Economic Integration In The NAFTA Zone: Public Policy, Corporate Strategy And “Plumbing”

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Abstract

The aim of this paper is to provide a partial and rough assessment of the state of economic integration in North America on three levels; that of large-scale national policy-making; that of corporate policy and decision; and finally, at a level that might be called technical, or the “plumbing” of the economic system.

The paper opens with a review of the concept of globalization and the problems that occur when we try to measure its existence, especially outside of trade and finance figures. Given that NAFTA is a regional agreement within this hazy global system, the concept of regionalization is presented and Canada’s position in regional organizations/agreements is noted. National policy and its effects on and impact from regional integration is discussed along four dimensions: military security, culture, political regime and economic.

At the corporate level, company responses to FTA/NAFTA are discussed along three dimensions: extinction, rationalization and opportunity. On the surface, the experience of Canadian companies is mixed in terms of integration, with a clear trend existing only in the experiences of corporate subsidiaries.

At the “plumbing” level, eight selected topics are considered from a list that is almost endless: transportation; electrical energy; communications; finance; labour; corporate taxation; health and NAFTA holdbacks. A variety of facts and observations lead to a tentative conclusion that integration is spotty and may be due as much to the forces of technological change as anything else.

This paper has illustrated the variety and complexity of behaviours, products, attitudes, policies and services that would have to be harmonized before one could meaningfully talk about integration. The creation of the NAFTA zone and its extension in practice into a number of areas beyond the original intent of trade has given a push to its members toward greater integration. Studies of globalization and technological development seem to suggest greater integration is taking place in all parts of the world. But, until we have considered the huge variety of potentially integrative aspects of micro-and even submicro-economic and business behaviour, the conclusion that North America is becoming more economically integrated is still only guesswork.

Introduction

The aim of this paper is to provide a partial and rough assessment of the state of economic integration in North America on three levels; that of large-scale national policy-making; that of corporate policy and decision; and finally, at a level that might be called technical, or the "plumbing" of the economic system.

A few caveats are in order. First, there is an assumption in this discussion that what is called "economic" can largely only be seen through the actions of governments and firms. Second, John Helliwell found that data on trade between provinces and states in North America was spotty at best and often non-existent. [1] Assuming that trade data should be of a better quality than other indicators of integration, it follows that any estimates for these others are likely to be of even less quantity and quality. What follows is an attempt to provide a partial survey of what seems to be happening at three levels of analysis with respect to the integration of the North American economies. The reader can expect the overall presentation to be inconclusive, but is reminded of the general systems theory paradox that the effect created by the whole may be quite different than the effects of each of the parts. Finally, economic integration cannot be seen outside the wider context of regional integration along a number of dimensions. These will be noted, explicitly or implicitly, in the body of the paper.

Public Policy

The process of globalization appears to have accelerated since the end of the Cold War. Once economic processes in Europe recovered from World War II and new industrialization had taken place in East Asia as a result of US military requirements in Korea and Vietnam in the 1960s and 1970s, it became common to speak of a Free World "trade" between regions that comprised most of the world's production and trade. [2]Since 1990, other countries have become participants in this growth of production and trade to the point where it was "globalized". Globalization, in broad terms may be taken to mean the:

1. Emergence of a global financial market
2. Transnationalization and increasing redundancy of technology
3. Global organization of production
4. Rise of transnational economic diplomacy
5. Rise of cultural flows and an associated universal identity, and
6. Emergence of a global geographic space as relatively more important than either regions or nation-states[3]

The use of globalization has engendered a certain amount of reaction. Titles of books with phrases such as "clash of civilizations" and "jihad vs. McWorld" dramatically illustrate this reaction. It consists of people in parts of countries, whole countries themselves and even regions of the world searching, sometimes violently, for an alternative identity to that of "global consumer". Some of the national reactions have ironically led to a "pooling of sovereignty" in regional groupings that may sacrifice some local characteristics in favour of a larger common identity.[4] There is some debate over whether this phenomenon is not just a temporary side-effect of globalization.

