 1974:8), but it certainly did not perceive that it had done much to change the extent of foreign investment in Canada, or to change Canada's status as a dependent country which must regain its independence.

The election campaign of 1974 provides some insight into the nature of the issue of foreign investment in Canada as the country was entering the mid-1970s. As Hurtig's lament suggests, foreign investment was simply not a question for most Canadians. Even The Financial Post observed that "all three major parties have been

avoiding the great nationalist debate like the plague
.... [A]t this stage in the campaign, at any rate,
foreign-ownership issues are seen by some party
strategists as a kind of political doomsday machine"
(Partridge, 1974:1). The forces of economic
nationalism, which had "won" the political debates of
the early 1970s (at least to the extent that an Agency
was created), no longer seemed very successful at having
their concerns articulated by political state managers
[1].

In seeming contradiction to the absence of foreign
investment as an election issue, Gallup reported that
positive assessments of U.S. investment in Canada had
reached an all time low in 1974. Gallup findings
revealed that the percentage of Canadians willing to
consider U.S. investment as a "good thing" for the
Canadian economy had declined through the early 1970s,
reaching a low of 45 percent in the election year, from
65 percent in 1970 (LeDuc and Murray, 1984:133). Munton
and Poel's analysis of the 1974 campaign helps to place
Gallup's findings in better perspective, concluding that
while foreign investment may have been an issue to
elicit negative sentiment, the intensity of feeling on
the issue was low. Other issues -- inflation and
unemployment among them -- were of far greater

significance [2].

The Committee for an Independent Canada: Life after FIRA?

The failure of foreign investment to play any role in the 1974 election may be due to a number of factors. Foreign investment was dominated by other concerns. Foreign investment appeared to have been dealt with in the creation of FIRA [3]. Party support on the issue was ambiguous, as Munton and Poel (1978) suggest. More importantly, however, the lack of electoral focus reflects upon the inability of the Central Canadian new middle class, and its implicit agency, the Committee for an Independent Canada, to broaden the basis of its support.

The Committee for an Independent Canada was more than a nationalist cause. It represented the interests of a class of people who defined their interests in terms of the de facto expansion of the Canadian state. State interventionism was to be the means of resolving the foreign investment question, just as state intervention had assisted in the creation of a large and viable post-secondary system, and a social welfare net. Both Mel Watkins and Robert Page, at various times chairmen of the CIC, had expressed a strong preference

for public ownership (rather than private Canadian ownership) as the means whereby the Canadian economy could be "Canadianized" (see Chapter Four). Economic interest, as much as nationalism, guided the principles of the CIC. As an organization representing the Ontario-based new middle class, these economic ambitions were quite viable. Public mistrust of Ottawa in Ontario is far lower than in other regions of the country. The CIC's "regional" class basis, however, was to pose problems for the permanence of its message.

The Committee for an Independent Canada was not an organization solely dedicated to the question of foreign investment regulation. A careful survey of its newsletter, The Independencer, reveals that other issues also occupied the group's attention: the use of Canadian written and published textbooks in schools, the dissemination of Canadian films, books and magazines, and most importantly, the question of energy self-sufficiency. The CIC had its own task force on energy, and since its inception had called for moves to return to Canadians control of the petroleum industry. For the CIC, the maxim "hewers of wood and drawers of water" had been replaced by "digger of uranium and pumper of oil" (Godfrey and Watkins, 1970:224).

Where the issue of foreign investment was

intrinsically vague, and the unspecific mandate of the Foreign Investment Review Agency could win it few friends, concern over energy was a widespread and specific issue. In February 1970, the Nixon administration released its "answer" to the problems of Third World nationalizations of U.S. energy resources. The Shultz Report, directed by Nixon's secretary of labor, George Shultz, recommended that safer stockpiles of oil be found -- and that the safest location for these was Canada. We have already discussed in Chapter Three how Canada maintained, and beyond 1970, in fact enhanced, its position as a supplier of resources to the United States. To emphasize the point, as Stephen Clarkson has detailed, in U.S. eyes Canadian resources were considered to be completely part of U.S. territory; as the President of the U.S. National Coal Association testified before the U.S. Senate, "our government considers Canada our own for energy purposes" (Clarkson, 1985:60).

These plans had greater relevance once the Arab members of the Organization of Petroleum Exporting Countries (OPEC) increased international oil prices four-fold and imposed a partial oil embargo. The Canadian state was totally unprepared (as was most of the western world) for the OPEC crisis -- in part, as

Toner and Bregha have identified, because the state had no information on which to base policy. Donald Macdonald, the Minister of Energy, Mines and Resources, was forced to acknowledge that "one of the difficulties facing the Canadian government is that it is virtually dependent on major international companies for its sources of information" (Cited in Toner and Bregha, 1984:116). The oil industry had apparently overestimated the extent of known oil reserves in Canada, raising fears that Canada would face a shortage on par with the energy crisis in the United States. More importantly, however, the industry's failure to provide accurate information to the Canadian state caused the bureaucratic structure to lose confidence in the control exercised by foreign multinationals over the industry. This undermining of the credibility of these MNCs made it easier to begin to contemplate alternative solutions. With the CIC suggesting that ownership equalled control, and with a bureaucratic structure unable to suggest any course of action for lack of information, the seeds of a more nationalistic policy were laid. In 1973, faced by the fear of Canadian oil shortages, frustrated by the often inaccurate information provided the state by the oil multinationals and needing a source of such information, under pressure

by the U.S. government to continue the process of continentalization of Canadian energy resources, and in a minority government situation, the Liberal government announced a new oil policy, which included among its provisions the creation of a public oil company.

The connection between ownership and control -- with ownership as the means of ensuring control -- was raised again during the 1974 summer election. Even the Committee for an Independent Canada, while pushing for the inclusion of the issue of U.S. control over the Canadian economy in the federal election, targeted more specifically provisions related to the Canadian ownership of oil and gas resources (Irvine, 1975:46). On July 8, 1974, the Liberals released an election policy paper which suggested that Canadians should gain a "greater say in their economic future". Prime Minister Trudeau, in answering press questions about the policy, said that new federal investment initiatives would be based on the premise that "natural resources are the underpinning of our whole economy", and that the future Liberal government would seek to achieve 50 to 60 percent Canadian ownership in major new resource projects (Globe and Mail, July 9, 1974). This announcement went a small way towards attenuating the CIC's demands for 75 percent ownership of all major

industries. The short-term implication of this policy was the creation of Petro-Canada in January, 1976.

FIRA, as we have seen, had a broad, cross-industry mandate. It was to review a whole range of investment proposals. As such, its potential to offend a group or sector was great, while the vagueness of its mandate guaranteed that it was unlikely to generate considerable sympathetic reaction. Petro-Canada, while still a symbol of state intervention, was sectorally targetted at a time when frustration with foreign firms operating in that sector was high, so that reservations about intervention were lower. As well, because of its specific role, Petro-Canada could find supporters; not only within a sympathetic public, but also within the bureaucratic structure. Officials of Energy, Mines and Resources, for example, saw the creation of the oil company as a means of extending their power within the bureaucratic structure (Toner and Bregha, 1984:117). FIRA was responding to a more general problem and based on a more general perception of that problem -- its ability to find strong adherents was more limited.

The CIC advocacy of energy self-sufficiency was sustained with the creation of Petro-Canada in a way in which its advocacy of foreign investment regulation was not with the creation of FIRA. It began to target other

energy-related programs: a comprehensive energy policy, a restriction in the extent of Canadian energy exports, a reduction of Canadian dependence on foreign energy sources, and a restriction in the development of the James Bay project and the Mackenzie Valley oil and gas pipeline project so that they not be developed to serve foreign needs (The Independencer, 1979:6-8). In fact, after 1977, detailed articles on foreign investment disappeared from its newsletter, while discussions of energy began to dominate.

The members of the CIC had two observations to make about Canada's location in the international political economy. As we have seen, its conclusion that Canada was a branch plant economy was incorporated, although watered down, in the criteria of significant benefit utilized by FIRA. Further, however, the CIC wanted to alter Canada's location as resource supplier to the United States, and advocated the development of a Canadian energy policy to meet exclusively Canadian demands. As Chapter Three has discussed in its brief sectoral review of foreign investment, the CIC's contentions as to resource industries were correct through the 1970s, but its observations about manufacturing investment were not. In terms of investment flows, the branch plant economy was changing,

but the resource grab was ongoing. The CIC would periodically remind policy makers that foreign investment remained a problem (by virtue of its numbers, which translated into ownership, and therefore, by their analysis, directly into control), and it usually did so by reflecting upon the erosion of the implicit international investment regime. Canada could strengthen its foreign investment regulations because other countries had done so (The Independencer, 1977:1).

Once its "victories" in the creation of FIRA and Petro-Canada were behind it, the Committee for an Independent Canada began to be plagued with declining membership. Its own attempt to evaluate the reasons for this decline is instructive. They suggested, for example, that the increase in issue-targetted nationalist groups (e.g. the Canadian Publishers Association) had drawn some members away to work on issues of more specific concern to them. Secondly, they implicitly contended that they had never been very successful in keeping the issue of foreign investment in the public eye, allowing Canadians to believe that "the problems of foreign ownership are not so severe as they were" (The Independencer, 1980). Finally, though, the CIC acknowledged that it had never been able to break out of the regionalism of its Ontario-centric, new

middle class position. The CIC argued that the regions, preoccupied with territorial jurisdiction and inherently anti-establishment ("the establishment being regarded as the tax collector who lays some claim on the property"), always perceived the CIC to be establishment. With its focus on Canadian state solutions to the challenges of economic development, this is hardly surprising.

The CIC gradually ceased to be an important force in influencing Canadian policy and in shaping state manager perceptions. Without a doubt, however, the creation of the Foreign Investment Review Agency stands as a tribute to the influence of the CIC, and its ability to place the branch plant issue on the political agenda. The CIC's failure to keep foreign investment in the public eye had more to do with the changing conditions of Canada's domestic economy than it did with the shortcomings of the Agency, however, and it is to the task of establishing an outline of those conditions that we now turn. Doing so will allow us to assess the evolution of the Agency in light of the economic and policy environment in Canada throughout the 1970s and into the early 1980s.

Canadian Economic Profile

We have earlier remarked that inflation was a major

concern of the Canadian electorate in 1974, and indeed, as with most OECD countries, the double-edged sword of inflation and unemployment dogged Canadian policy makers through the period of FIRA's operation (See Appendix II, Tables II.1 and II.2). As a whole, the economy experienced a mild recession in 1974-1975, and a slowdown in 1980 which led to the deep recession of 1982 (See Appendix II, Table II.3). The years 1971 through to early 1974 had seen a period of economic expansion in Canada. Not surprisingly, this is the period during which debates about foreign investment were at their most intense, supporting contentions by many students of Canadian foreign policy that negative assessments of Canada's bilateral relationship with the United States are more likely in times of relative prosperity (see Dolan and Tomlin, 1984, for example). The year 1974, however, saw the fuelling of inflation (although not as severely as for most other OECD countries), and a decline in foreign demand for Canadian exports, born of stagnant or declining aggregate world demand, diminishing Canada's merchandise trade surplus. Despite this, overall position on the balance of payments (current and capital accounts) remained good (See Appendix II, Table II.4), largely through a particularly strong inflow of portfolio investment. By 1975, unemployment (which had

been dropping through the early 1970s) reacted to the economic slowdown with a significant increase (from 5.3% in 1974 to 6.9% in 1975).

Canada was able to weather the international recession of the mid-1970s "much better" than most other OECD countries (OECD, Canada, 1977:5). In part, this was the result of resource factor endowments which partially mitigated the impact of the OPEC oil shocks, and compensated slightly for the decline in Canada's manufactured exports. From 1976 to the economic slowdown of 1980, the Canadian economy had settled into an uneasy pattern. Inflation rates averaged between 7.5 and 9.2 percent, unemployment rates vacillated around 7.5 percent, and the annual increase in real GNP remained around 3 percent. Canada continued to run a persistent deficit on its current account, counterbalanced by an equally persistent and larger surplus on its capital account. The current account deficit was fuelled by a mounting increase in the deficit on interest and dividends -- the costs of servicing the Canadian debt increased sharply through this period. On the other hand, the continued fall in the value of the Canadian dollar (reaching a low of U.S. \$0.832 in the first two months of 1979)[4], together with upward pressure in world commodity markets, helped

improve Canada's performance in merchandise trade. Canadian export performance thus improved in a full range of raw material exports -- wheat, petroleum, natural gas, petroleum products, metals and minerals (CALURA, 1981:16). As well, the economic recovery in the United States between 1976 and 1980, while sluggish, stimulated housing starts (and thus demand for Canadian lumber) and automobile production (and thus Canada's contribution through the Auto Pact)[5].

John Curtis (1985) has argued that this pattern of post-1975 economic recovery implied that few fundamental adjustments in the structure of Canada's economy were necessary. This perception was built around the fact that the area in which Canada was traditionally strong -- raw material production -- continued to contribute to a Canadian merchandise trade surplus:

With a relatively comfortable balance-of-payments situation, and with a strong and growing government sector, economic policy attention in Canada during this period focused less on economic growth than on the distribution of income, as well as on inflation and those policies thought best to control it" (Curtis, 1985:23).

The performance of the resource sector from the mid-1970s to the end of the decade helped emphasize the historical sectoral orientation of the Canadian state on the more specific question of foreign ownership. In

many respects, it can be hypothesized that had the export of resources not bolstered the Canadian economy, the state might have endeavoured more systematically to seek to address some of the longer term structural problems identified in the foreign investment debate; precisely the point implied in John Curtis' earlier observation.

THE EVOLUTION OF STATE MANAGER PERCEPTION: CHANGES IN FIRA

The relative stability of the Canadian domestic economy in the late 1970s, particularly as compared to other OECD economies, did not act to specifically re-politicize the issue of foreign investment until the 1980s. This did not imply, however, that the new "knowledge" of some state managers about the consequences of direct foreign investment and the branch plant economy would simply wither away. In fact, the first significant "post-FIRA" development among Canadian state managers lay with Industry, Trade and Commerce's July 18, 1975 release of the criteria for good corporate citizenship, a document entitled "Principles of International Business Conduct", but more widely known as the "Gillespie Guidelines". Like the Winters guidelines of a decade earlier, they proposed that

multinational firms operating in Canada meet their obligations to foster a vibrant and innovative Canadian industrial climate. Gillespie had been profoundly influenced by the Committee for an Independent Canada, and had called for stringent measures to control foreign ownership, including ceilings and freezes on ownership, a takeover prohibition to cover larger Canadian companies, and a plan to Canadianize selected enterprises operating in Canada (Godfrey and Watkins, 1970:248-50). As such, he went much further than Winters had in the release of his suggestions. When they were tabled in the House of Commons by Gillespie, he announced that they were introduced to reflect "broad government policy regarding the activities and responsibilities of foreign controlled business enterprises in Canada", and that they were to "provide an added indication of the sort of benefits the Government looks for in assessing investment proposals under the Foreign Investment Review Act".

The Gillespie Guidelines requested that foreign-controlled enterprises operating in Canada attempt to comply with certain principles of "good corporate citizenship". These were as follows:

- a) pursue a high degree of autonomy in the exercise of decision-making and risk-taking functions, including innovative activity and the

marketing of any resulting products;

- b) develop as an integral part of the Canadian operation an autonomous capability for technological innovation, including research, development, engineering, industrial design and pre-production activities; and for production, marketing, purchasing and accounting;
- c) retain in Canada a sufficient share of earnings to give strong financial support to the growth and entrepreneurial potential of the Canadian operation, having in mind a fair return to shareholders on capital invested;
- d) strive for a full international mandate for innovation and market development, when it will enable the Canadian company to improve its efficiency by specialization of productive operations;
- e) aggressively pursue and develop market opportunities throughout international markets as well as in Canada;
- f) extend the processing in Canada of natural resource products, to the maximum extent feasible on an economic basis;
- g) search out and develop economic sources of supply in Canada for domestically produced goods and for professional and other services;
- h) foster a Canadian outlook within management, as well as enlarged career opportunities within Canada, by promoting Canadians to senior and middle management positions, by assisting this process with an effective management training program, and by including a majority

of Canadians on boards of directors of all Canadian companies, in accordance with the spirit of federal legislative initiatives;

- i) create a financial structure that provides opportunity for substantial equity participation in the Canadian enterprise by the Canadian public;
- j) pursue a pricing policy designed to assure a fair and reasonable return to the company and to Canada for all goods and services sold abroad, including sales to parent companies and other affiliates. In respect to purchases from parent companies and affiliates abroad, pursue a pricing policy designed to assure that the terms are at least as favourable as those offered by other suppliers;
- k) regularly publish information on the operations and financial position of the firm;
- l) give appropriate support to recognized national objectives and established government programs, while resisting any direct or indirect pressure from foreign governments or associated companies to act in a contrary manner;
- m) participate in Canadian social and cultural life and support those institutions that are concerned with the intellectual, social, and cultural advancement of the Canadian community; and,
- n) endeavour to ensure that access to foreign resources, including technology and know-how, is not associated with terms and conditions that restrain the firm from observing these principles (Dept. of Supply and Services, 1984:31-2).

Gillespie's guidelines, by all accounts, could have

been pulled out of the four federal-level reports on the impact of foreign investment. He had learned his lessons well at the hands of the CIC; he addresses, in these guidelines, all the major problems associated with branch plant economic development. From marketing they moved on to management training, to equity participation by Canadians, to sourcing policies, to research and development. Were these guidelines to be followed, there would exist a real possibility for the transformation of the model of the branch plant economy in Canada. As well, in requesting that firms improve the extent of their resource processing in Canada, the guidelines sought to address one of the major flaws of the picture of Canada as an economy serving U.S. resource needs.

Of course, the guidelines were merely that: guidelines. While much more stringent and specific than the FIRA significant benefit criteria, the guidelines were limited in their ability to alter the nature of the industrial structure in Canada fundamentally. In fact, as we shall see, it was not until after the recession of the 1980s that these guidelines would be given serious consideration -- with the introduction of the Canada's world product mandating policy.