There is a question about the centrality of economic relationships to the existence of a society. At one extreme are arguments that these relationships are central and that other aspects of life are "superstructure", dependent on the economic and of less importance. At the other end of the spectrum are arguments that, given adequate incomes and resources, people focus on a variety of expressions, interpersonal relationships and lifestyles. The economy is instrumental rather than central.[5]

Acceptance of one side or the other of the centrality/instrumentality debate is important for policy-making because of its implication for the Canadian identity. The centrality argument leads to the conclusion that increasing economic integration may lead to integration in all sorts of cultural and lifestyle dimensions, since these are to a great extent dependent on the economic relationships. Acceptance of the instrumentality argument leads to a less deterministic outlook: economic integration could provide Canadians with a more prosperous society, which in turn enhances their ability to have choices and to make their own decisions about them.

These positions are very real today. The "Jihad vs. McWorld" characterization of tribalism and a global economy flourishing alongside and in part because of each other is perhaps the most starkly dramatic version of this argument today. In this vision, the question of centrality/instrumentality is not resolved. A greater harmonization of products and services provided though a globalized economy not only creates greater similarity in lifestyles across the world; it also seems to encourage greater attempts to diversify and to reconstruct and resurrect local, regional and national cultures. This is not just occurring in developing countries, but, as Robert Kaplan notes, in places like the United States and Canada. [6]

It may well be that there is no good answer, except at the level that one chooses to analyze the evidence. In modern physics, the distinction between matter and energy tends to disappear as one moves to a more micro level of analysis until one is confronted by a universe of wave/particles that behave in ways rather different than those noted at more macro levels. John Helliwell's study of border effects illustrates this tendency to some degree. He can point to relative border effects in trade between national economies. Similar effects are more complex at the subnational level and even more so at the level of individual industries. As he pushes on, into areas of social capital, trust and community, his means of distinguishing border effects becomes more abstract and in some ways different from those at a more macro level. [7]

Globalization becomes a less powerful term as one moves away from the large scale forces in the world and into a micro universe of borders and pastiches of relationships between parts of societies and between similar parts in different societies. To rephrase a point noted above, this is the classic paradox in general systems theory: there is no obvious connection between the effects produced by a whole system and those produced by each constituent part.

Regionalization

The process of regionalization implies a shift from a heterogeneous to a more homogenous identity among peoples who already share some common characteristics. The different dimensions along which this shift may occur are:

1. Military security
2. Culture
3. Political regime
4. Economic policy[8]

Within the global context, there appear to be five types of regional interaction:

1. Intergovernmental regional cooperation, where activities are undertaken for mutual benefit by sovereign states
2. State-promoted regional integration, where states coordinate or merge their economic policies into a single regional economy and / or political system.
3. Market and society induced regionalization without any necessary state action. Businesses, NGOs and others work to promote regional activities.
4. Regional initiative and coherence, where the region is the political and economic actor on the world stage.
5. Regional identity, where people in the geographic area share an identity, culture and values.[9]

These are not stages and countries may be participants in a number of these types. Canada is involved in #1 and #3, with some movement through NAFTA in #2. Involvement in cleaning up the Great Lakes is an example of #1, as are the annual conferences of the New England Governors and Eastern Canadian Premiers. The binational identity of NGOs like the Conference Board and Chambers of Commerce and the Sierra Club are examples of #3.