In the meantime, lost in the shuffle of the 1974

federal election, the Foreign Investment Review Agency did not recapture public attention for most of the remainder of the 1970s. For much of this period, the Agency was experiencing inevitable teething pains, made worse by the difficulties of an unspecified mandate. These administrative problems contributed to the rapid marginalization of the Agency.

By November 1974, the administrative problems which were to plague FIRA were becoming apparent. The Financial Post reported that "foreign corporate takeover applications are piling up at the Foreign Investment Review Agency" (Baxter, 1974:1). After seven months of operation the Agency was studying seventy applications, with new ones "pouring in almost every day." The cumbersome application and review procedure was to plague the Agency until the 1982 streamlining changes, with slowness of review constantly cited as a source of frustration for investors (see Beckman, 1984, for example). Further, Industry, Trade and Commerce Minister Alastair Gillespie was wrestling with the problem of information -- how much should be released about the specifics of the review and decision making process. Secrecy was a difficulty which was to plague the Agency for its administrative lifetime. The problem was compounded by Cabinet decision making (which was not

necessarily defined in all cases by a rigid set of rules) and the need to keep corporate information secret. The picture painted of the first few months of Agency operation was one of the hectic pace of getting used to a new procedure and a set of new rules. "The staff at the Foreign Investment Review Agency is now furiously busy. After long quiet weeks while the summer election was under way and foreign buyers hung back waiting whether to move into Canada, buyers are now pushing hard" (Baxter, 1974:1).

The first few months of the Agency also saw the last attempts of the Committee for an Independent Canada to strengthen FIRA's provisions to include measures to Canadianize firms operating in Canada. In submitting a proposal to the Privy Council, CIC chairman Robert Page indicated that he hoped that the Agency would be strengthened by the end of 1974. Plans to include Canadianization proposals within the Agency structure were abandoned, however, in consultations between Trade Minister Gillespie and provincial trade ministers, (Partridge, 1974:1). As we saw in Chapter Four, not all provincial officials had been enthusiastic about the regulations underlining FIRA in the first instance, and were loathe to see any extension of its powers. In part, these concerns were born of the fear that Ottawa

would be providing itself with the leverage to intervene too heavily in provincial incentive programs. The failure to strengthen FIRA convinced CIC officials that the Agency would remain a "symbolic" presence against foreign investment in Canada.

The Agency did also undergo some changes which were not related to a change in state manager assessment of the costs of foreign investment. Some restrictions and liberalizations can be associated with interests of the individual ministers responsible for the conduct of the Agency, apart from the definition of particular assumptions. Jean Chretien succeeded Don Jamieson as Minister of Industry on September 14, 1976. It is widely acknowledged that his tenure led to the liberalization of FIRA's administrative process. Chretien was known for his pro-business views, but he had no objection to FIRA. By his own account, "all countries have laws that control foreigners" (Chretien, 1985:98), and Canada should not have to be "odd country out" in the restriction of foreign investment. On March 11, 1977, amendments were made to the regulations respecting the Foreign Investment Review Act. The new regulations attempted to combine, simplify, and reduce the information requirements for acquisition and new business proposals. Chretien, who saw the changes

through, also provided for an abbreviated form of notice for "small business" investment proposals -- proposals involving the acquisition or establishment of business with gross assets of less than \$2 million and less than 100 employees (FIRA, Annual Report, 1978:1-2). The Minister still retained the right to request that an applicant completing the small business application procedure complete the lengthier process if he believed that more information would be useful.

Chretien undoubtedly helped to speed the administration of the Act through the development of a small business "short form" for investment applications. Officials once at FIRA commented that the processing of the complete forms was so time consuming as to make it virtually impossible to review any application within specified time periods. One official suggested, in fact, that the Departments of Finance, and Industry, Trade and Commerce, in consultation with Cabinet in the original formulation of the Act had deliberately made the process so cumbersome that the Agency would be buried under the weight of applications (Confidential interview, Winter 1988).

Further administrative changes were almost proposed after the election of the Clark Conservative Government in 1979. Robert de Cotret, Minister of Industry, Trade

and Commerce for the new government, announced in the summer of 1979 that he had requested a review of FIRA's procedures. The lessons of the foreign investment debate clearly crossed party lines; de Cotret claimed that the Clark government supported FIRA in principle, and had no intention of dismantling the agency. His procedural review was to answer three basic questions of administrative detail: how to handle the growing complaints over the Agency's penchant for secrecy, how to administer the growing number of small business applications, and how to concretely clarify, despite the Gillespie guidelines, the concept of significant benefit.

De Cotret's administrative review was to be followed by a public "policy-legislative" review. His purpose was simple; he claimed that he wanted to assess "if the problem the act was designed to solve is still there" (Lukasiewicz, 1979:B1). This was the first acknowledgement since the creation of the Agency that foreign investment patterns might have changed, implicit as that observation was. Commentators have suggested that had the Conservative government lasted for longer than a few months, the Agency might in fact have been disbanded, but there is no evidence to suggest that this was the case. As James Spence observed, "whatever

currents of change may have been developing at the political level, people actually dealing with FIRA on specific cases found that, generally, it was business as usual..." (1984:316).

The administrative details of Agency functionings, and the changes therein, did not imply any change in state manager perception of the Canadian economic climate. FIRA continued to embody notions of Canadian attractiveness to new investment all the while seeking to remedy the consequences of branch plant investments. In fact, the commitment of FIRA officials to the cause of redressing the inequities of the Canadian economy is quite clear; in reports and interviews, FIRA officials were far more likely to be placed on the defensive with accusations that they were allowing too many investment proposals to pass through than not enough. Gorse Howarth, Commissioner of the Agency until 1982 often repeated his assessment that FIRA officials were doing their job -- despite high approval rates, they were negotiating for greater benefits out of proposed investments. Howarth clearly perceived his role and that of his Agency as making foreign investment as palatable as possible to Canadians. Without negotiation, he argued, Canada would lose out on opportunities for jobs, for a greater degree of research

and development, for greater participation in management, and for greater opportunities to export goods (The Independencer, 1979). Of course, without any effective enforcement branch, such undertakings on the part of investing firms may well have been moot. Still, the point remains that FIRA officials operated along the lines of the basic assumptions incorporated within the act; that the branch plant structure of the economy needed to be remedied through more effective investment, and that Canada would remain attractive enough as a site for investment to permit negotiation of specific undertakings on the part of the prospective investor.

The Department of Industry, Trade and Commerce, for its part, had begun a program of consultations with the manufacturing sector. Bruce Doern argues that at a minimum, the government wished members of the Canadian state to be at least seen to be consulting with the voices of business, and a series of consultations by the Export Promotion Review Committee of ITC were part of that process (Doern, 1982:20). Political state managers not only wished to obtain information from these firms, but to "introduce new Canadian content "habits" in corporate decision making" (Doern, 1982:20). Political intentions to further the cause of transforming the branch plant economy were not to be rewarded. The Final

Report, Strengthening Canada Abroad reflected what we have seen to be the as the "traditional" orientation for ITC. A former ITC official described the industry section of the department as truly and wholly captive of its industrial clients -- so much so as to make a coherent viewpoint on industry generally near impossible. Different industrial sectors, for example, would have a different perception of the likelihood of a threat to their competitiveness from foreign investment, ensuring that a general policy on foreign investment from the industry side of the department would never be forthcoming. Policy articulation for the department fell, de facto to the trade side (Personal interview, September 1989). The Report recommended a more liberal policy toward direct investment in Canada with a view to reducing foreign borrowing -- with a view to improving a balance of payments picture which was suffering as Canada entered into the recession of the early 1980s. The Report also contended that Canada needed to make foreign investment feel welcome. Suddenly, in an official Report, we now have a wholly different view of foreign investment; Canada needs investment, and must make it feel welcome -- that is, must attract it. Finally, the Report suggested that all restrictive policies should be abandoned in favour of policies which

"emphasize positive incentive for Canadian-owned firms to become internationally competitive, rather than negative measures to constrain the foreign multinationals" (1979:9).

The ITC Report was completed through a review of submissions from 170 firms operating in Canada. While the bureaucratic memory of ITC may have felt comfortable with a proposal welcoming foreign investment (see Williams, 1982), the Report also suggested that Canadian capital had come to a relatively unanimous view about the advisability of the Foreign Investment Review Agency. FIRA was definitively now without bureaucratic support from ITC.

From a position of non-politicized status quo in 1979, FIRA once again became an item on the agenda of 1980 politics. During the election to replace the fallen Clark government, Trudeau pledged to strengthen FIRA. A senior Liberal party official commented that the Hatch Report had little impact on the Liberal party campaign strategy with respect to the Agency. Although the product of a Liberal initiative, the Report was released during the Clark government, and could therefore be dismissed as Conservative government propaganda. Furthermore, revealing the extent to which political and bureaucratic leadership learning takes

place on different bases, the official suggested that, at any rate, the Hatch Report was the product of bureaucracy, and that "it's bureaucracy's job to harp on things, and it's the politician's job to ignore them" (Confidential interview, September 1989). Trudeau committed himself to allowing FIRA to periodically review and assess the performance of large foreign firms in areas such as research and development and export promotion, to publicize proposed foreign takeovers of firms larger than some specified size, and to guarantee bank loans to Canadian companies that wished to compete for foreign takeovers or to repatriate the foreign ownership of assets (Trueman, 1980:9).

These provisions implied a far more radical stance on the issue of control over the Canadian economy than was currently a part of FIRA, reflecting the CIC's assumption that control equalled ownership. The CIC itself, during the election campaign, had randomly published information revealing the extent to which other countries had developed foreign investment policies far more restrictive than those of the Canadian state, keeping a "scoresheet" against which Canadians could still view themselves as far more liberalized than any of a number of other countries (The Independencer, 1980). In fact, the newsletter intimated that the

mildness of Canada's provisions might in fact suggest that it was out of step with the rest of the world economy -- that the liberalized investment policy norms of old were well and truly a thing of the past.

It is, in fact, certainly not the impact of a diminishing CIC which convinced Canadian political leaders to try to play to a nationalist theme. The Committee, well aware of its own reduced role, was preparing to officially disband in 1981, at any rate. Neither was it a new calculation based on a different perception of the Canadian location in the pattern of international investment flows. Rather, it was undoubtedly the realities of electoral politics which brought back the call for a strengthened FIRA, and the conviction of the Trudeau Liberals that they could win political acclaim for attacking the beast of foreign investment. Trudeau's call for a strengthened Agency came just four days before the election. Announced in Toronto, the unofficial capital of the CIC and the central Canadian new middle class, his call had time to create an impact without generating much of a response from his electoral competitors. Glen Williams argues that Herb Gray helped to convince Trudeau to give economic nationalism one last chance, and that Gray's reward for the Liberal victory was found in his Cabinet

post as minister of Industry, in charge of the Agency his task force had helped create [6] (Williams, 1982:125). Trudeau himself later accepted the characterization that politics had been the sole reason behind the move to strengthen FIRA; claiming that the economic nationalism of the 1980 election had been a policy "pushed on the Liberals by the Ontario caucus" (Rusk, 1982:1). In an election in which Ontario seats were widely assumed to be the wildcards, and to hold victory, such a calculation was not unfounded.

This casual dismissal of the FIRA pledge makes it appear as though it was never taken seriously by party officials. In fact, quite the opposite is true. Most readers will recall the pledge to strengthen the Foreign Investment Review Agency as a mere footnote to the Liberal government's introduction of the National Energy Program [7]. Promises to strengthen the Agency were, however, made well before any mention of the creation of the NEP; the Throne Speech of April 1980 pledge to invoke a stronger FIRA, while the NEP was not made public until a policy statement by Marc Lalonde in September. In addition, Herb Gray was Minister of Industry. If we could have expected anything, surely it would have been reasonable to expect that under Gray's tenure, the Agency which was his brainchild would be

given authority more in line with the proposals of the Gray Report. In July 1980, Gray in fact prepared a new report for Cabinet in keeping with his original views on foreign investment and the branch plant economy:

First, it contended that the branch plant economy presents serious structural barriers to the realization of Canadian industrial potential. Second, these structural barriers cannot be corrected simply with expenditure programs. Finally, it was suggested that the government must begin to monitor the branch plants with an eye to framing "regulatory mechanisms" to "ensure that Multinational Enterprises (MNEs) perform to world standards in terms of innovation and export freedom" (Williams, 1982:125).

While Gray was clearly still concerned about the negative consequences of branch plant development, the same can hardly be said of the rest of the Liberal Cabinet. Gray was involved in a debate within the Liberal party, a debate which took the form of a conflict between a comprehensive industrial strategy on the one hand, and a resource exploitation, mega projects strategy. When, eighteen months later, Economic Development Minister Senator H.A. Olson's rival report was appended to the November 1981 Budget as Economic Development for Canada in the 1980s, it was clear that the National Energy Program would be the most interventionist policy to be pursued by the Liberal

government of the early 1980s.

What happened to FIRA? The simple answer is that the Liberal Party abandoned it. Herb Gray's assessment is somewhat different, yet equally simple. The debate in Cabinet over an industrial strategy did not represent a repudiation of FIRA, although it did move the Agency onto the back burner on the priority list of the Trudeau government. The Liberals, however, fully intended to keep their Throne Speech pledge to strengthen the Agency, but they simply ran out of time. Gray, and the government, simply had too many things to do. The National Energy Program was bigger than they had anticipated, and drained a tremendous amount of government's time and energy. Constitutional battles loomed in the background. The recession of 1982 hit, creating a whole series of instant crises which displaced everything else. Gray himself spent a considerable portion of this time working out the details of the Canadian Chrysler bailout. Finally, when the recession came under control, Trudeau resigned. With the party into a leadership race, few initiatives could be undertaken -- and FIRA was not high priority enough to be one of them (Confidential interview, Senior Liberal party official, September 1989).

Before turning to a discussion of the implications

of the defeat or abandonment of FIRA for state manager learning, we will briefly mention another source of opposition to the Agency, the United States. The strongest of the U.S. measures directed against FIRA in this time period involved the filing of a petition before the GATT. After almost two years of strong diplomatic representation (see Clarkson, 1982:90-104), the United States launched a protest against the FIRA imposition of performance requirements on foreign investors. In particular, they cited the agency under GATT Article 3, arguing that Canada violated the national treatment principle when it required sourcing and exporting commitments from prospective investors [8]. U.S. intervention at this level was designed to reaffirm the principles of the implicit international regime, which by then was no longer an effective guide to international investment (in fact, U.S. officials had by then started calling for a formal regime -- "a GATT for investment" -- which remains an objective of U.S. policy makers in the current Uruguay Round of GATT negotiations). Despite the U.S. actions, policy makers in Ottawa recalled that American threats had little or nothing to do with the reduced priority placed by the Liberal government on strengthening FIRA (Confidential interview, Senior Liberal party official, September

1989).[9]

What are the implications of the debate within the Liberal party for state manager learning? Clearly, Herb Gray continued to accept the decade-old analysis of the new middle class, even as the CIC disbanded. Just as clearly, the majority of the Cabinet did not find arguments which suggested that the branch plant economy had to be tackled one more time very compelling. Bureaucratic state managers, never wholly committed to FIRA, had (at least in ITC) broken their discreet public silence with the release of the Hatch Report and the call for a liberalized investment policy. We have argued, though, that knowledge comes from somewhere, that state managers take decisions in response to interpretations of the international economy. If the branch plant thesis no longer seemed to be compelling, and both bureaucratic and political state managers were pulling away from a commitment, however implicit, to FIRA, we must conclude that new information was challenging the understanding of state managers as to Canada's place within the international pattern of foreign investment. It is to the task of tracing this new understanding that we now turn our attention.

The Growth of Canadian Capital

One of the most significant features of the period following the creation of FIRA is found in the "coming of age" of Canadian multinationals. The extent of their investment abroad increased phenomenally, and in the process, they became far more politically active and influential. Reflecting the changes in the flows of foreign investment internationally, these Canadian multinationals began to articulate a new understanding of Canada's place in the global economy. It is Canadian capital which challenged the branch plant interpretation of Canada's location in the international political economy, and thus provided the basis for new learning which eventually resulted in revisions to FIRA and the creation of Investment Canada.

Niosi reveals that thirty-three Canadian firms are on the list of the 500 largest non-American industrial corporations (Niosi, 1985a:57) -- placing Canada between France, with 38, and Sweden, with 22. In 1982, the stock of Canadian direct investment abroad controlled by Canadian firms was \$28.219 billion, of which \$18.870 billion was invested in the United States (an increase from \$9.986 billion in 1979, and \$13.601 billion in 1981) and \$2.116 billion in the United Kingdom (Statistics Canada, 1986:34)). In terms of sectoral

distinctions, Canadian firms had considerable foreign investments in the beverage industry (Seagrams, Hiram Walker[10], Molson's, Labatt's), in metals (Alcan Aluminium, Inco, Noranda, Comico, Falconbridge), in wood and paper products (Abitibi-Price, Consolidated-Bathurst, Domtar, MacMillan-Bloedel), and, most substantial of all, in financial industries (the "Big Five" Canadian Banks). Niosi concludes that "[b]ased on their size (absolute and relative), their presence in the large American and European markets, their number, and the position they occupy in the industries in which they operate, Canadian multinationals resemble those of the advanced industrial countries much more than those of the major Latin American or Asian countries" (1985:56).

The changing conception of the Canadian location in the global economy as a result of the growing activities of Canadian multinational firms and of the high profile given to Canadian foreign investment activities is clear. The Globe and Mail, for example, argued that we must no longer conceive of the "typical multinational corporation" as a "huge, sprawling business enterprise based in the United States or Europe and with subsidiary operations in Canada and other countries", but rather acknowledge that "a score of Canadian companies has made

it to the big league" (Anderson, 1984:B2). Canadian firms suddenly seemed big, and competitive.