Additionally, a typology of various regional trade groupings demonstrates this mix of national involvements in regional groupings:

Table 2: Countries in Regional Groupings

AEC	African Economic Community. All Africa.
Andean Group	Andean Common Market. Bolivia, Colombia, Ecuador, Peru, Venezuela.
ANZCERTA	Australia–New Zealand Closer Economic Relations Trade Agreement. Australia, New Zealand.
APEC	Asia Pacific Economic Cooperation. ASEAN members, NAFTA members, Anzcerta members. Chile. China, Hong Kong, Taiwan, Japan, South Korea.
ASEAN	AFTA: ASEAN Free Trade Arrangement. Brunei, Indonesia, Malaysia, Philippines, Singapore. Thailand, Vietnam from 1995 (not included in data), Myanmar and Laos from 1997 (not included in data).
CACM	Central American Common Market. Costa Rica, El Salvador, Guatemala, Honduras, Nicaragua.
CARICOM	Caribbean Community. Antigua and Barbuda, Bahamas, Barbados, Belize, San Cristobal, Dominica, Grenada, Guyana, Jamaica, Montserrat, St. Kitts and Nevis, St. Lucia, St. Vincent and the Grenadines, Trinidad and Tobago.
EU	European Union. Belgium, Denmark, France, Germany, Greece, Ireland, Italy, Luxembourg, Netherlands, Portugal, Spain. United Kingdom (EU 12); Austria, Finland, Sweden from 1995 (EU 15).
FTAA	Free Trade Area of the Americas. All Western Hemisphere.
MERCOSUR	Southern Cone Common Market. Argentina, Brazil, Paraguay, Uruguay (MERCOSUR 4): Bolivia, Chile from 1997 (Mercosur 6).
NAFTA	North Atlantic Free Trade Area. Canada, Mexico, United States.
SAARC	South Asian Association for Regional Cooperation. Bangladesh, Bhutan, India, Maldives, Nepal, Pakistan, Sri Lanka.
SACU	Southern African Customs Union. Botswana, Lesotho, Namibia, South Africa, Swaziland.
SADC	Southern African Development Community. Angola, Botswana, Lesotho, Malawi, Mauritius, Mozambique, Namibia, South Africa, Swaziland, Tanzania, Zambia. Zimbabwe; Congo and Seychelles from 1997 (not included in data).

Source: Sheila Page, "Survey of Regions", *Politeia*, 17(3) 1998 ,p.24

Tables 1 and 2 identify 14 regional trade groupings and their members that exhibit a wide variety of characteristics. Canada is a member of three of them, NAFTA, APEC and FTAA. These last two have relatively little substance at present, while NAFTA requires serious treaty obligations. Hence, this discussion of regionalism and its implications for Canada will focus on the North American region.

Canadian Policy and Regional Integration

Regional integration can occur along the four dimensions mentioned above: military security, culture, political regime and the economy. Canadian involvement in North American integration has been mixed on these dimensions. Integration has proceeded most strongly along the lines of **military security** since World War II, when Canadian attachment to Britain's military presence in the world was replaced by an attachment to the US. The creation of the Dew Line air defence system in the Canadian North, participation in the Korean conflict and the development of NORAD represented a rational response to the pressures of the Cold War. Since then, Canadian forces have been integrated into the NATO regional alliance as well. Canada has exercised a degree of independence by staying out of the Vietnam War and in promoting its forces as peacekeepers. On the economic side of the military, much of the equipment for the Canadian Forces has come from purchases from the US or US designs built in Canada. There have been regular purchases of equipment and designs from Europe as well, which illustrates the Canadian unwillingness to integrate military forces and policy completely with the US.

Cultural integration, including attitudes toward various social questions, is much harder to gauge. A recent report by the Cultural Industries SAGIT claimed that foreign (mostly US) firms accounted for 45-95% of all sales of books, English-language magazines, music tapes, CDs, films and film distribution revenues. [10] Major sports leagues are, with the exception of football, integrated across the border. In football, it would appear that the US NFL treats the Canadian CFL as the "minor league" it never has had in the US. One SAGIT presenter said "…if we don't do things now… we will become a regional market for the United States–as we are to a certain extent–far more than we are today". [11]

Political regime integration, like military integration, is mixed. At the Century's end, all the parties to NAFTA have federal structures. Federations always have some division of power between the central governments and the constituent units. Canada's system tends to be more decentralized than that of the US because of historical accidents: most importantly, the US Civil War and the miscalculation of the future by Canadian founders who gave the 20th Century's critical domestic powers to the Provinces in 1867. Mexico's system is highly centralized but is tending towards more decentralization in terms of the ability of the States to make policy. Canada's decentralized system has been in rough balance for decades and the American system is moving towards more decentralization as legacy of the Reagan agenda and as the country reverts to a weaker Presidency now that the Cold War is over.