It is not only Canada's largest firms that have been investing abroad, although these are the firms whose geographical investment patterns are most varied. Investment in the United States, at 77 percent of all Canadian foreign investment for 1984, is often conducted by smaller firms wishing to expand into a lucrative, and geographically proximate, market. Canada is now the third largest foreign investor in the United States, ranking behind Japan and the United Kingdom, and in 1984, accounting for 14 percent of the United States inward foreign investment. Northern Telecom is now the second-largest manufacturer of telecommunications equipment in the U.S. (Gibbens, 1984:B15). Olympia and York, the second-largest commercial landlord in New York City has invested in excess of \$2 billion to develop Battery Park (Martin, 1985:37). In Houston, Cadillac Fairview has redeveloped 30 blocks of the city's core. Canadian developers own a third of Minneapolis' downtown buildings. Canadians own 15 percent of Denver's entire apartment stock. Imasco owns the 10th-largest drug store chain in the United States. Even the fast food industry, once an American preserve, is being penetrated by Canadian firms, with companies such as Swiss Chalet,

Mother Tucker's, Country Style Donuts, and Pizza Pizza moving into the United States. More recently, we have seen the much heralded takeover of Bloomingdale's and the rest of Federated Department Stores by the Campeau Corporation (The Economist, 17 September, 1988:71), although the stability of the Campeau financial empire is now in doubt. A Canadian firm, Seagram Company Ltd., consistently tops the Fortune magazine's list of the top 100 foreign investments in the United States, with revenues high into the billions of dollars annually from the sale of its alcoholic beverages and from its 23 percent share of du Pont de Nemours chemical and energy conglomerate (Goodspeed, 1986:D1).

The expansion in Canadian investment is the result of several factors. The capital maturity of the Canadian economy has made such investment financially possible. The attractiveness of the United States in the 1980s as a location for investment has been felt by Canadian firms as much as it has by other foreign investors. As we saw in Chapters Two and Three, where U.S. firms were the first to engage in multinational investments in large numbers, firms of other countries have become more extensively involved in this process, seeking to reap the same profits born of their oligopolistic advantages (Canada's resource-based

advantages, for example).

Canadian multinationals are different from the MNCs of many other countries, however. We will recall that a lack of indigenous R&D was identified as a feature of the branch plant economy. It is not clear that the rapid expansion of Canadian multinationals has done much to stem the problem. While a significant percentage (nearly 50 percent) of Canadian foreign investment is concentrated in manufacturing investment, to a great degree these firms are involved in the processing and marketing of resources. Rugman and McIlveen report that, on average, R & D expenditures in Canada's largest firms is at 1.4 percent of sales. This, however, includes figures for Northern Telecom, Canada's largest R & D establishment, and thus skews the percentage of R & D activity actually undertaken. Without Nortel, the average proportion of R & D drops to 0.8, as compared to figures of between 2 and 3 percent for multinationals from the United States, Europe, or Japan (1985:29). Canadian firms have become multinational in areas which typically produce intermediate products (lumber, metals, paper, for example) rather than consumer end-products. This has meant that these firms have largely concentrated their research and development on productivity improvement, rather than on product

innovation. The rapid internationalization of Canada's largest firms through the 1970s and 1980s on the one hand, necessarily forces a re-evaluation of the branch plant thesis underlying the creation of FIRA, and yet on the other hand, the nature of those Canadian capitals does not help to redress one of the ills of the branch plant economy.

The Business Council on National Issues is the political lobby for these new Canadian multinationals, as well as for MNCs operating in Canada. Formed in 1976, the Council was born of the conviction that no voice in the business community was being listened to in a serious way. As Langille writes, the BCNI "sought to overcome the reputation that existing business organizations had acquired for carping and special pleading" (1987:48). An official with Investment Canada confessed, for example, that "nobody listens to the Canadian Manufacturers' Association any more because they're all foreign firms anyway" (Personal Interview, September 1989). The Business Council is made up of the largest corporations operating within the Canadian market, and covers the spectrum of industrial sectors -- from resource operations to banking. Included in among its membership are firms such as Imperial Oil, Texaco, Kodak, Ford, Xerox, IMB, CIL, as well as Canadian firms

such as Inco, Stelco, Alcan, as well as the Canadian banks. These large corporations engage in international activities, and require access to markets larger than the Canadian one. Most are intimately involved in production for international trade, or have substantial international investments. Any move toward market liberalization which could enhance the potential for growth and profitability of these corporations is welcomed by the Business Council. As Tom d'Aquino, president of the BCNI has often stated, "[f]rom the 1960s to the 1980s..., a number of Canadian companies achieved economies of scale or a level of success that gave them confidence they had not had before" (Business Week, 27 July 1987:39). Larger Canadian companies did not want to be party to the nationalisms of the Canadian state which could lead to protectionist responses by other states; competition and level playing field became the new terms of the game.

The Business Council on National Issues was to prove instrumental in the reshaping of state policy through the redefinition of certain state manager assumptions. While it had become a matter of state policy to consult business on issues of relevance to them (particularly after the imposition of price and wage controls in 1975), the policy was not always a

successful one. Doern argues that because much of the consulting was taking place on an individual firm basis, the firm was just as likely to be the loser in the consultative process as not (1982:20-1). Reflecting upon the process later, Michael Pitfield observed that although business was being included in consultation over foreign economic policy making, there was no general sense of business interest, and meetings between business and government more often than not were part of the problem given that many of the existing business organizations had badly atrophied (Pitfield as quoted in Langille, 1987:47). The case for the creation of a new organization which could speak to government while claiming to represent the general voice of business was strong.

On June 30, 1982, the Trudeau government announced that FIRA would effectively cease to be an important -- if ever it had been -- barrier to foreign investment in Canada. The government raised the threshold for review of acquisitions or new business start-ups by foreign firms in Canada from \$2 million and 100 employees to \$5 million and 200 employees. More importantly, new streamlined application and review procedures were announced, ensuring that the processing of investment applications would be dealt with more rapidly. The

implication of these changes was clear; the state was moving away from its perception of the costs inherent in foreign investment. The appointment of the pro-business Ed Lumley to the position of Industry minister (to replace Herb Gray), and the replacement of Gorse Howarth with Robert Richardson as the new FIRA commissioner (Richardson was not known to be an economic nationalist), underscored the change in attitude taking place in Ottawa.

The change went beyond the purely cosmetic. FIRA became an Agency which tried to actively solicit foreign investment. Robert Richardson, attending the Davos symposium in January 1984 considered personally making contact with all those investors who had felt put off by the old FIRA, and asking them to try again (Webster, 1984:1). The new assumptions guiding FIRA "II" apparently included the notion, as Strengthening Canada Abroad had suggested, that Canada now needed foreign capital. The approval of investment applications by Getty Oil Co. of Los Angeles and Mobil Corp. of New York, involving the indirect takeover of Canadian oil and gas properties (after initial rejections in the heyday of Canadian petroleum takeovers in 1981), more than any other act, revealed the extent to which FIRA was no longer acting as part of a sectorally-targetted

industrial policy (although the Agency did extract commitments from each investor to increase Canadian equity ownership in the Canadian operations to fifty percent within two to five years) (Lewington, 1982).

NEW STATE ASSUMPTIONS: THE ROAD TO INVESTMENT CANADA

In order to understand precisely how state manager assumptions were being redefined, it is useful to examine the statements and briefings presented to the Conservative government of Brian Mulroney surrounding the conversion of FIRA to Investment Canada. These assumptions also reflected the underlying motivations for the changes in FIRA -- for clearly the wholesale revisions of the Trudeau government suggested that a new pattern of state manager learning was at work.

When the Mulroney government created Investment Canada to replace the Agency, there was little doubt that the new perception of a dynamic Canada, characterized by a competitive multinational economy, had gained the upper hand in the minds of state managers. The regulation of investment was no longer a priority of the Canadian state, rather, the state would enable investment. Prime Minister Mulroney commented to the Economic Club of New York that:

In 1974 we started down this costly
[inward and interventionist] path

with the Foreign Investment Review Agency Such a direction ignored the basic lesson of our history, namely that free and unfettered access to world markets has been a boon to strong and dynamic economic growth in our country. It was indicative of the misguided belief that regulation by politicians and bureaucrats was superior to the decisions of individuals and firms competing in the global marketplace.

...[W]e must adopt policies that foster higher investment, greater innovation and increased international competitiveness. Investment contributes directly to the growth of output and employment, and is central to ensuring that Canadian business responds rapidly to new technology and new market opportunities. Greater innovation, enhanced productivity and increased competitiveness are essential if Canada is to compete effectively in the world marketplace.

The message to prospective foreign investors in Canada is the same message we send to our trading partners: a world economy more open and interdependent is in Canada's interest and every nation's interest. We want an environment conducive to dynamic growth in trade, investment and development on a global basis.

Investment Canada will be governed by two fundamental operational objectives: first to facilitate investment in Canada; and second, to limit government intervention in the foreign investment area (*italics added*).

Our message is clear: Canada is open for business again (Mulroney,

1984:4-7).

Mulroney's "open for business" speech illustrated several new assumptions which were not part of the creation of FIRA. States should not intervene in the foreign investment process; such intervention was seen to have had negative consequences for the Canadian economy. One of those consequences was assumed to be protectionism, which would affect the ability of Canadian business to respond "rapidly to new technology and new market opportunities" (Mulroney, 1984:5). The state now also was assumed to have obligations toward the foreign investor, and would act to facilitate investment, rather than to regulate or restrict it. Once again, this is consistent with the perspective that Canadian firms were operating abroad more extensively than previous; the Canadian state would act to permit, and in fact attract, investment in part because these actions would assist the requirements of Canadian capital in its foreign investments.

The new assumptions of Canadian state managers did not emerge out of thin air. Canadian business interests were unanimous, and numerous, in their push to convince Canadian state representatives to break out of the assumptions which had characterized state regulation of foreign investment under FIRA. Interestingly enough,

representatives of capital were far more numerous and lengthy in submitting testimony before the Standing Committee investigating the Investment Canada bill than they had before the committees looking into the Foreign Takeovers and Foreign Investment Review Acts. In these testimonies, capital was not ambiguous in the least.

Clear views emerge through an examination of the submissions of capital. To begin, business interests unanimously presented the view that Canada could no longer take its attractiveness as a location for investment for granted. Samuel Hughes, for example, President of the Canadian Chamber of Commerce, argued that "[o]ur first priority must be to encourage investment The global environment is changing. More countries are competing more aggressively for scarce investment dollars" (1985:12/6). Thomas D'Aquino, President of the Business Council on National Issues, argued strongly for the least amount of regulation possible in order to not compromise Canadian attractiveness on international investment markets. Rather D'Aquino suggested that the new Agency should become one virtually singly concerned with the promotion of investment (1985:11/27). These views, of course, are fundamental reversals of position from those embodied in FIRA. If Investment Canada's mandate was to be

primarily concerned with the encouragement and promotion of investment, this not only suggested that Canada needed to be marketed more effectively in order to stand out as attractive to prospective investors, but also implied that Canada needed new investment -- that it no longer "had enough" foreign investment.

With the exception of the Canadian Labour Congress and Mel Hurtig (whose brief was presented on behalf of Hurtig publishers), FIRA's concept of branch plant investment was universally derided. Robert Blair of NOVA Corporation argued forcefully that his firm could compete with anyone doing anything. "In the NOVA company group, which is Canadian owned, we exist daily in competition around the world with some of the toughest international business rivals in several of the world's most competitive sectors" (1985:8/5). Thomas D'Aquino went so far as to speak of branch plant development as a phenomenon of the past. Concerns over lack of exports or foreign sourcing were reflective of a "branch plant mentality of the 1950s The branch plant mentality is one that many Canadians were brought up on, based on the fact that we did have a long history of branch plant development in this country" (emphasis added) (1985:11/28). Canada was no longer to be thought of as a branch plant economy, but rather one of competitive

and aggressive firms.

To a great degree, these perspectives did reflect Canada's changing position in the pattern of international investment through their observation of the decline in branch plant forms of manufacturing investment and of the increased competition for investment. Investment Canada certainly reflected some of these perspectives; as a regulatory agency, it clearly has a more open attitude toward investment than did FIRA. In its 1985-86 Annual Report, the mandate of the new Agency was spelled out as three-fold; first, to promote investment in Canada by Canadians and non-Canadians; second, to undertake research and provide policy advice on matters relating to investment; and third, to review significant investments by non-Canadians to ensure net benefit to Canada (Investment Canada, 1986:12). Investment Canada has put together a volume on investment opportunities in Canada, subject to yearly update, entitled The Canadian Edge (1986). Investment Canada's new mandate was thus, in fact, vastly expanded over the FIRA mandate. The new Agency had the authority to act as an international promoter for Canada as an attractive location for investment, as well as a regulator of incoming investment, although such regulation has been restricted

largely to investments involving acquisitions of over \$5 million (or \$50 million for indirect acquisitions), or investments in culturally sensitive sectors (New businesses are exempt from review under the Investment Canada mandate).

Through this chapter, we have traced how state managers were confronted with a new interpretation of Canada's location in the pattern of international investment flows. The Central Canadian new middle class was unable to form a cohesive enough group (a national group defined in terms of class based interests rather than a regional group, defined as separate from other regions), and thus did not challenge an emerging perspective of Canada as something other than a branch plant economy. Canadian business interests, for their part, had largely consolidated their perspectives and become more powerful -- many as multinational firms in their own rights. Their perceptions of the international investment environment were not determined by academic study and inference, but rather through direct participation in some aspect of the international economy. We have not come full circle, however. Prior to the debates surrounding the enactment of FIRA, Canadian state managers had a country open for business, but one which did not have to canvass for that business.

The interpretations of Canada's international position in the creation of Investment Canada are unique to the period.

Yet, one can legitimately ask: what happened to the branch plant economy of FIRA? Was FIRA so successful as to eliminate the truncated structure underlying the concerns motivating the creation of the Agency? And if FIRA was not successful, then we must ask whether state managers have "unlearned" their interpretations based on branch plant investment. Chapter Six will turn its attention to both of these questions.

ENDNOTES

- [1] Prime Minister Trudeau was the only leader to devote a single speech to foreign economic policy, a speech in which foreign investment was not singled out as an issue (Munton and Poel, 1978:240). Frederick Fletcher's content analysis of newspaper front pages through the election campaign illustrates the extent to which media focus on the issue was lacking as well. Including front page stories and editorials, Fletcher found that general economic conditions were the topic of 46 percent of all stories, leadership of 22 percent, and national unity of 15 percent of stories. Foreign investment was not a leading issue (Fletcher, 1985).
- [2] By the fall of 1973, a pre-election poll revealed that inflation had replaced unemployment as the most significant problem facing Canada. The Canadian economy had experienced a period of sustained economic expansion from the first quarter 1971 through to the end of the first quarter of 1974. Unemployment, which had reached 6.6 percent in August 1972, dropped to its trough of 4.9 percent in June 1974 (OECD, 1975:11). While this decrease was disappointingly modest (the OECD reported that the rate of unemployment remained higher than in periods of similar capacity utilisation), the drop was substantial enough to lessen national concern over unemployment. Inflation, on the other hand, had become a serious problem. In the two decades between 1953-1973, Canadian prices had generally been more stable than in most other OECD countries, averaging an annual consumer price increase of 2.7 percent. With a year-on-year increase of the consumer price index of 7.6 percent in 1973, however, "the loss of [Canadian] price stability, at least in relative terms," became "as pronounced as in most other OECD countries" (OECD, 1973:8).
- [3] Murray and Leduc (1982) for example, found that negative public concern about foreign investment dropped in 1975, after the creation of FIRA, and continued to decrease through the remainder of the decade. This is not to say that the Agency had resolved all the problems raised by the nationalist movement, but that other economic issues began to compete in the public mind for urgent attention.

5

MICROCOPY RESOLUTION TEST CHART
NATIONAL BUREAU OF STANDARDS
STANDARD REFERENCE MATERIAL 1010a
(ANSI and ISO TEST CHART No. 2)

- [4] From October 1976 to December 1979, the value of the Canadian dollar had undergone an effective depreciation of 35% against the "Group of Ten" currencies.

- [5] Automobile production in Canada through the Auto Pact was not as strong as the lower value of the Canadian dollar might have suggested. Two reasons for this can be found. The economic recovery in the United States was weak, depressing demand below the levels of the early 1970s. As well though, Canadian auto plants had been concentrated in the production of large cars at the same time as the oil crisis was moving the North American market toward smaller, more energy efficient vehicles (CALURA, 1981:16).

- [6] The experience of the National Energy Program and the failure of economic nationalism through the 1982 recession appears to have dampened even Herb Gray's ardour for nationalist solutions. Carol Goar has described Herb Gray as a "crusader [who has] climb[ed] off his charger and walk[ed] slowly to the side of the battlefield" (1985:A14). She credits the demise of Herb Gray's economic nationalism to his removal from Industry, Trade and Commerce in 1982, and his support of the anti-nationalist John Turner in the 1984 Liberal leadership campaign.

- [7] For a full review of the National Energy Program, see Doern and Toner (1985) The Politics of Energy. For a review of U.S. reaction to the provisions of the NEP, see Clarkson (1985) Canada and the Reagan Challenge. The NEP may have been more successful than FIRA in the short term because it served the Canadianization interests (although it was not loved for its taxation measures) of an identifiable group of Canadian energy producers. While Joel Bell, Executive Vice-President of Petro-Canada had been involved in the development of the NEP, and therefore defended most of its provisions, Bob Blair of NOVA, Jack Gallagher of Dome, and Husky Oil, among the most notable firms, were generally supportive of incentives to Canadianize, although they were less sanguine about the state interventionism implied in the NEP (Doern and Toner, 1985:220-50).

- [8] In July 1983, a GATT panel ruled that FIRA had violated GATT Article 3 (the national treatment article) when it required some foreign owned firms operating in Canada to restrict imports and buy materials in Canada. The panel also found that FIRA did not violate GATT Article 17 when it encouraged some foreign investors to undertake to export goods manufactured at their Canadian plants. It is instructive of the extent to which the international norms had eroded that Canadian officials complied by rewording the offending section of the Act, and argued that there would be no difference in its administration. A FIRA official reasoned that since "effect on employment" was still an important criterion in considering any investment proposal, and the sale of domestic goods and services has an impact on employment, then a willingness to source from within Canada would remain a factor of approval (Globe and Mail, January 20, 1984:B4).
- [9] While specific U.S. actions against FIRA before the GATT may have raised little apparent concern in Ottawa, there is no doubt that U.S. pressure over FIRA was felt. FIRA was particularly singled out for attack when it worked to prevent retributive takeovers of Canadian energy resources by U.S. interests during the "Canadianization" sales under the NEP. For a discussion of the impact of such U.S. pressure, see Clarkson, 1985.
- [10] In 1985, Gulf Canada purchased Hiram Walker Resources. The various companies that made up Hiram Walker have either been absorbed or sold (Rugman, 1985:5.19).

CHAPTER SIX

CANADA IN THE GLOBAL ECONOMY: BRANCH PLANT OR INTERNATIONAL COMPETITOR?

We have argued that as a result of new trends in the international economy and changes in the international investment activities of Canadian firms, Canadian state managers came to alter their perception of Canada's place in the pattern of direct foreign investment. In the 1960s, the period which structured the debate surrounding the creation of FIRA, state managers were made aware of the extent of manufacturing branch plant investment within Canada, and of the implications for Canadian economic development of such a phenomenon. During the 1960s, of course, Canada had been host to a significant amount of branch plant investment, and although this trend had been attenuating by the time the Foreign Investment Review Agency came into being, perception of such a change had not yet been translated to state managers. One decade later, Canadian state managers created an agency whose role was defined primarily as investment promotion, this in response to new assessments of the country's location in a now changed pattern of foreign investment. Secure -- albeit branch plant -- investment was superceded by the need to compete for investment dollars.

This chapter seeks to address two questions. The

first, a more technical one, examines the record of the Foreign Investment Review Agency, asking in particular if it was able to deal with the branch plant phenomenon for which it was created. Was the Agency able to extract significant benefit from foreign investment? Is there any evidence that it had any effect on the pattern of foreign investment coming to Canada? In order to answer these questions, it begins by examining the FIRA record of allowances and disallowances, as well as the sectoral investment pattern during FIRA's tenure. The statistical profiles are then supplemented with sectoral overviews for the decade involved, enabling us to better judge the extent to which FIRA had an impact upon investment. A determination of the success or failure of FIRA must be made in terms of the assumptions which it embodies. Following this position, this analysis reveals that while FIRA was an agency largely created to review a particular kind of investment proposal -- the establishment of a manufacturing branch plant -- it was precisely this type of proposal which it was increasingly less likely to review.

Secondly, the chapter goes on to ask whether Canadian state managers have continued to act upon "residual learning" -- that is, upon their earlier perception of Canada as a branch plant economy, and

hence of the need to improve the gains from it? Are policies still enacted which contain these assumptions, or do state managers now operate under a belief of Canada as a dynamic, competitive economy, which needs to attract investment on the same footing as any other country? In order to answer this question, we will return to the Gillespie Guidelines, and evaluate the world product mandating policy of which the Guidelines are a part as a response to the same branch plant concerns which brought about the creation of FIRA.

FIRA: EVALUATING THE RECORD

Despite analogies by groups such as the Chamber of Commerce that FIRA represented the "border guard" of the Canadian state (Globe and Mail, December 8, 1984:B6), FIRA's allowance rates have been the subject of considerable frustration among those hoping to see the Agency play a significant role in redressing the balance of foreign ownership in the Canadian economy. These rates themselves, together with a more detailed review of FIRA's performance, are not unimportant for the argument that we are making here, for they allow us to see how the Agency was administered. FIRA was based on a very specific interpretation of Canada's location in the global economy -- as an attractive branch plant

economy, with resource stockpiles. Its success or failure as a review agency is in no small measure related to the extent to which the assumptions underlying its creation correspond to the reality of the international economy. Rather than allowing us to make a definitive argument about the extent and nature of investment which may or may not have been deterred by the FIRA's presence, reviewing features of the Agency's operational record gives us an indicator of the "fit" between the state's perceptions and the global economy. Tables 6.1 and 6.2 provide a summary of case outcomes of the FIRA review process.

Table 6.1 Outcome of resolved acquisition cases by industry
sector
Percentage of industry sector total

1984-85

	Allowed	Disallowed	Withdrawn
Resources	92.6	--	7.4
Manufacturing	95.6	1.5	2.9
Services	92.8	0.4	6.8

1983-84

Resources	94.1	--	5.9
Manufacturing	95.9	--	4.1
Services	88.6	2.0	9.4

1982-83

Resources	67.9	17.8	14.3
Manufacturing	92.7	--	7.3
Services	91.2	2.7	6.1

1981-82

Resources	35.7	50.0	14.3
Manufacturing	88.0	6.8	5.2
Services	75.4	12.0	12.6

1980-81

Resources	43.8	31.2	25.0
Manufacturing	80.4	9.8	9.8
Services	70.4	12.4	17.2

1979-80

Resources	72.4	20.7	6.9
Manufacturing	86.7	5.2	8.1
Services	86.5	7.6	5.9

1978-79

Resources	91.7	--	8.3
Manufacturing	87.1	6.8	6.1
Services	88.0	9.6	2.4

1977-78

Resources	82.6	4.4	13.0
Manufacturing	93.2	2.6	4.2
Services	90.3	5.7	4.0

1976-77

Resources	64.3	21.4	14.3
Manufacturing	84.7	6.7	8.6
Services	76.4	12.5	11.1

1975-76

Resources	68.2	13.6	18.2
Manufacturing	75.8	16.7	7.5
Services	69.2	12.3	18.5

1974-75

Resources	81.8	9.1	9.1
Manufacturing	60.0	17.8	22.2
Services	79.4	8.8	17.6

Source: Foreign Investment Review Agency (Government of Canada) (various years). Foreign Investment Review Act: Annual Report. Ottawa: Supply and Services

Table 6.2 Outcome of resolved new-business cases by industry sector[a]
Percentage of industry sector total

1984-85

	Allowed	Disallowed	Withdrawn
Resources	87.6	6.2	6.2
Manufacturing	95.2	0.8	4.0
Services	93.2	1.1	5.7

1983-84

Resources	85.0	--	15.0
Manufacturing	93.3	3.0	3.7
Services	84.4	5.3	10.3

1982-83

Resources	94.4	--	5.6
Manufacturing	91.0	2.2	6.8
Services	77.3	10.7	12.0

1981-82

Resources	66.7	11.1	22.2
Manufacturing	83.1	4.8	12.1
Services	56.3	14.3	29.4

1980-81

Resources	57.9	5.3	36.8
Manufacturing	95.3	1.9	2.8
Services	72.0	14.3	13.7

1979-80

Resources	87.0	8.7	4.3
Manufacturing	92.7	2.7	4.6
Services	84.5	8.7	6.8

1978-79

Resources	81.0	--	19.0
Manufacturing	94.6	3.2	2.2
Services	85.4	7.3	7.3

1977-78

Resources	88.5	3.8	7.7
Manufacturing	93.0	1.0	6.0
Services	87.2	5.7	7.1

1976-77

Resources	80.0	--	20.0
Manufacturing	84.7	4.2	11.1
Services	77.6	8.8	13.6

Source: Foreign Investment Review Agency (Government of Canada) (various years). Foreign Investment Review Act; Annual Report. Ottawa: Supply and Services

[a] New Business applications were not subject to review until October 15, 1975, and were tabulated for the first time in the Annual Report for the fiscal year 1976/77.

The vagaries involved in FIRA's screening mechanism have been the topic of considerable debate and consternation since the Agency began to screen investment applications in April 1974. As we have mentioned, public business reaction assumed a "wait and see" attitude as its initial response to the creation of the Agency. Confronted with the allowance figures cited in Tables 6.1 and 6.2, it is too easy to contend that FIRA has not discouraged investment. A closer look at these rates, however, at least allows us to make some inferences about the manner in which the Foreign Investment Review Act was administered.

If we average allowance rates for each fiscal year, we find that troughs in allowance rates exist for acquisitions in the initial period of operation (1974-1977), where acquisition allowance rates varied between 75.1 percent and 73.7 percent, and for the period 1980-1982, where rates were 64.5 percent and 66.4 percent. In terms of new business applications, the pattern is somewhat different, given that new business applications were not considered until the end of 1975. The one trough in new business investment occurs in the 1980-1982 period, where allowance rates averaged 75.1 and 68.7 percent. The highest rates stood near or above 90 percent, and account for almost every other fiscal year. Specifically, peaks of allowances for

acquisitions were in the period 1977-1979 (with allowance rates of 88.9 and 88.7 percent) and in the years 1983-1985 (allowance rates 92.9 and 93.6 percent). For new business investment, the peaks in high allowance rates follow the same pattern: from 1977 to 1979 (with a low of 87 percent and a high of 89.6 percent), and 1983-1985 (87.6 percent and 92 percent).

A more detailed picture is obtained with a closer sectoral examination. In particular, the period 1980-1983 saw allowance rates of as low as 35.7 percent for acquisitions of resource industries. This we could easily have anticipated, given the operation at the time of the National Energy Program. In fact, it is well documented (see Clarkson, 1985, for example) that FIRA operated in the resource sector in those years to prevent attempts at retaliatory buy-backs on the part of mostly U.S. firms whose Canadian assets had been repatriated by Canadian oil firms following the spirit of the NEP. Robert Dalpe's investigation of FIRA's activities led him to conclude, in fact, that "[l]'activite du FIRA a surtout ete visible dans le secteur primaire.... La politique du FIRA jointe a d'autres politiques de nationalisation a permis une reduction du controle etranger dans le secteur primaire" (Dalpe, 1987:356-7). Anecdotal evidence exists to support Dalpe's suggestion and our contention that

FIRA's activities were primarily visible in the resource sector beyond the role it played as part of the effective articulation of an industrial strategy with the creation of the NEP. Frank Swedlove has described how, for example, the American firm Simpson Timber Co. (Alberta) Ltd. was asked to change its proposal before FIRA to establish a forestry complex in Alberta. Both the Canadian government and the Alberta government were interested in some Canadian participation in the project, and the U.S. firm accepted the bid of the Alberta Energy Corporation (50 percent owned by the Alberta government) to obtain a 40 percent interest in the forestry complex (Swedlove, 1978:15).

FIRA not only worked to limit the resource investments of a particular firm, or to negotiate better terms to an investment proposal. It would often assist in finding a joint venture partner from Canada, particularly for large projects. One of the most prominent examples of this was found in the case of Syncrude Canada Ltd. One of the original four partners, Atlantic Richfield Canada, Ltd., decided to withdraw from the project. It quickly became clear that it would be impossible to find another private concern with the available capital. In order to preserve the chance for access to future oil supplies, and employment, FIRA assisted the private sector partners (Imperial Oil, Gulf

Canada, and Canada-Cities Service) to find public sector partners, in this case, shares divided between the federal, Alberta and Ontario governments (Swedlove, 1978:14).

It is crucial to remember, however, that FIRA reviewed but a few resource related applications as a percentage of all applications. Resource applications as well, particularly for the establishment of new businesses, typically involved very high capital commitments (See Tables 6.3 and 6.4). FIRA may well have been a better "guardian" in resource-related investments than in other sectors, but this is hardly surprising during a decade in which energy resources in particular were sensitive assets to Canadian state managers, and energy resources were the target of the state's Canadianization proposals.

Table 6.3 Reviewable Acquisitions, classified by Industrial Sector

Resources

	Number of cases	Average assets of acquirees (\$000)	% of cases	% of assets
1974-75	22	5,118	14.6	11.6
1975-76	16	5,654	11.1	13.5
1976-77	13	13,756	7.0	16.4
1977-78	22	5,271	7.4	7.7
1978-79	32	39,334	8.6	24.1
1979-80	26	15,514	6.8	11.4
1980-81	20	25,735	6.1	12.6
1981-82	12	11,569	3.5	4.8
1982-83	23	48,368	5.4	20.9
1983-84	16	22,367	3.5	8.0
1984-85	27	249,645	5.7	56.7

Manufacturing

	Number of cases	Average assets of acquirees (\$000)	% of cases	% of assets
1974-75	65	6,252	43.4	41.9
1975-76	75	4,714	52.1	52.7
1976-77	98	5,094	52.7	45.7
1977-78	125	5,470	41.8	45.3
1978-79	172	9,564	46.1	31.5
1979-80	171	9,480	45.0	45.9
1980-81	136	12,797	41.2	42.7

Manufacturing (con't)

	Number of cases	Average assets of acquirees (\$000)	% of cases	% of assets
1982-83	168	15,118	39.3	47.7
1983-84	201	11,243	43.6	50.3
1984-85	189	13,225	39.9	21.1

Services

	Number of cases	Average assets of acquirees (\$000)	% of cases	% of assets
1974-75	63	7,170	42.0	46.5
1975-76	53	4,272	36.8	33.8
1976-77	75	5,528	40.3	37.9
1977-78	152	4,666	50.8	47.0
1978-79	169	13,755	45.3	44.4
1979-80	183	8,240	48.2	42.7
1980-81	174	10,467	52.7	44.7
1981-82	194	5,132	57.4	34.2
1982-83	236	7,086	55.3	31.4
1983-84	244	7,666	52.9	41.7
1984-85	258	10,230	54.4	22.2

Source: Foreign Investment Review Agency (Government of Canada) (various years). Foreign Investment Review Act: Annual Report. Ottawa: Supply and Services

Table 6.4 Reviewable New Businesses, classified by Industrial Sector

Resources

	Number of cases	Average planned investment (\$000)	% of cases	% of invest
1976-77	15	2,916	6.3	12.5
1977-78	27	2,406	8.1	40.3
1978-79	25	3,263	7.4	23.0
1979-80	24	3,193	5.9	27.4
1980-81	37	21,647	9.2	63.0
1981-82	14	25,289	3.5	50.3
1982-83	14	173,143	3.0	70.3
1983-84	21	4,289	4.1	3.3
1984-85	14	6,659	3.1	11.4

Manufacturing

	Number of cases	Average planned investment (\$000)	% of cases	% of invest
1976-77	70	3,024	29.4	60.4
1977-78	102	687	30.6	43.4
1978-79	98	983	28.8	27.1
1979-80	102	884	25.3	32.3
1980-81	130	1,614	32.4	16.5
1981-82	109	890	27.2	13.8
1982-83	129	5,838	28.0	21.8
1983-84	138	15,313	27.0	76.9
1984-85	113	3,371	24.8	46.4

Services

	Number of cases	Average planned investment (\$000)	% of cases	% of invest
1976-77	153	622	64.3	27.1
1977-78	204	130	61.3	16.3
1978-79	217	816	63.8	49.9
1979-80	278	406	68.8	40.3
1980-81	234	1,113	58.4	20.5
1981-82	278	911	69.3	35.9
1982-83	317	854	69.0	7.9
1983-84	353	1,546	68.9	19.8
1984-85	328	1,054	72.1	42.2

Source: Foreign Investment Review Agency (Government of Canada) (various years). Foreign Investment Review Act: Annual Report. Ottawa: Supply and Services

As well, though, a review of FIRA's approval ratings in the services sub-sector of "transportation, communications, and other utilities" reveals that an overall allowance rating of only 72.9 percent was achieved -- and only 62.3 percent of acquisition applications were allowed. This again is not surprising. As detailed in Appendix I and discussed in Chapter Four, the Canadian state had long sought to protect the Canadian transportation industry, and had also moved into the protection of television and radio broadcasting, as well as of publication. At first glance, therefore, we must conclude that FIRA operated to restrict investment in those sectors in which there was a well articulated state policy with regard to Canadian ownership or the Canadianization of a particular industry. The Gray Report, in a warning which was to forecast some of the major criticisms directed at the Agency commented that in the absence of a clearly defined series of regulations establishing the goals of the state in terms of "efficient industrial development", a screening agency might end up doing no other than "concern itself with bargaining for more exports, more procurement and more research and development without regard for their impact on ... industrial development in Canada" (1972:456). The NEP

and ad hoc legislation on transportation and communications provided such an "industrial policy" guideline. Other sectors were noticeably not subject to such guidance.

It has been suggested as well that FIRA was responsive to domestic economic pressures and that general economic conditions affect the degree to which FIRA pursues nationalistic policies (See, for example, Globerman, 1984b:126-8). Specifically, it has been argued that FIRA could afford to be more stringent in times of economic prosperity, and became more lenient when the economic indicators performed less well. To some extent, this argument is specious; the Canadian economy was plagued by nearly constant stagflation and a serious recession through the period of FIRA's tenure. While this hypothesis would coincide with the 1974-1979 period, it does not seem to bear out in the economic recession of 1980-82 (when allowance rates were low until the latter part of 1982), nor does it bear out in the period beyond the 1982 crisis -- allowance rates increased considerably in a period of better economic prospects. Looking at balance of payments circumstances exclusively (Appendix II, Table II.4), we find much the same story. Canada ran a consistent deficit on its current account through the period of FIRA's operation

-- until the trade surpluses with the United States in the 1980s left their mark in the 1982-1985 period. The country ran more positive balances on the capital account, however, offsetting deficits on the current account throughout the period. The consistency of the pattern throughout this period makes it difficult to establish any relationship between FIRA allowance rates and Canada's balance of payments position, although, as we have seen, representatives of capital did return to the notion of a balance of payments crisis needing resolution by foreign investment.

Business concern over allowance rates was never greater than when Herb Gray assumed ministerial control of FIRA. Gray's desire to strengthen the administration of the Agency was well known -- he had discussed his views and made his case during the Liberal party's period in opposition. Trudeau himself made known the party's intention during the election campaign; he announced plans to broaden FIRA's mandate to review all large foreign firms based in Canada in order to determine their performance in such aspects of business as export promotion and research and development. Further, and most significantly, Trudeau pointed to the state's perceived convergence between ownership and control.

FIRA will also be required to publicize proposed foreign takeovers beyond a certain size once they have been submitted to the Agency. This will encourage counteroffers from Canadian-controlled interests. More importantly, through government guarantees of bank loans, FIRA will help provide financial assistance to Canadian companies that want to compete for foreign takeovers or repatriate foreign ownership of assets (Toronto Star, February 13, 1980).