Constitutionally, the most important move towards integration was the adoption of a Charter of Rights in 1982 that resembles the Bill of Rights in the US. The most significant de-integration move has been the strong policy against firearms in Canada in the face of the opposite trend in the US, which is a result of a provision in their Bill of Rights.

The federations have similar competition laws, differing taxation regimes, though these are gradually being harmonized, and roughly similar social legislation, though Mexico is hampered by a lack of resources in fulfilling its legislative hopes in this regard. At the municipal level, Canada and the US share similar types of administrative organizations, with the significant exception that Canadian municipalities do not possess the kind of constitutional autonomy that US municipalities enjoy. In practice, this has relatively little effect, however.

The simplest explanation for Canadians who see **economic** integration as a function of the FTA signed a decade ago is that it represented a reaffirmation of the special status that Canada had enjoyed with the US economic policy-makers since the 1950s. This special status, which had largely exempted Canadian producers from American protectionist and retaliatory actions for over 30 years, was coming unravelled. The economic shocks affecting the US in the 1970s and early 1980s, coupled with nationalist economic policies pursued by the Trudeau governments of the same period appeared to have put Canada into the same category as all other countries. Given its high degree of dependence on the US economy, the status quo ante had to be restored. The formulation inherent in a treaty gave the Reagan administration its first step towards its free trade in the Americas goal, while providing Canada with a more secure replacement for the special status policy statements Washington had made 30 years before in a different economic and political context.

Economic integration seems also to have a certain historical force as well. The economic organization of the Western alliance in the Cold War was centred on the opening of economies that had been closed to a great degree by 30 years of wars and depression. In a sense, 1990 saw a general restoration of the kind of global system that had existed in 1890. The seven-fold growth of the world economy since 1945 only served to encourage policy-makers to continue along this path.

A related point concerns the accession of Mexico to the FTA in NAFTA. This was both a part of the Reagan hemispheric agenda and an extension of the historical process mentioned above, but beyond these, it also constitutes a great experiment in economic development, more ambitious than the accession of Portugal or Greece to the EU. Critics of foreign aid policies have emphasized for decades that open trading relations ought to be a more effective means of development that government-to-government transfers of resources. In global terms, NAFTA is the first strong the test of this claim.

Finally, the process may be pushed by the nature of production, transportation and communication technologies that, in the 20th century at least, have led to scale economies in production that outstrip the individual absorptive capacities of all but the largest world economies. Globalization of financial movements, international product development and efficient distribution have led to pressures by business for more stable and coordinated economic policies among nations. To a great extent the heavy dependence of Canada on the US as both a supplier and a market has meant that North American integration has substituted for globalization. This is less the case in Europe and Asia, where the US is a very important factor, but not to the extent it is for Canada.

Corporate Policy

It is a truism that governments tend to follow where people lead. Democratic governments are especially prone to assessing the mood of the public before taking a serious policy stand. In the case of the negotiation and adoption of the FTA, public opinion was tested first by the work of the Macdonald Commission, created under the 1981-84 Trudeau government.[12] Royal Commission recommendations do not often come out of thin air and the Macdonald Commission's clear call for free trade with the United States was no exception. The Commission recognized that intrafirm trade between Canada and the United States was a significant part of the total trade between both countries. Pierre-Paul Proulx in the early 1980s put the proportion at about 50%.[13] The failure of the National Energy Program and its political backlash in Western Canada served as a backdrop for the call for Free Trade. It was hard to justify a policy of free trade for the Ontario auto industry, while subjecting Western oil production to a nationalist regime. By the time the Macdonald Commission reported, the Autopact was 20 years old and it had provided Canada with economic activity in this sector that appeared to be superior to what a more protectionist policy might bring. Public opinion seemed to be allied with corporate pressure in the mid-1980s in a willingness to try a new direction for the country's economy.