Gray's presentation to Cabinet as to the importance of an industrial policy built around recognition of the problems of foreign direct investment lent credibility among observers to the notion that he was going to considerably strengthen Agency (see Williams, 1983:165-7; Clarkson, 1985:87-90).

Other than increased stringencies in the allowance of resource investments, tied into the philosophy of the NEP, it is hard to substantiate that Gray was a significant factor in rendering the Foreign Investment Review Agency a more stringent agency. Tables 6.1 and 6.2 indicate that the disallowance rates for manufactures and service industry sectors had not increased in the 1980-1982 period, although the withdrawal rate appears to have increased for the review of acquisition applications. Whether this withdrawal rate reflected greater intervention on the part of FIRA officials, advising prospective investors that they

stood little chance of having a proposal allowed, or reflected a growing perception among investors that Canada was increasingly inhospitable to new investment cannot be determined with any accuracy. In 1984, the Group of Thirty, a New York based economic think tank, released a study in which it cited Canada as having a deteriorating climate for investment. Their study identified the newly industrializing countries, Japan, and the United States as the areas with improving investment climates. Their report does not situate this change as we did in the context of changes in the pattern of production and competition globally, in which labour costs, large markets and technology were the principal sources of attraction rather than natural resources. Canada shared its poor rating with Western Europe, Latin America and Africa -- certainly not alone in the category of poor performance (Cook, 1984:IB1).

Allowance and disallowance rates are in some senses misleading. As Herb Gray himself remarked, FIRA was never intended to act as a Canadianization agency. He argued before the Canadian Bar Association that ... "the government's object in establishing FIRA was not simply to permit blocking of foreign investments but also to negotiate the matter of benefits as part of reaching decisions on transactions" (Gray, 1980:9). As we

recall, the Canadian state's perception of itself as recipient of branch plant investments had led it to accept the creation of investment criterion of significant benefit. These criteria were to assist in the process of developing a Canadian industrial structure not truncated by the effects of branch plant investment.

In order to help us assess the extent to which FIRA was successful in its mandate, we can turn to statistics from the U.S. Department of Commerce (DOC). The United States DOC conducts periodic reviews of the conditions to which affiliates of U.S. parents are subject in their locations outside the United States. These surveys are one of the best indicators available allowing us to evaluate systematically the success of performance requirements imposed upon foreign subsidiaries. It must be re-stated from the outset that FIRA only reviewed the investment applications of firms wishing to acquire Canadian companies, to establish new businesses, or to expand existing businesses into unrelated economic activities. Clearly, many of the firms surveyed by the United States Department of Commerce would not have been subject to any of the provisions mandated under FIRA. This hardly invalidates the survey as an evaluation of the state's success in dealing with its branch plant

status, however -- investment incentives are still far more prevalent than performance requirements (not all of which came under the aegis of FIRA. Investment incentives often carry their own performance requirements).

Table 6.5 Incentives for U.S. Nonbank Affiliates of Nonbank
U.S. Parents in Canada, 1977 and 1982
Distribution of Affiliates which received incentives

		Year	
		1977	1982
Total number of Firms		2271	2048
(% total)		100	100
Tax Concessions	Yes:	451	353
(% total)		13.8	17.2
	No:	2727	1673
		83.4	81.7[a]
Tariff Concessions	Yes:	173	146
(% total)		5.3	7.1
	No:	3007	1876
		91.9	91.6
Subsidies	Yes:	182	208
(% total)		5.6	10.2
	No:	2995	1820
		91.6	88.9
Other Concessions	Yes:	138	102
(% total)		4.2	5.0
	No:	3032	1903
		92.7	92.9

Source: United States Department of Commerce, Bureau of Economic Analysis (1981). U.S. Direct Investment Abroad: 1977. Washington, D.C.: Printing Office, pp. 168-71; United States Department of Commerce, Bureau of Economic Analysis (1985). U.S. Direct Investment Abroad: 1981. Washington, D.C.: Printing Office, pp. 135-40.

[a] Number may not add to 100 due to non-respondents.

Table 6.6 Performance Requirements for U.S. Nonbank Affiliates
of Nonbank U.S. Parents in Canada, 1977 and 1982
Distribution of Affiliates which were subject to performance
requirements

		Year	
		1977	1982
Total number of Firms		3271	2048
(% total)		100	100
Export a minimum amt	Yes:	10	5
(% total)		0.3	0.2
	No:	3163	2014
		96.7	98.3[a]
Restrict Imports	Yes:	31	13
(% total)		0.9	0.6
	No:	3144	2010
		96.1	98.1
Acquire Local Inputs	Yes:	36	19
(% total)		1.1	0.9
	No:	3136	2002
		95.9	97.8
Employ Local Persons	Yes:	55	64
(% total)		1.1	3.1
	No:	3119	1957
		95.4	95.6
Parent Required to	Yes:	64	24
Limit Equity		2.0	1.2
(% total)	No:	3103	2000
		94.9	97.7

Source: United States Department of Commerce, Bureau of Economic Analysis (1981). U.S. Direct Investment Abroad: 1977. Washington, D.C.: Printing Office, pp. 168-71; United States Department of Commerce, Bureau of Economic Analysis (1985). U.S. Direct Investment Abroad: 1981. Washington, D.C.: Printing Office, pp. 135-40.

[a] Number may not add to 100 due to non-respondents.

Looking at Tables 6.5 and 6.6., one must be careful not to draw the conclusion that FIRA was unable to impose performance requirements -- to extract significant benefit -- as per its mandate. Yet, it is clear, comparing the two tables, that for 1977 and 1982, at least, the percentage of U.S. affiliates operating in Canada under the constraints of performance requirements was very small, and a good deal smaller than the percentage in Canada with incentives. For example, in 1982, 17.2% of the U.S. affiliates operating in Canada received tax concessions, whereas only 0.2% had to undertake to export a minimum amount. This is further reflected in the DOC's evaluation of Canada's relative location as a host for U.S. investment. The Department calculated that 19 percent of U.S. affiliates in Canada received incentives, while only 4 percent were subject to performance requirements. This compares to Luxembourg's permissive investment regime (38% incentives, 1% performance requirements), to Australia (37%:8%), the United Kingdom (32%:3%) or to Japan (9%:9%) (1981:15). Canada's requirements hardly appear to be out of line with international trends.

The only notable exception comes with the relatively significant increase in the number of affiliates required to employ local personnel -- 3.1

percent of affiliates in 1982, up from 1.1 percent in 1977. This is consistent with observations made in the late 1970s and mid-1980s that FIRA's stringency was being sacrificed in search for commitment to create new employment in Canada during periods of high unemployment (beyond 8 percent in the 1977 and 1978 period, beyond 11 percent in the years 1982 through to 1985). "In the search for jobs," the Globe and Mail reported, "the Federal Government has transformed the Foreign Investment Review Agency into a foreign investment promotion agency" (6 March 1984; see also Teasdale, 1979). FIRA officials themselves continued to promote their Agency through reference to the number of concessions which they had been able to extract in negotiating the terms of the investment application with the prospective investor. The FIRA Annual Report of 1983-84, for example, details the number of jobs planned or saved through FIRA's intercession -- 31,215 in 1982-83, 24,089 in 1983-84. (1984:2).

One must also question FIRA's stringency when one examines the Department of Industry, Trade and Commerce/Regional Economic Expansion's own data on the performance of foreign owned subsidiaries operating in Canada. While once again it must be cautioned that these figures examine a sample of all subsidiaries in

Canada, and that many of these would thus never have had to deal with FIRA, it is clear that the exports and sourcing problems identified under FIRA's criterion of significant benefits did not improve through the 1970s and into the early 1980s. Where in 1971, export sales as a proportion of total sales of foreign subsidiaries in Canada was at 25.8 percent, by 1981, that figure had dropped to 23.4 percent. In 1971 we also find that 71.9 percent of the exports were to parents or other affiliates of the subsidiary, whereas in 1981, that figure had risen as well to 76.0 percent. In essence, we see both a trend to fewer imports (with the greatest overall drop for the mining and primary metals industry, which likely reflects the drop in international commodity prices and the increase in competition for commodity sales internationally rather than any change in industry strategy), and more significantly, a trend to greater integration with the parent firm.

In terms of imports, we again see a moderate increase in the imports from abroad as a percentage of total sourcing purchases (38.1 percent in 1971 to 39.7 percent in 1981), while we see relative stability in terms of the imports of a subsidiary from parents and affiliates in terms of total imports (74.0 percent in 1971, 74.4 percent in 1981) (Industry, Trade and

Commerce, 1974; 1983). The impact of FIRA in diversifying sourcing and increasing exports is clearly not seen in these figures.

Jack Horner, Minister of Industry in 1979 (and thus charged with overseeing the operations of the Agency), and never a great fan of FIRA, commented after taking on his portfolio that:

I was not always just as keen on FIRA as I am today. But now I have had the advantage, as the responsible minister, of seeing at first hand the benefits we have obtained and are obtaining in terms of additional opportunities for Canadian workers, for our scientists and engineers, for managers and suppliers of goods and services, for Canadian consumers and investors (Teasdale, 1979:2).

Certainly, some investors are on record indicating that they have made concessions to FIRA in order to invest in Canada. The Korean automaker Hyundai, for example, reported that it had committed itself to exporting Canadian goods equivalent to half the import value of imported cars (Daw, 1985:C1).

More often though, as an observer of FIRA remarked, the process of securing significant benefit from an investor was detracting to the investor himself.

FIRA officials would get the CEO of a company down to Ottawa and ask him to pledge that his firm would meet certain criteria to ensure that his investment would confer significant

benefit to the Canadian economy. It wasn't so much the performance requirements which bothered the CEO; often he would have undertaken to do these anyway because they were a reasonable part of doing business in Canada. It was the fact that some junior bureaucrat was hassling him in a way that would get him fired if he were to talk that way to his Deputy Minister" (Confidential interview, Winter 1988).

Keith Ackroyd, President of the drug-store chain Boots Canada from the date of its original investment in Canada (with the acquisition of Tamblyns from George Weston Ltd) in 1977 until 1982, observed much the same thing from his own experience. Detailing his experience with the Agency at a conference celebrating the creation of Investment Canada, he commented that "[f]rankly, FIRA was irrelevant to the needs of the business, its customers, and the people who worked for it. It is difficult to think of a single thing we undertook to do ... which we would not have done in the course of normal, sensible business practice" (Ackroyd, 1986:43).

FIRA: The Unintended Consequences of Investment Regulation

It is likely, in the final instance, to prove impossible to make a determination of the positive and negative benefits of the Foreign Investment Review Agency on the Canadian economy. The most ambitious

study of foreign investors' reactions to FIRA as an obstacle to investment concluded that a small minority of investors indicated that they had been deterred from investing in Canada by Canadian state regulation, including the Foreign Investment Review Agency. Duncan McDowall's study points out, however, that most of the deterred investors wished to invest in petroleum, or communications and publishing (1984:68), sectors which we have already presented as coming under particular scrutiny in the Agency's administration of the Foreign Investment Review Act. In the case of publishing and communications, sectoral restrictions preceeded the creation of the Agency. Resource industries were also being protected by the Canadian state in the period before the creation of FIRA, largely through ad hoc interventions preventing a sale (the Dennison Mines case cited in Chapter Four, for example).

More interesting in many respects than the specific question of how much, or whether, investment was deterred is the question of the reaction given FIRA over time. This is instructive because there appears to be a clear breaking point in the responses to FIRA "mark I" (1974-1979) and to FIRA "mark II" -- the agency which was pledged to change, but which never did in the nationalist revival of the Liberal party. Despite the

fact that overall approval levels were only between 70 and 75 percent in the first three years of the Agency's operation -- a level considerably lower than any other period save the NEP years, criticism of the Agency was muted at best. Maclean's magazine commented in the summer of 1977 that FIRA was "falling apart in the face of ... government indifference" (Urquart, 1977:18).

Barrons, the widely respected American business magazine, commented that "one has the impression that the only U.S. business which wouldn't be cordially welcomed to Canada would be Murder, Inc." (Editorial, Barrons, July 1975). The Financial Post, bastion of opposition to state intervention in the Canadian economy, ran very few stories about the Agency at all, the most critical raising the question of how FIRA was going to monitor compliance to the performance requirements which it had imposed upon investing firms (Gordon, 1976:1,2).

Even the response of U.S. business and state actors was moderate. John R. Petty, a partner at Lehman Brothers, testified before a joint subcommittee of the U.S. House of Representatives and the U.S. Senate, remarking that:

...from time to time conspicuous
direct investors in Canada were
subject to "guidance" from
ministries in Ottawa regarding their

business plans. The guidance was not such that investors thought it could be ignored. The purpose was to create more employment in Canada. Therefore, FIRA in some respects did not make all that basic a change in doing business in Canada. However, the present procedure is more straightforward" (Petty, 1976).

Richard Vine, Deputy Assistant Secretary of State for European Affairs, underlined that ... "the shift in policy in Canada which found expression in the Foreign Investment Review Act was neither abrupt nor ill considered. It is not anti-American or anti-investment in its intent, nor to date in its administration" (Vine, 1976). Even as late as 1979, Julius Katz, Assistant Secretary of State for Economic and Business Affairs could not find grounds to criticise the performance of FIRA.

On a relative basis, one would have to say that Canadian policies in investment are more restrictive than ours. But, as a practical matter, Canadian investment policies are really quite liberal. Just recently, a few years ago, the Canadians did install an investment review board that screens investment. They have certain criteria by which they review investments and decided to permit, or not to permit them. In fact, it has really operated with great liberality. I cannot even think of a particularly outstanding case since the creation of that board where there was a turndown of American investment.

They generally do not look kindly on takeovers that do not contribute anything to the economy. As I say, I cannot think of a recent case that was particularly -- at least, that comes to my attention -- where there was sufficient concern that somebody came to the government and complained about unfair treatment (Katz, 1979).

It is in 1980 that we can identify a clear turning point in attitudes toward the Foreign Investment Review Agency, and that turning point has implications for the state's own perceptions of its place in the patterns of international investment. Approval rates in the fiscal year 1979/1980 were still higher, on average, than they had been in FIRA's earlier days, making it difficult to argue that the restrictiveness of the FIRA process was to blame for a shift in opinion. Superficially, at least, it is apparent that the heightened negative reaction was in response to plans announced by the Liberals during the winter election campaign that FIRA would be strengthened. Clearly vitriolic accusations were made. Writing for The Financial Post, Philip Teasdale claimed that the underlying reason for the "Canadianization" of firms (such as Husky Oil, Trizic, Anaconda, Odeon Holdings, Slater-Walker, and MLW-Worthington) lay in the "desire of the foreign owned-firms to escape from FIRA's control" (1980:2).

Teasdale appeared to ignore the reality -- that FIRA had no authority to intercede in the activities of foreign owned firms operating in Canada unless they sought to acquire a Canadian firm, or to expand into an unrelated business.

In the transition from 1979 to 1980, the American state's benevolent reading of FIRA also began to change. The chair of the U.S. House of Representatives subcommittee on Consumer Protection and Finance offered that FIRA was "largely subjective and unpredictable....[t]here are no published standards, no objective standards" (Scheuer:1980). The Executive of the Detroit International Bridge Company, R.W. Lich, testifying before the same subcommittee, complained that "...compared to the relatively lower or nonexistent barriers which exist on our side of the border, the Canadian act clearly puts Americans in a disadvantageous position" (Lich, 1980). The issue of transparency was a sensitive one. An official representing Canada in the United States commented in an interview that

FIRA is objectionable to foreign investors because they don't understand how decisions are reached. Placing an application before the Agency seems to them like playing the slot machines; they pull the lever once and get three different fruit, so they pull again and get three lemons. They don't understand what makes the outcome

different" (Confidential interview, Autumn 1984).

Several processes seem to be at work here. To begin, as Gordon (1976) alluded to in his comments about performance requirements and FIRA, Agency personnel were simply becoming more experienced with the process of screening investment. They were better able to negotiate the specifics of the investment application, and were gaining a better understanding of the nature of the benefits which could be extracted from potential investors. FIRA agents, over time, simply became better at doing their jobs. Unfortunately, they became better at those jobs in a time of economic upheaval and reduced international investment flows. Where the state had believed that Canada was so attractive as a location for investment that it could bargain with potential investors at will (without incurring a cost in terms of the diminution of investment flows) it was becoming clear that in a period of economic crisis, this equation no longer seemed to hold. FIRA officials were themselves very aware of this changed equation, arguing that "whereas in the 1970s, Canada had little trouble attracting investment, by 1980, the situation had changed. Canada had to compete for investment" (Confidential interview, Investment Canada, Winter

1987).

Even if FIRA officials were getting better at their jobs, without a concomitant decrease in investment proposal allowances, we cannot explain the sudden outburst against FIRA in 1980 -- before the NEP was put into place, allowing FIRA to act as an element of a sectoral industrial policy. There is little doubt that the vague plans of the Liberal government to monitor existing investment and to play a "Canadianization" role by offering "first crack" at the sale of a firm in Canada to Canadian firms went far beyond the original function of the Agency and was therefore a matter of concern. FIRA never did expand its role, however -- negative response on this basis implied a response to pledges rather than to reality.

What appears more likely as the source of negative assessments of the Agency is the reality of the changing U.S. role in international investments and the growing financial capacity of Canadian capitalists. It is instructive, for example, that the negative evaluations of FIRA cited earlier as testimony before a committee of the U.S. Congress were contributing to a hearing on the possibility of legislating a U.S. investment reciprocity act. Any investor wishing to acquire five or more percent of a U.S. corporation would be, under the terms

of this legislation, subject to the same penalties and regulations as a U.S. investor attempting to acquire control of a firm in the investor's home country. As Table 3.9 illustrates (Chapter Three), inward direct investment was flooding into the United States with virtually exponential increases each year.

This reality of course was exacerbated by the National Energy Program, and the enormous Canadian investments which resulted. Canadians were not only repatriating sectors of their economy (mostly from U.S. investors), they were investing in the most lucrative international market as well -- the United States. As James J. Harrison, the secretary and general counsel of McCormick and Company (a specialty food firm in Maryland) complained before the U.S. Congress, Brascan had just spent in excess of \$70 million dollars acquiring equity positions in six American consumer products companies:

As per the discussion of FIRA, and the immense restriction and problems that American companies would have in buying shares of Brascan or anybody else in Canada, again it seems unfair and absolutely the opposite of anything smacking of reciprocity that Brascan can come in and, it chooses, acquire six American companies with no more basically than the filing of the required forms with the SEC [Securities Exchange Commission], and a phone call to their broker.

That is about the sum and substance of what they would have to go through. American companies would, by and large, have no chance of going the opposite way (1980).

These observations as to the relative successes and failures of the review process do little to convince us that the Agency was a successful watchdog, altering fundamentally the nature of branch plant investment in Canada. Rather, they seem to indicate that FIRA was not a serious long term and cross-sector inhibitor of investment.

FIRA: SECTORAL INVESTMENTS

In order to come closer to an understanding of the development of the Canadian industrial structure in the FIRA era, we must turn our attention to more detailed sectoral profiles of the Canadian economy. Examining the processes at work in these sectors will allow us to draw more detailed conclusions as to the success or failure of the Foreign Investment Review Agency in terms of the assumptions it embodied than permitted by an examination of statistical profiles. As an Agency created to "protect" the Canadian economy from the consequences of branch plant investment, FIRA's greatest effectiveness would most likely have been achieved in

international circumstances favouring branch plant investment. In a world in which other forms of investment were becoming more prevalent, however, FIRA quickly became marginalized in terms of the real effects which it could have on the pattern of foreign direct investment seeking to locate in Canada.

We begin our sectoral review by examining changes in the ownership structure of Canadian industry, focussing on the transition between 1967, the base year used by the Gray Report, and 1985, the final year of operation of the Foreign Investment Review Agency.

Table 6.7: Foreign-controlled Share of Total Non-financial Assets and Sales, by 33 Major Industries, 1985

	% Majority of Non-Resident Ownership as Measured by		
	Assets	Sales	Profits
Agriculture, forestry and fishing	3.5	2.9	10.2
Mining			
Metal Mining	17.5	26.0	7.9
Mineral Fuels	37.7	58.0	67.6
Other Mining	25.2	31.4	10.1
Total--Mining	32.1	48.0	67.5
Manufacturing			
Food	32.2	26.4	53.4
Beverages	22.3	36.6	20.4
Tobacco Products	99.8	98.0	99.9
Rubber Products	90.8	88.1	84.2
Leather Products	15.5	10.7	31.6
Textile Mills	51.5	52.3	45.1
Knitting Mills	11.9	9.2	14.7
Clothing Industries	10.6	9.2	13.6
Wood Industries	14.7	13.0	8.1
Furniture Industries	16.6	13.6	11.9
Paper and allied Industries	24.5	26.1	39.3
Printing and publishing	11.9	12.7	12.6
Primary Metals	20.2	16.8	45.9
Metal fabricating	25.0	25.4	29.1
Machinery	46.7	52.1	62.7
Transport Equipment	73.4	88.3	94.4
Electrical Products	53.4	67.8	66.6
Non-metallic minerals Prods.	70.8	54.9	71.4
Petroleum and coal Products	42.1	57.4	46.7
Chemical and Chemical Prods.	69.1	76.0	87.1
Miscellaneous manufacturing	35.2	35.8	40.4
Total--Manufacturing	41.7	49.2	58.4
Total--Construction	8.5	6.9	5.3

Table 6.7 (Con't)

% Majority of Non-Resident Ownership
as Measured by

	Assets	Sales	Profits
Utilities			
Transportation	4.4	5.4	15.0
Storage	3.8	1.4	9.8
Communications	12.1	11.1	13.6
Public utilities	0.3	3.2	2.1
Total--Utilities	3.3	5.4	15.0
Wholesale Trade	23.8	25.8	26.5
Retail Trade	13.3	12.0	9.2
Services	16.0	15.4	24.0
Total:			
Non-financial industries	23.4	29.0	40.7

Source: CALURA (1987) Annual Report, 1985, p. 46.

Certain trends of the pre- and post-FIRA eras are apparent from a comparison of between the earlier 1967 and these 1985 ownership statistics. As expected, foreign ownership decreased in those sectors where FIRA acted within an "industrial policy" framework: petroleum and coal products (assets 42.1 percent in 1985 versus 99.5 percent in 1967), printing and publishing (assets 11.9 percent in 1985 versus 21.0 in 1967), although foreign ownership did increase in the communications industry (12.1 percent in 1985 versus 1.0 percent in 1967).

Additionally, the trend to decreased foreign ownership in the manufacturing sector in general is evident from the decrease in foreign ownership in several industries within the manufacturing sector. A decline in foreign ownership of assets was evident in the wood and furniture manufacturing industries, the paper and paper products industries, primary metals and machinery manufacturing, and chemicals and chemical products manufacturing. Wood, furniture and paper products industries were industries in which Canadian ownership was well above 50 percent in 1967, while the other industries reflect a more dramatic change of ownership. Overall, the ownership of manufacturing assets has declined in Canada from 58 percent in 1967 to

41.7 percent in 1985. Interestingly, however, foreign enterprises continued to account for over 50 percent of the profits in the manufacturing sector, down from 63.6 percent in 1967 to 58.4 percent in 1985 (clearly not commensurate with the drop in foreign ownership of assets). Foreign enterprises, while reducing their level of ownership of the Canadian economy in general, clearly remain important in those sectors characterized by the more efficient generation of earning power, as evidenced by their profits to assets ratio.

This fact is in part explicable by the concentration of foreign firms in a few industrial sectors which are far more capital-intensive than the average, such as automobiles and pharmaceuticals, and which enjoy sufficient market power and/or economies of scale to permit significantly higher profit margins. Despite changing ownership figures, the largest foreign enterprises continued to be engaged in the extraction and refining of oil, and in the manufacture of automobiles. General Motors of Canada Ltd., Ford Motor Company of Canada and Chrysler Canada Ltd. are among the top ten firms operating in Canada, as is Imperial Oil Ltd. In contrast, the leading Canadian private enterprises are predominantly found in utilities, in mining, smelting and refining, and in the wood

industries. There are, in addition, several large Canadian conglomerates (Argus, Power Corporation, or Canadian Pacific Enterprises, for example) (CALURA, Annual Report, various years). Foreign ownership may have dropped as a whole, but it remains highly concentrated in the capital intensive sectors of the Canadian economy, consistent with the oligopolistic advantages of many foreign investors. These investments were the branch plant investments of early U.S. penetration into Canada, the first wave of investments for Vernon's analysis.

Further insight into the nature of economic activity in Canada as it relates to changes in the international system can be obtained from an overview of changes in investment patterns in each of the major economic sectors in Canada. While we can explain a decrease in ownership of petroleum resources in the early 1980s to the effects of the National Energy Program, for example, we gain little insight from this into reasons for the decline of foreign ownership in other sectors. Closer examination of the changes within each sector over the term of FIRA's authority permits us to draw conclusions as to the impact which the Agency could have had in a changing environment. Each of three sectors will be considered in turn.

Resource Investments

The collapse of international oil prices in 1982 both undermined the revenue-generating premises underlying the National Energy Program and ensured that the state would not try to "Canadianize" more industries. Despite this, resource industries, and manufacturing concerns based on resource extraction and processing, continue to be a crucial industrial sector driving the Canadian economy. Not surprisingly, resource industries have been most attractive when international commodity prices are highest, and least attractive in periods such as the one during which FIRA operated, characterized by the depression of commodity prices in different industries at different times throughout the whole period.

Traditionally, resource industries in Canada have had very distinct foreign ownership patterns. The mining industry, for example, was only 11 percent foreign owned by total number of corporations operating in the industry in 1977, a percentage which dipped below 6.5 by 1982. Despite this, foreign owned corporations continued to control close to 50 percent of the assets in the industry, near 60 percent of the sales, and close to 70 percent of the profits (CALURA, 1982). Table 6.7

reveals that, by 1985, foreign owned firms owned only slightly above 32% of the assets in the industry, but still made nearly 70% of the profits. Foreign controlled firms have tended to concentrate in profitable sectors, largely mineral fuels, while Canadian operations tend to be concentrated in the mining of non-ferrous metals. The nickel industry, for example, is wholly dominated by Canadian firms, and has been troubled by wild international price fluctuations. Within metal mining industries, we only find a high foreign presence in iron mining. Both iron mining and mineral fuels have tended to be more profitable among resource industries than have the more general metal mining industries.

Changes in ownership structure throughout the period of FIRA's tenure resulted from primarily two phenomena; the National Energy Program "Canadianization" provisions, reviewed earlier, and the extension of Canadian control through a series of ad hoc takeovers, industrial reclassifications, and firm expansions rather than through the establishment of new firms. In 1976, for example, the Potash Corporation of Saskatchewan acquired the assets of the Sylvite division, the potash operations of Hudson Bay Mining and Smelting Company. In 1978, Petro-Canada Explorations, Inc., a subsidiary

of Petro-Canada, issued preferred shares to a group of Canadian banks, a move which was sufficient to more than double the corporation's assets (CALURA, 1978). In 1976, Dome Petroleum was reclassified from United States to Canadian control, when the reciprocal buying of shares by Dome Mines Ltd and Dome Petroleum Ltd. "clearly demonstrated that even though there existed some foreign ownership of the two companies, control was being exercised by their predominantly Canadian management" (CALURA, 1976:49)[2]. These increases in the Canadian share of assets in the industry are certainly more attributable to the specific decisions of Canadian governments and firms than to any one particular act of the Foreign Investment Review Agency.

Officially, Pierre Trudeau's 1974 and 1980 election pledges of 50 percent Canadian ownership of the petroleum industry remain on the books. Brian Mulroney reiterated the commitment in the 1984 election, agreeing that Canadians should own and control the oil industry (Toulin, 1984). However, the most recent report of the Petroleum Monitoring Agency indicates that Canadian ownership is once again beginning to slip with the stabilization of, and potential increases in, international petroleum prices, and an improvement of the market for petroleum. Canadian ownership figures

were at their peak in 1985 (as illustrated in Table 6.1) with the take-over of the U.S.-owned Gulf Canada by the Reichman family and Petro-Canada. Since then, some of the smaller Canadian firms have been purchased by larger foreign concerns better able to withstand the crash of the oil market. In late 1987, the new Mulroney government allowed the sale of Husky Oil (which had participated in the "corporate grab" of 1981-82) to foreign interests. Specifically, Ottawa approved Hong Kong industrialist Li Ka-shing's \$484 million investment in the Calgary-based Husky Oil [3]. (Plaskin, 1988:F9; Ferguson, 1988:F8; Critchley and Reguly, 1987:1).

Imperial Oil acquired Sulpetro Ltd., and Sudbath Explorations, while Swedish-owned Erickson Resources acquired a controlling interest in Trans-Canada Resources Ltd. The most heralded takeover, of course, is the purchase of the once-mighty, but fiscally devastated, Dome Petroleum by Amoco Canada Petroleum Company (owned by the Chicago-based Amcco Corp.), finalized in September 1988 (Montreal Gazette, September 2, 1988:D6). Also expected are the partial purchase of Bow Valley Industries Ltd. of Calgary by British Gas PLC of London, and the now foreign Husky Corporation's takeover of Canterra Energy Ltd. of Calgary. Canadian ownership of assets in the petroleum industry is

expected to decline to between 41.7 and 34 percent, depending on the final agreements reached in these prospective takeovers (Ferguson, 1988:F8, Plaskin, 1988:F9). While these figures are certainly better than the near 100 percent foreign ownership of the industry in the late 1960s, there is little doubt that less stringent investment regulation has contributed to the return of some of Canada's energy resources to foreign hands. Clearly, there has been a change in the attitude of the Canadian state, despite the grandfathering in the Canada-U.S. trade agreement of Energy Minister Marcel Masse's 1986 policy limiting takeovers of Canadian petroleum companies to those in financial trouble.

The reassertion of foreign interests in the petroleum industry is not unexpected. A lack of vigilance -- or recognition of a problem -- on the part of the Canadian state had meant that the industry was virtually 100 percent foreign owned in 1967. The creation of Petro-Canada and its subsequent pattern of acquisitions produced a decline in foreign assets in the industry, and the Canadianization provisions of the National Energy Program, together with the willingness of Canadian banks to provide access to capital, extended Canadian ownership. Canada still constitutes the safe source of resources identified in the Paley and Shultz

reports, however, and a change in state attitude toward Canada's historic open door investment policy can only produce the result which has been identified.

Furthermore, the high barriers to entry in resource extraction and processing industries ensure that only capital-rich investors can bid for major acquisitions. Many of those investors, such as Amoco, are necessarily important players in a highly concentrated industry.

While there has been a resurgence in foreign investment particularly in Canadian petroleum resources, there is no indication that Canada is particularly attractive to investors as a location for the processing of other resources. As U.S. bankers commented, "[n]atural resources are under the gun worldwide I feel very sorry for Canada because it has built its whole existence on natural resources" (Walkom, 1984:5). Sympathy aside, increased competition from developing countries makes it more difficult for Canada to attract resource investment. Even if resource prices were to rise significantly and thus promise higher returns, investors might choose to direct their investments toward countries such as Brazil and Indonesia, which combine low wages with high-grade resources.

Service Investments

Service sector pattern of investments in Canada are an illustration, in many instances, of areas in which state regulation of direct investment has offered protection to domestic interests. As argued earlier, however, this protection predated the creation of FIRA, and relatively low ownership levels cannot be attributed to any extraordinary vigilance on the part of the Agency. As well, though (see Tables 6.3 and 6.4), the service industry was the sector in which there were the greatest number of applications for both new business and acquisition investments, and the only sector in which new business applications outnumbered acquisition applications, reflective of the dynamism of this sector as an increasing focus of economic activity in Canada. We must not ignore the fact, however, that the dollar values for investment proposals, whether acquisitions or new investments, were lower for the service sector than for other sectors, reflective of the nature of economic activity in this industrial group.

Reference to Table 3.13 reveals that foreign ownership of service sector industries did increase in the FIRA years, to 28.8 percent of all service industries, as we would expect from the activity indicated above. Many of these sectors in Canada,

however, due to the pattern of Canadian economic development, are subject to direct equity participation by federal, provincial or municipal governments -- including rail and air transportation, broadcasting, electric and water utilities, and telephone companies. The potential for foreign ownership growth in these industries is thus particularly limited. Government participation, and regulation protecting these assets (See Appendix I) accounts for the high level of Canadian control of transportation, communications and utilities industries. In terms of private sector investments, foreign-controlled activities were concentrated particularly in hotels, restaurants, and taverns; computer services; and the leasing of trucks, cars, machinery and equipment. Canadian controlled operations are dominant in the recreation and accommodation services industry, as well as in utilities, transportation and communication, as already outlined (CALURA, various years).

Service sector investments tend to differ from investments of goods-producing industries because they can only rarely expand into a market through the export of their product. In their nature, therefore, they are fundamentally different than the traditional branch plants, which invested into a market as an alternative

to export. Retail operations, such as Ikea, Brettons, or Marks and Spencer, have moved to Canada in order to "test out" the North American market before moving into the U.S. market itself. These firms have hoped to save themselves the cost of a larger failure which headfirst investment into the United States might have brought. The Canadian market was, in these cases, predominantly attractive because of geographical proximity, and relative similarity, to the United States (Confidential interview, Investment Canada, Winter 1988).

Retail operations, of course, do not mark the only kind of service sector, or even the most interesting one. The growth of consulting -- particularly with the development of specialized computer software -- has created a "new idea" type of innovative foreign investment. FIRA reported that it received applications by foreign computer companies specializing in software programs designed for the use of lotteries, the dental profession, auto dealerships, aircraft maintenance firms, racetracks and real estate firms. As well, speciality services have been offered by foreign investors to those concerned with air and water pollution, footwear manufacturers, the forest products industry, and waste disposal firms (Swedlove, 1980:15). As well, new service sector investment has come from

firms with an established manufacturing capacity in Canada who are interested in becoming involved in the distribution or servicing of their operations, or from financial institutions who wish to service their multinational clients by following them into a host market. Japanese financial institutions, for example, have overseas operations worth more than twice those of its carmakers and consumer-electronics firms put together. In large part, these institutions have moved abroad by the need to follow their domestic clients. Seven of the world's ten largest banks are now Japanese, with the bulk of their foreign investments in North America (34%), Europe (33%) and Latin America, including Caribbean offshore centres (24%) (The Economist, 5 March 1988:84). In Canada, the liberalization of the Bank Act has ensured that this internationalization of finance has grown to include a foreign bank presence in the country.

Manufacturing Investments

Manufacturing investment during the FIRA years has been the least dynamic of the three sectors. In large part, this is due to the performance of U.S. firms and to the changes in United States foreign investment patterns. Canada's Royal Commission on Corporate

Concentration, which reported to the government in 1978, pointed to precisely these changes in the pattern of foreign investment in the manufacturing sector. They concluded that first, American investment in manufacturing was bound to slow as the comparative advantage offered them by their size began to erode. As we discussed in chapters Two and Three, American multinationals began to feel the competitive pressure from other MNCs, particularly those from Europe and Japan, but also including the emerging firms from the newly-industrializing countries. These competitive pressures are reflected in the rate of divestment of U.S. multinationals. In the 1961 to 1965 period, the ratio of new investments to divestments for U.S. firms was 3.3; by the 1971-1975 period, that ratio had dropped to 1.4 (Foreign Investment Review, 1978:22). In Canada, the Royal Commission argued, divestment of American manufacturing assets through the 1970s had particularly taken place in non-concentrated industrial sectors -- consistent with Hymer's thesis that oligopolistic advantage is likely to be the best predictor of foreign investment behaviour. As mentioned earlier, though, the decreasing American presence in Canadian manufacturing assets can be easily overstated; American firms continued to generate nearly 60 percent of the corporate

profits in the sector.