The FTA brought with it three types of pressure for continental integration:

1. Small companies that had grown up under the National Policy and its later protectionist derivatives were threatened with extinction if they could not quickly acquire the scale economies of American competitors.
2. Larger multinationals could rationalize production on a transnational basis, either by closing inefficient plants on either side of the border or refocussing Canadian production where product diversity for the Canadian market had meant a number of short (and inefficient) product runs.
3. Product and service areas that potential Canadian producer/entrepreneurs had heretofore not had the markets to exploit were now opened to them. This would include repositioning of existing forms of production as well.[14]

Extinction

The reaction of those who opposed the FTA tended to centre on the problem of the extinction of Canadian companies, and not without some cause. 120 years of using tariff barriers and other devices to encourage a wide range of domestic production for an economy 10% the size of that in the US meant that the FTA could bring an avalanche of bankruptcies, mergers and acquisitions across Canada. In the end, the experience did not prove to be so catastrophic, in part because of the adaptability of Canadian firms, their tendency to form alliances with American partners, the coincident trends in corporate North America favouring spin-offs, outsourcing and, finally, the dissolution of many conglomerates and utility monopolies. The end result seems to have been neutral with some firms going under and others expanding to next new demand.

Retail sales is one area where the record appears mixed. The past decade has seen the disappearance in Canada of two US chains, K-Mart and Woolco, and the growth of the largest such chain, Wal-Mart. On the Canadian side, Hudson's Bay Company has managed to hold its own, especially through its Zellers subsidiary, while the Bay has been troubled. Eatons has been pushed to the edge as it has not responded well to the new environment. Canadian attempts to enter the US market have generally been failures, from Canadian Tire to the Future Shop. Imasco withdrew from the US fast food business while Wendy's (US) and Tim Hortons (Canada) merged.

The mixed experience of American retailers in Canada has meant that the wholesale distribution of goods has not consolidated itself as an extension of the US system. Canadian wholesale and distribution systems have traditionally been centralized in Toronto and much of these systems appear to have survived in the face of predictions of extinction.

The brewing industry has adapted in the face of US pressure over the decade by rationalizing production to gain scale economies in the face of opposition from provincial governments. The industry has also licensed US brands and participated in a variety of mergers and acquisitions. Unlike the US market, national and even regional brands have kept their identity even while the ownership and structure of the industry has changed.

Rationalization

US transnational corporation (TNC) branch plants in Canada were generally active in getting both the Canadian and US governments to agree to the FTA. Again, the Canadian opponents to the agreement saw the wholesale closure of branch plants, but again, the process, after a decade, has produced mixed results. Some plants have been lost but others have been enlarged and still others represent new corporate expansions.

There appear to be at least six elements in the corporate strategies of American, Canadian and Mexican TNCs in the decade after FTA and NAFTA. These are:

1. Integration of the other countries' markets in NAFTA into a continental corporate strategy;
2. Rationalization of work processes and production scale;
3. Cross-border mergers and acquisitions;
4. Product standardization;
5. Development of new organizational relationships;
6. Increased intrafirm trade.

In their study of corporate strategies and attitudes in NAFTA, Blank and Haar point to survey results from US subsidiaries in Mexico and Canada for an indication of the development of a continental strategy.

Table 3

Respondents in subsidiary companies to : "As your firm looks towards the next several years, what are the major goals it hopes to accomplish in Mexico/Canada?"