While the decline of American investment in manufacturing has to some extent been taken up by the increased presence of other foreign assets, it cannot be argued that the interest in non-American firms in Canada as a particularly attractive location for manufacturing investment has been overwhelming. The Japanese, for example, have not invested in Canadian manufacturing as heavily as they have in the United States and in Europe. Their major investments in automobile production have been made in part because of Canadian barriers against the import of Japanese cars (Critchley and Reguly, 1987:4; see also The Economist, 27 February 1988:54-5). Japanese investors also prefer joint venture and minority equity investments in Canada over the fully owned subsidiary; less than one third of Japanese subsidiaries abroad are majority owned. In Canada, the Japanese have invested in resource development and resource-related industries in order to secure for their industry at home the needed raw materials resources. As such, patterns of Japanese investment have been characterized by changing targets over time: from non-ferrous metals and forest products, to coal, then to oil and to uranium (Gherson, 1979:5). Richard Wright has gone so far as to call Japanese investment in Canada

"uninspiring". "Investments in the past two years, such as the purchase of a McDonald's restaurant in Toronto and a lobster plant in New Brunswick, and the start-up of an interior decorating business in Vancouver, will transfer little money or technology to Canada" (Wright, 1987:44).

European investors have been more active in acquiring the assets of formerly U.S. subsidiaries than have been the Japanese -- in part because the divestment of U.S. assets in European markets can mean that the purchasing European firm also indirectly acquires the Canadian assets of the same U.S. parent. Western European investors also respond to Canada because of its abundance of relatively inexpensive energy. British banks have expanded their assets since the liberalization of Canada's banking laws, while German firms have been acquiring Canadian real estate assets as a result of the growing German tourism market in Canada (Howarth, 1980:8).

All of these investment plans and proposals must be seen in the light of a very different climate for international investment, however. Canada has not fared particularly well as a location for new manufacturing investments because of changes in the nature of that investment itself. As we discussed in Chapter Two, MNC

investment strategies have been changing in response to their need to maintain their competitive position in an international economic environment under crisis. Firms chose internationalization strategies through the 1970s in response primarily to the cheaper labour of the developing countries. Even Canadian companies have participated in the process. Massey-Ferguson had responded to the lowering of tariff barriers amongst European Community members by internationalizing production throughout Europe in order to take advantage of particular factor assets in different locations. The firm produced wheel assemblies, chassis, and engines in different locations throughout Europe, and brought them together for assembly (Bishop and Crookell, 1986:311-12). In the Canadian case, though, internationalization strategies made little sense for MNCs in the 1970s. Canada -- at least until its dollar began to depreciate rapidly in the latter part of the 1970s and early 1980s -- could not offer the incentive of a substantially lower wage rate. The plant shut-downs and labour strikes endemic in the 1970s did not provide an environment conducive to attracting new investment capital either.

The extent to which this is the case is observable in FIRA's own analysis. Acquisition proposals in

manufacturing before the Agency consistently outnumbered the new business proposals in manufacturing (see Tables 6.3 and 6.4). Furthermore, FIRA officials have suggested that most of the acquisition applications were in fact made by MNCs already operating in Canada who wished to extend their business into a sector not directly related to their main line of existing production (over 70 percent of applications). As could be expected, most of these applications were designed to integrate horizontally or vertically with existing operations in Canada or with parent operations, and of these, horizontal integration with existing Canadian operations was the most often cited factor for new acquisitions (76 percent of the cases) (Foreign Investment Review, 1979:13).

These same observations have been made by other analysts. The Economist, for example, points to the fact that the consolidation of U.S. firms in their activities abroad has meant (as we have shown to be the case in Canada), that these firms have been more profitable. U.S. firms, however, have not tended through the late 1970s and 1980s to open new businesses; rather, they have invested in existing subsidiary operations. In addition, the expansion of existing activity has been far more important than the process of

U.S. investment acquisitions. "While there have been a few multi-million dollar American takeovers of foreign firms in the past 18 months..., such investment is trivial compared with the re-investment of earnings" (17 September 1988:71).

This review of sectoral investment has confirmed our suspicions. FIRA, best suited, as we have argued, to deal with the branch plant characteristics of new manufacturing investment proposals, operated in an era in which these investments were declining. This is not to say that the manufacturing sector in Canada did not continue to be characterized by a branch plant structure, but only that the specific design of the Agency suited it to review a type of investment proposal which was less likely than ever before to come to Canada. State managers in Canada created an Agency to deal with a problem as they had learned about it. The previous decades of branch plant investment had not led them to seriously consider that investment patterns would change to such an extent as to marginalize their Agency. This reemphasizes an argument presented in Chapter One: State managers make policy decisions within contextual layers which are constantly changing. The net effect of this is that state managers may act on the basis of perceptions which no longer adequately

capture the context in which they are operating.

**WORLD PRODUCT MANDATING: WHERE HAVE ALL THE BRANCH
PLANTS GONE?**

If FIRA was not able to rectify any of the longstanding problems of the Canadian economy and its truncated industrial sector, does this imply that all of state manager learning with respect to this pattern of development in the Canadian economy has been for naught? In particular, as we argued in Chapter Two, how will Canada compete in an era in which knowledge intensive production is gaining ground in a whole range of industries -- given that one of the primary characteristics of the branch plant economy is poor performance in technological research and development? Certainly, there is no evidence that these characteristic problem conditions improved under FIRA's tenure; Canada's trade balance in high technology goods moved from bad to dismal (see Table 6.8).

Table 6.8 Canadian trade balance in high technology
goods,
Selected Years, 1968-1981 (millions of \$)

1968	-2,046
1971	-2,512
1974	-4,982
1976	-5,912
1978	-6,843
1980	-8,625
1981	-9,555

Source: Gassend, Max (1982). "Canada's International Trade Performance of Manufacturing Industries by Levels of Research Intensity." Ottawa: Ministry of State for Science and Technology (November).

Clearly, the concerns underlying the branch plant thesis of Canadian industrialization have not been mitigated by time or by FIRA, and state managers have accepted this. Industry, Trade and Commerce's Strengthening Canada Abroad, for example, reflected a grave concern with the lack of Canadian technology trade, and helped to champion a world product mandating model.

In recognition of the historically poor performance of subsidiaries operating in Canada in redressing their export and research and development problems (see Dalpe, 1987, for example), alternative strategies have been identified to resolve the Canadian branch plant dilemma. ITC's Report called for the public encouragement of "worldwide or regional marketing rights" for subsidiaries operating in Canada (Industry, Trade and Commerce, 1979:17). The Department of

Regional Industrial Expansion, in part the successor to ITC, and the Department of Supply and Services began in the mid-1980s to jointly administer a program of subsidies and tax concessions for the "rationalization" of branch plants operating in Canada. This rationalization has come to mean, in its Canadian context, the procurement of world product mandates for subsidiary operations. In fact, as late as the summer of 1988, an official of DRIE commented that world product mandating was still the "name of the game" in the rationalization of high technology firms in particular. "I am constantly told to try to get world product mandates for subsidiaries operating in Canada. There's a lot of pressure for us to do this" (Confidential interview, DRIE, summer 1988).

The Gillespie guidelines for good corporate citizenship, interestingly enough, are at the basis of this incentive to rationalize program. We will recall that these guidelines looked for the development of an autonomous capability in subsidiaries for technological innovation, and for production and marketing, as well as for firms to strive for "a full international mandate for innovation and market development", enabling the Canadian company to "improve its efficiency by specialization of productive operations". External

Affairs' Publication A Review of Canadian Trade Policy pronounced its support for world product mandating along the lines of the Gillespie guidelines, and they have gone on to form the centrepiece of a program administered jointly by the Department of Supply and Services and DRIE (Supply and Services, 1985). This program uses the Gillespie Guidelines to assess whether a foreign subsidiary operating in Canada is "rationalized" or not. If it is, it is treated as a Canadian-controlled firm for government procurement purposes [4] (Supply and Services, 1985).

We will recall that world product mandating, at least in the ideal, grants to the subsidiary the right to sell a specific product or product line on a world-wide basis. As a strategy to reduce costs and risks, the allocation of WPMS is seen as one which allows the multinational to tap into local research and development resources, to gain access to government procurement contracts of the host country, and to take advantage of host country investment tax credits and export subsidies. Foreign subsidiaries operating in Canada have received such mandates; Digital Equipment's subsidiary has five mandates, including one top-of-the-line personal computer and the back panels of all DEC's machines (The Economist, June 18, 1988:70).

Westinghouse and Honeywell have about 20 world product mandates, Honeywell, for example, producing temperature control systems, and Westinghouse producing gas turbines (Bishop and Crookell, 1986:318). Most of the aeronautical firms operating in Canada also have world product mandates [Pratt and Whitney (small gas turbine engines), Litton (commercial avionics, electronic systems), McDonnell Douglas, and Garrett Manufacturing (aircraft temperature control systems, emergency beacons)] (Dalpe, 1987:359; Bishop and Crookell, 1986).

Much debate has grown around the notion of world product mandating and Canadian subsidiary operations. The Ontario Advisory Committee on Global Product Mandating, arguing that there were few "pure" world product mandates available (mandates which would imply complete responsibility for all phases of research and development, which would imply responsibility for all phases of production, and for all phases of product marketing and exporting), contended that incentives should be provided to firms who have managed to acquire a "specialized mission strategy" (implying the specialization in one or a few product lines for international exports) (Government of Ontario, 1980:3). The concept of world product mandating has become stretched at best in this perspective, but it is

consistent with the perspective of Canadian state managers. Officials from DRIE indicated that their prime concern in acquiring world product mandates (however defined) was to increase the manufactured exports of Canadian subsidiaries, rather than to worry exclusively about the capacity of these firms to engage in their own research and development (Confidential interview, summer 1988). Interestingly, this continues to reflect the "trade" obsession of the old ITC, despite the fact that the trade service was by then incorporated into the Department of External Affairs. Foremost in the minds of these officials was to increase investment, to make Canada a more attractive location for investment, reflecting in itself a changed perception of Canada's place in the pattern of foreign investment. World product mandating, complete with incentives, was perceived to be a vehicle to accomplish this.

Interestingly, world product mandating has brought about a convergence of nationalist and continentalist views, with nationalist groups such as the Science Council of Canada arguing in favour of WPMs as a means to develop Canada's R & D capacity in an era of lower tariff barriers, and the continentalists -- such as state managers at Finance, and to some extent, those at DRIE -- supporting WPMs because such a strategy is

consistent with the reduction of trade and investment barriers (Proulx, 1982). Implicit in these arguments has been a new view of the role of the state, and indeed, of Canada's location in the global economy. Canada can no longer count on foreign investment, unlike assumptions which underlay the Gray Report, and must compete for investment projects. The state, therefore, must facilitate investment, rather than regulate and potentially deter investment.

The adoption of world product mandating as a strategy to combat the effects of the branch plant economy appeared to increasingly marginalize the Foreign Investment Review Agency. While FIRA officials were certainly not ignorant of the important role which world product mandating was beginning to assume as a resolution for Canada's industrial policy dilemma, they were frustrated by a lack of awareness of the changing nature of Canada's international location. It is true, for example, that FIRA had been used as a mechanism to ensure the allocation of world product mandates; as early as 1975, FIRA officials negotiated the allocation by Brown Boveri of a world product mandate to Conron Limited when the former acquired its electronic division assets (FIRA, Annual Report Supplement, 1978-79:7). Despite this, an official of the Agency commented that

"while we know that something is going on, we don't know how much of it, or with whom. We don't know whether we should be targetting industries, or how to go about it if we should" (Confidential Interview, Investment Canada, Winter 1987). Given that FIRA's mandate incorporated investment criteria which suggest that it was to be on the forefront of the battle against the more severe consequences of branch plant investment, it is disconcerting to find that it was largely ignorant of those international processes which might make Canada particularly attractive for new forms of international investment.

The inability of FIRA officials to "learn" about world product mandating -- at least beyond the point of simply knowing of its existence -- tells us much about FIRA officials as state managers. FIRA's mandate might have been vague, but it was also narrow. It was a regulatory agency without real decision making authority, and its response to any application for foreign investment was intrinsically regulatory in nature (review the application, make a recommendation). FIRA officials faced serious limitations in attempting to learn which are not faced by either government departments or regulatory agencies with decision making authority. FIRA's mandate effectively "interpreted" the

issue of foreign investment for Agency officials, and as a result their capacity to learn appears to have been structurally limited by their organizational setting. More importantly, however, unlike most other bureaucracies, FIRA did not represent an identifiable domestic constituency. At the time of its creation, it can be argued that it served the interests of the nationalistic new middle class -- but only in a sense, given that these class actors were largely disenchanted with the Agency. Once the nationalist movement ceased to play a significant role in policy formulation, however, FIRA was left in a vacuum, without a constituency which would structure an interpretation of the changing international investment environment.

In the sense of "learning", the mandate of Investment Canada is considerably broader. Its regulatory role is limited, and will be increasingly so when the full provisions of the Canada - U.S. free trade agreement take effect. Its investment promotion role, however, allows it not only to respond to foreign investment from a number of different perspectives, but also permits them to target a particular domestic constituency. In 1989, for example, Investment Canada has targetted mid-size, high technology Canadian firms, and is working to develop programs to try to meet their

industrial needs (arrange a joint venture with a non-Canadian firm which would allow for the possibility of technology transfer, for example) (Confidential Interview, Investment Canada, September 1989). The constituency will be built up one firm at a time, though. Even an organization such as the Canadian Advanced Technology Association (CATA), which in itself clearly reflects an awareness of the contemporary importance of knowledge-intensive production, does not have an organizational position on foreign investment due to the diversity of the opinions of its members.

Despite the broadened mandate of Investment Canada, the country does not appear destined to receive any greater inflow of capital than would otherwise have been the case under FIRA's tenure. Table 3.8, for example, indicates that Canada continues to attract an uneven -- although recently increasing -- pattern of investment flows, while continuing as well to invest larger amounts of capital abroad even in the period beyond FIRA. The changing role of the United States as an international investor, as we have earlier outlined, does not lead us to anticipate any near future large investment flows from the United States, Canada's historical principle investor. The Toronto Star, for example, has surveyed economists and concluded that "[e]ven with the welcome

mat out,...[there would not seem to be] any reason why all of a sudden we're going to have a big in-flow of foreign investment.... [There is no reason to expect that] Canada [will] attract new net capital.... [It does not seem that] changing FIRA is going to make any difference" (Toulin, 1984:D1). Headlines such as the Ottawa Citizen's "Investors aren't breaking down doors as Canada opens for business" heralded the transition to the new investment climate in Canada (June 28, 1985). The Citizen cited new international competition for investment as a possible reason for the Canadian failure to attract new investment, and certainly other countries (Australia and France, for example) have been increasing their efforts to attract investment dollars (Plommer, 1985; Globe and Mail, 29 July 1986). As an Investment Canada official noted, there are six thousand jurisdictions in the world which are promoting themselves as attractive investment sites. The fact that Canada announces that it is open for business is hardly enough (Confidential Interview, September 1989).

In a new investment climate in Canada, it still appears as though businesses which have a traditional resource-based competitive advantage (such as energy and petrochemicals) will continue to expand and remain attractive. While high technology manufacturers have

been successful in obtaining world product mandates for their operations in Canada, it may now appear that this trend is moving to consumer products firms; the Economist has reported that Procter & Gamble has recently announced plans to revamp its worldwide manufacturing operations, plans which "should make Canadian subsidiaries the main suppliers of some products" (18 June 1988:70). Finally, the strength of the Canadian economy and the relative position of the Canadian dollar are still likely to have more impact on investment flows than any specific restriction of a regulatory agency. David Hartman, chief international economist of Data Resources, Inc., a U.S.-based economic forecasting agency, may have defined the international situation better than most.

What we've seen is that the real rate of return to capital is now so attractive in the U.S. that corporations are investing here and even foreign capital is coming to America.... [However], if Canada and the U.S. are growing at roughly the same rate, if the investment climate is similar and Canadian tax policy compensates for the lower exchange value of the Canadian dollar, then I don't see any major change in Canada's ability to attract ... investment (Toulin, 1984:D3).

This chapter has brought us to some conclusions about the nature of state manager learning, and of the consequences of that learning for FIRA. It is clear

that there was some incommensurability between FIRA's mandate -- which permitted the screening of investment to obtain greater advantages from branch plant investment -- and the pattern of foreign investment in which Canada found itself located in the mid-1970s and early 1980s. There is no guarantee in the formulation of any national policy targetted to the international environment that the perfect fit will be found, and in the uncertainty created by the rapidity of international economic changes over the past two decades, the guarantee is bound to be impossible to give.

The problem with FIRA was not so much that the information about the Canadian place in the pattern of international investment flows learned in its creation was wrong, as that it was increasingly out of date. New branch plant investments might have been less likely, but the truncation of the branch plant economy still existed. Policies such as the one to encourage world product mandating recognized this, although the DRIE/Supply and Services initiative appeared principally designed to generate more exports, rather than to rectify any other deficiency of the branch plant. In this respect, the Gillespie Guidelines, with their emphasis on technology, may eventually become diluted in a manner reminiscent of the FIRA emphasis on exports.

Appendix I: Regulatory initiatives of the Canadian State
taken with regard to foreign investment; 1929-1973

In 1929, Canadian Airways, predecessor to Trans-Canada Air Lines and Air Canada, was formed, with capital contributions from both the Canadian Pacific Railway (the CPR) and the government-owned Canadian National Railways. Canadian Airways' president stated that this financial participation was to constitute a warning to American airline interests that Canadian Airways "was financially in an impregnable position" (Franck, 1976:58), and thereby not open for takeover. The consequence of this 1929 decision to retain air transport in the hands of Canadians has been to effectively ensure that not only air, but also rail and water transport, are, or have become virtually 100 percent Canadian owned.

The subsequent National Transportation Act provides for regulation by the Canadian Transport Commission of any direct or indirect proposed acquisition of an interest in rail, water or motor carriers with federal jurisdiction. As Franck has pointed out, the Commission uses a criteria of "public interest" in making its decision to allow or disallow an acquisition bid, a criteria which is broad enough to "include considerations of foreignness" (1976:58).

Similarly, under the provisions of the Canadian Aeronautics Act, the Canadian Transport Commission can exercise discretionary power with respect to any proposed changes of control over commercial air carriers. Additionally, as of 1963, under the provisions of the Air Regulations, two-thirds of the directors of a corporation owning a Canadian aircraft must be of Canadian nationality. Effectively, therefore, the Canadian Transport Commission has had the wide discretionary powers necessary to prohibit foreign takeovers of Canadian transportation corporations if it deems these not to be in the Canadian public interest.

In 1936, the Canadian Broadcasting Corporation was established, winning acceptance "in large part as a means of protecting radio from foreign control" (Fayerweather, 1974:10). Further, in 1951, provisions were added to the Canadian Broadcasting Act authorizing the Canadian Broadcasting Corporation to develop regulations to promote and ensure the greater use of Canadian talent.

ENDNOTES

- [1] Steven Clarkson's Canada and the Reagan Challenge (1985) is the most comprehensive source of information on this period. What is particularly important for our purposes is the pattern of Canadian takeovers and takeover attempts which took place around the Canadianization provisions of the National Energy Program. Among these are included the Hudson's Bay acquisition of Anvil Mining Corporation, Husky Oil's acquisition of the Canadian assets of Shell Explorer Ltd. (a subsidiary of Shell, Houston), Canadian Pacific Enterprises' acquisition of the U.S.-owned Canadian International Paper Company, and the Seagrams' bid on Conoco, the 9th-largest U.S. oil company.
- [2] The reclassification of Dome clearly illustrates the difficulty of equating ownership with control; and the problems underlying the reasoning and political priorities of the Committee for an Independent Canada.
- [3] Li Ka-shing's \$484 million investment actually amounts to 43% ownership of Husky. The other major stockholder is Nova Corporation of Alberta, also with 43%. Li's son, Victor, a Canadian citizen, owns 9% of the stocks, with the balance held by the Canadian Imperial Bank of Commerce. The Petroleum Monitoring Agency considers Husky to be under foreign control since Nova can potentially be outvoted (Plaskin, 1988: F9; Critchley and Reguly, 1987:1).
- [4] Supply and Services and DRIE's determination of the "rationalized" status of a particular subsidiary effectively means that a firm may fill procurement demands with goods which have no Canadian value added. The rationalization program does not mean that all lines in a firm's production must possess a WPM, and classification of firms as rationalized (and therefore effectively Canadian controlled) does not discriminate between production lines.

CONCLUSION

In 1984, the Department of Finance released a discussion paper setting out the concerns of the Canadian economy under the newly elected Mulroney government. This document, A New Direction for Canada: An Agenda for Economic Renewal, confirmed the extent to which one of the principal assumptions underlying the creation of the Foreign Investment Review Agency had been rejected. The Department of Finance's key statement on foreign investment argued that "[t]he past few years have witnessed large scale capital investment by Canadians in the United States; we cannot take for granted our attractiveness as a place to invest" (Department of Finance, 1984:35; emphasis added). Where a decade before, the question of Canada's attractiveness to foreign investors was not an issue worth serious discussion, it had now become a central assumption in the minds of state managers. Where a decade before, Canada's economy was understood only in terms of its relationship to foreign multinationals operating within its boundaries, largely on a branch plant subsidiary basis, Canada was now seen as an important home country for foreign investors, with active and dynamic multinationals of its own.

This thesis opened with Joseph Nye's question of "...how states learn. How do national interests become defined, and how do these definitions change?" (1988:238). In answering this question, we distanced ourselves from mainstream interpretations of international relations, focusing on the development of a theory of the state which explicitly linked state action to both the international and the domestic environment of state managers. We have taken as our starting point the international politicization of the issue of foreign direct investment. Following Robert Cox, we argued that the dominance of political hegemons has been assisted because it appeared to take place according to nonpolitical economic laws, that the economic structure and norms created by the system hegemon become part of a "natural" order which is not politically challenged although its benefits may not accrue evenly between the systemic hegemon and all others. The development of these international norms implies that state managers are not as routinely and systematically involved with the regulation of the international economic environment as they might otherwise be; "rules" of international economic exchange allow them to "choose" certain courses of action because these appear to correspond to a "natural" order, and

these choices can be made without serious political debate.

Once the hegemonic international economic order begins to breakdown, however (as it did beginning in the 1960s and early 1970s), the rules which had been assumed to be "natural" are found to be suspect, and the non-political patterns of the relationship between state managers and the international system become contentious and open for redefinition. The "rules", either changed in mid-play (the U.S. abandonment of Bretton Woods, for example), or challenged because they appear to be increasingly unable to confer benefits to a non-hegemonic country or industry (under the principle of national treatment for foreign investment, for example), become a source of political struggle within domestic societies. In this period of change, the state managers can no longer rely upon the assumptions about the international economic environment which they have long held to be true. Their most important political information about the changing international environment becomes the domestic class struggle, and the manner in which it is -- and is not -- reflected in the organization of the state bureaucracy. The failure of established bureaucracies to provide new insight into the manner by which state managers can cope with the

breakdown of the traditionally non-political issues of the international environment encourages the political state managers to seek non-bureaucratic roads to knowledge; task forces and Royal Commissions among them.

In the creation of FIRA, this thesis focused its attention upon the evolution of four key assumptions: balance of payments and Canada's need for foreign investment, the question of extraterritoriality, the extent to which Canada was attractive as a location for foreign investment, and the extent of negative consequences from Canada's branch plant economy. Through this task, we discovered that state managers learn differently. Political leaders, more sensitive to societal pressures, learn not only through interaction with bureaucratic structures, but through discussion with non-bureaucratic representatives. In the case of FIRA, the role of the Central Canadian new middle class was crucial in articulating concerns over the branch plant economy, and its message was "learned" by political actors such as Herb Gray and Alastair Gillespie. Bureaucratic leaders, on the other hand, appear to learn more slowly. Located in organizational structures with historically defined mandates and representing the interests of identifiable social groups, bureaucratic state managers continued to raise

traditional interpretations of the foreign investment question. The Department of Finance expressed concern over the balance of payments consequences of foreign investment regulation, as did, surprisingly, the Department of Industry, Trade and Commerce. ITC clearly reflected a historical evolution which emphasized the importance of trade and commerce concerns over the individual interests of industry.

In the revisions to FIRA and the creation of Investment Canada, political leaders reflected the views of Canadian business, primarily articulated through the Business Council of National Issues, for a more liberalized investment policy. New interpretations of Canada and foreign investment came to the fore: the Canadian economy was competitive and capable of supporting its own multinationals, and the competition for foreign investment had increased to the point where state managers could no longer take for granted Canada's attractiveness as a site for DFI. As we have seen, the principal economic departments also reflected these same views. In this case, these departments appeared to learn more easily for two reasons: the interpretation of foreign investment was more consistent with their traditional position on the issue, and the interests which they represented were the same ones advocating a

change in investment policy.

In developing an answer to the question of how states learn, this thesis builds a bridge between the international economic system and the state managers who make choices. It does not deny the importance of the international system in locating interpretations of that system within domestic classes; in fact, as we have found, we cannot pretend to understand the Canadian experience with FIRA without first understanding the changing pattern of foreign investment and Canada's place within these. The growing incommensurability between the interpretations of foreign investment reflected in FIRA's mandate and the pattern of foreign investment contributed fundamentally to the reevaluation of the Agency. The interpretations of foreign investment articulated by various classes and class fractions are not etherial -- they reflect tangible processes underway in the international system, which are reinforced or challenged by the development of that system.

The international system was crucial in pointing out the anomalies in the assumptions behind FIRA's mandate. Canada did not remain as attractive to prospective new investors as the creators of FIRA had assumed. An extended period of economic downturn capped

with a severe recession cut into the flow of international direct investment capital, not only in Canada, but worldwide. New production strategies, particularly among manufacturing MNCs, tended to pass Canada by as an expensive economy in which to produce. MNCs seeking knowledge attributes and research infrastructure equally did not turn first to Canada, whose low level of R&D activity is notorious. The increased competition between advanced industrial countries, as well as between AICs, newly industrializing and less developed countries for foreign investment (not defined solely, or even most importantly, in terms of capital), meant that Canada could no longer take for granted that it would attract investment no matter the conditions. An Agency whose most significant purpose was to screen manufacturing sector investments (given that service sector investments and resource industry investments were governed under other legislative arrangements which FIRA upheld, but which would likely have been administered on an ad hoc basis in the absence of the Agency) in an era no longer characterized by a branch plant form of subsidiary investment was likely from the start to be marginalized.

The examination of structural factors influencing

state manager learning in this thesis is not intended to deny the importance of the overtly political in shaping the decisions of political state managers. It does contend, however, that political debates may not be as decisive for issues such as foreign investment as are underlying domestic economic and social changes, as well as international changes in the pattern of foreign investment. State managers make decisions within contextual layers, and in the case of foreign investment these layers are both many and complex. State managers exist within an institutional state structure which has a history and an orientation towards the range of "possible" action in any given policy area.

Bureaucratic state managers operate within organizations which have a historical orientation toward the issue of foreign investment, and which represent the interests of particular classes or class fractions. The class struggle which develops around complex issues such as the regulation of foreign investment sets limits to and creates opportunities for the development of politically viable policy options, limits to which political state managers are particularly sensitive. The international economic environment seen in the evolution of foreign investment patterns sets limits on the development of economically viable policy, limits which are interpreted

through these domestic structures, and which may not always be understood or respected. State managers make policy decisions within these contextual layers, layers which are themselves changing. State managers may and do act on the basis of perceptions which are no longer reflective of the context in which they operate, as the FIRA decision aptly reflects.

This dissertation develops a link between the international economic environment and the state manager. All too often, the international economic system is treated as a "given", a set of economic realities which are knowable and accepted. This thesis argues that we cannot assume that state managers have knowledge about changing international investment patterns to such an extent that they can view the international economic system as a "given" and thereby make rational, self-interested, value-maximizing decisions about it. The international system is a powerful constraint to policy making, but it is a constraint which is first interpreted through a domestic class struggle. This struggle takes an empirically definable international economy and interprets it so as to inherently permit, and condition, state manager choices. This struggle is fundamentally political, and it is in the manner in which different interpretations

of foreign investment are reconciled by state managers that the most fundamentally political choices take place. In the end, it must be possible for international relations to identify international structures and yet to still accept that state managers make political choices.

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In 1929, Canadian Airways, predecessor to Trans-Canada Air Lines and Air Canada, was formed, with capital contributions from both the Canadian Pacific Railway (the CPR) and the government-owned Canadian National Railways. Canadian Airways' president stated that this financial participation was to constitute a warning to American airline interests that Canadian Airways "was financially in an impregnable position" (Franck, 1976:58), and thereby not open for takeover. The consequence of this 1929 decision to retain air transport in the hands of Canadians has been to effectively ensure that not only air, but also rail and water transport, are, or have become virtually 100 percent Canadian owned.

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The Canadian and British Insurance Companies Act was amended in 1957, in response to concern about foreign takeovers in the insurance industry, to require that a majority of the directors of Canadian insurance companies be resident Canadian citizens. The amendment further granted the power to the boards of Canadian insurance companies to refuse to allow the transfer of shares sold by a Canadian citizen to a non-resident, based on the assumption that the directors themselves would resist further foreign takeovers (an assumption which was recognized as unfounded with more stringent restrictions enacted in 1965). In 1958, the Canadian Broadcasting Act set a limit of 25 percent on foreign ownership of television broadcasting undertakings, excluding cable television.

1957 also marked the year in which the key sector approach to foreign investment restrictions began in earnest. In an issue which was to recur, the Liberal government of St. Laurent attempted to impose a magazine tax on advertising revenues of Canadian editions of foreign magazines (such as Time and Reader's Digest), efforts which were undone by the Conservative victory of that year.

Through the early and mid 1960s, further restrictions were enacted to prevent takeovers or ensure Canadian participation in specific sectors. In 1960, Canadian Participation Provisions (CPP) were implemented, granting oil, gas, and mining leases only to Canadian citizens or to Canadian corporations (at least 50% owned by Canadian citizens, or trading on a recognized Canadian stock exchange). In 1962, the Corporations and Labour Unions Return Act (CALURA) empowered the government to collect financial and other information on the affairs of corporations and labour unions carrying on activities in Canada.

In 1964, the Insurance and Loan and Trust Companies Act amendment limited the proportion of shares owned by nonresidents to no more than 25% of any one of these concerns. The Radio Act placed radio on the same basis as television, regulated in the 1958 broadcasting act, setting a limit of 25 percent on foreign ownership of radio broadcast undertakings. In 1965, important changes in the Income Tax Act and Customs Act affected the establishment of new foreign-controlled newspapers and periodicals and the foreign takeover of existing newspapers and periodicals under Canadian control. No longer could a tax deduction be made for the cost of

advertising directed primarily at the Canadian market in an issue of a non-Canadian newspaper or periodical, although exemptions were made for Time and Reader's Digest. Changes in the Customs Act prohibited entry of non-Canadian periodicals containing advertisements directed at the Canadian market.

1966 saw the release of the Winters "Guiding Principles of Good Corporate Behaviour for Subsidiaries in Canada of Foreign Companies". Sent to all foreign-owned companies operating in Canada by Robert Winters, Minister of Trade and Commerce, the guidelines set out general principles of business behaviour in Canada. These principles included such suggestions as developing "maximum ... market opportunities in other countries as well as in Canada", extending the processing of resources in Canada, developing economic sources of supply in Canada to serve procurement requirements, engaging in a greater degree of research and development, and technological activity in Canada, including Canadian citizens as a majority on boards of directors, publishing financial information, and encouraging through fiscal support the development of intellectual, social and cultural activity in Canada (cited in Fayerweather, 1974:175-6).

In 1967, the Bank Act stipulated that at least three-fourths of the directors of banks in Canada must be Canadian citizens. Further, the proportion of shares in such banking interests held by nonresidents was not to exceed 25%, with no one person to hold more than 10% of the shares. Growth limits were placed on banks which, in 1967, had more than 25% foreign ownership; a provision aimed at Mercantile Bank, which was then wholly owned by the First National Citibank of New York. It was 1971 before the Canadian government was able to negotiate the sale of Mercantile shares to Canadian to the 75% level of Canadian ownership required by the Bank Act. The action of the Canadian state through the 1966-67 Mercantile Bank affair made clear the intention of the government to retain specified sectors of Canadian economic activity under majority Canadian ownership, despite the pressure of foreign, predominantly American, investors. The provisions of the Bank Act, while restrictive, continued Canadian state policy which, since 1913, had "required that a majority of bank directors be subjects of Her Majesty resident in Canada" (Franck, 1976:58).

As well, in 1968, the Broadcasting Act was amended

to include a clause stipulating that the Canadian broadcasting system must be owned and controlled by Canadians, in order to "safeguard, enrich and strengthen the cultural, political, social and economic fabric of Canada". Licences and renewals would only be granted to Canadian citizens and eligible Canadian corporations (Fayerweather, 1974:172).

By 1970, part of the Winters Guidelines had come into force, with the Canada Corporations Act requiring that foreign companies publish annual reports. Further, the Loan Companies Act extended the protection of the Bank Act to other financial establishments, requiring that 75 percent of directors be Canadian citizens, that nonresidents be restricted to ownership of no more than 25 percent of shares, and prohibiting voting by nonresidents by nominees or proxy. In 1971, the Investment Companies Act restricted to 25 percent foreign ownership of federally incorporated sales finance firms.

In 1972, the Foreign Takeovers Review bill was proposed, although not enacted. It required that all acquisitions by foreign investors of Canadian firms with assets of more than \$250,000 or gross revenues of more than \$3 million be subject to review by cabinet.

On January 24, 1973, the Foreign Investment Review Bill was tabled in the Canadian House of Commons, proposing the creation of the Foreign Investment Review Agency. The Bill was passed by the House on December 12 of the same year.

Appendix II: Canada's Economic Performance Indicators;
1972-1985

Table II.1 Canadian Unemployment Rates
total figures, both sexes, 15 years and over
yearly average percentages; 1972-1975

1972	6.2
1973	5.5
1974	5.3
1975	6.9
1976	7.1
1977	8.1
1978	8.3
1979	7.4
1980	7.5
1981	7.5
1982	11.0
1983	11.9
1984	11.3
1985	10.5

Source: Statistics Canada (Government of Canada)
(1988). Historical Labour Force Statistics: 1987.
Ottawa: Supply and Services Canada, p. 200.

Table II.2 Canadian Inflation Rates
yearly averages, percentage increases
1972-1975

1972	4.7
1973	7.7
1974	10.9
1975	10.8
1976	7.5
1977	7.9
1978	8.8
1979	9.2
1980	10.2
1981	10.5
1982	10.8
1983	5.8
1984	4.4
1985	4.0

Source: Statistics Canada (Government of Canada)
(1988). The Consumer Price Index, 1987. Ottawa: Supply
and Services Canada, p. 11.

Table II.3 Canadian Real GNP Growth
Annual percentage rates of change
1972-1975

1972	5.5
1973	7.1
1974	3.2
1975	0.6
1976	5.5
1977	2.4
1978	3.4
1979	3.0
1980	0.5
1981	3.4
1982	-4.4
1983	3.3
1984	5.5
1985	4.0

Source: Statistics Canada (Government of Canada) (1987). National Income and Expenditure Accounts, Fourth Quarter 1986. Ottawa: Supply and Services Canada, p. xii; CALURA (various years). Annual Reports.

Table II.4 Canadian Balance of International Payments
with all countries
Millions of C \$; 1972-1975

	Current Account	Capital Account
1972	-283	+1,847
1973	+312	+538
1974	-1,299	+2,331
1975	-4,631	+5,957
1976	-4,096	+7,876
1977	-4,322	+6,594
1978	-4,903	+6,043
1979	-4,864	+7,472
1980	-1,130	+2,438
1981	-6,131	+14,740
1982	+2,906	-1,055
1983	+2,942	+3,132
1984	+3,362	+3,843
1985	-584	+6,083

Source: Statistics Canada (Government of Canada)
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