	Mexican respondents # of mentions n=37	Canadian respondents # of mentions n=32
	Mexico	Canada
Increase profitability	21	22
Heighten local identity of business	5	6
Increase market share	24	22
Increase volume of local operations	25	20
Increase lines of business	2	1
Integrate operations into a North American framework	15	19
Integrate operations into a global framework	11	7
Reduce overheads in local operations	10	12
Close local operations	0	0

Source: Stephen Blank and Jerry Haar, *Making NAFTA Work: US Firms and the New North American Environment*, (Miami: North-South Center Press, 1998) pp. 33-34.

The parallels in the responses are striking given that company respondents were surveyed as different times between 1994 and 1996 and were not necessarily from the same companies. The most common responses tended to be optimistic about local activities and recognized that these operations would be more closely integrated into a continental framework.

The rationalization of work processes, not unexpectedly, focussed in Canada on the scale of production, new production opportunities and marketing changes. Canadian and Mexican subsidiaries of US corporations were hit with reductions in the scale of their production, though no one is sure whether the recession of 1991-3 or NAFTA was the cause. At the same time, a number of companies began to institute world product mandates and go so far as to develop an intrafirm bidding process for these mandates. Winners could see an increase in production scale.[15]

Clearly, as rationalization of production and product mandates were instituted, the products themselves had to become more standardized. Technology, however, added a twist to the traditional goal of making every product the same. Computerization and automation allowed factories to produce a more flexible range of goods without losing much in the way of scale economics. One sees in these two trends a mixture of standardization and flexibility that was unknown two decades ago.

Canadian managers of subsidiaries noted that their autonomy in product research and development had been eroded since the FTA. Variations in product specifications that might once have reflected local tastes were being subordinated to the continental scale of operations.[16]

New organizational forms have accompanied this closer integration of transnational operations. While some of the high-tech companies adopted a more decentralized format as part of company policy, many of the other TNCs close to centralize "hard" activities like investment allocation and product planning and to leave local public affairs relationships, labour relations, training and other "soft" functions in the hands of local subsidiaries.[17]

As well, companies have been experimenting with different activities and intrafirm relationships across borders. The product mandate bidding process mentioned above creates a competitive atmosphere between subsidiaries. Labour experiments related to flexible manufacturing systems have been assigned to subsidiaries in Mexico or Canada in areas where labour relations are more permissive. Shifts between divisions based on location to ones based on product groups have changed reporting relationships inside firms.[18]

Finally, TNCs see more intrafirm trade arising out of these changes. The tendency to locate various types of production depending on labour force quality, transportation modes and business costs means that the process of the disintegration of production will continue. Seventy-five years ago, Henry Ford could boast of his integrated automobile plant in River Rouge near Detroit that iron ore went in one end and cars drive out the other. This is not the model that today's transnational corporation uses for any part of its activities. Back offices can be far from headquarters, perhaps product development can be at a distance, and clearly parts and assemblies, even in the software industry, can be geographically distributed. NAFTA's role in this evolution has been more to provide a stable environment for these processes than to have engendered them.

While the information in this section has focussed on subsidiaries to US companies, it should be noted that the same processes have been taking place in Canadian and Mexican TNCs. [19] Whether in the communications or transportation equipment sectors, in railroads or bakeries or property development, technology and transportation revolutions are driving new TNC configurations.

Opportunity

One of the problems with the Canadian economy, pre-NAFTA, was its fairly narrow scope, largely limited to automobiles, parts, raw materials and a range of manufactures and services for the domestic economy. Because of the structure of US tariffs, many areas of enterprise were difficult for potential Canadian producers to enter. With the exception of the Autopact, US tariffs tended to be much higher, the more "value added" was included in the product. Services were difficult to export because of immigration and visa hassles. With NAFTA, the expectation arose that these impediments to diversifying the Canadian production picture would decease and Canadians would take advantage of this opportunity.

To a degree this has happened, though the big numbers in terms of exports still favour autos and raw materials in both Canada and Mexico. Outsourcing and the tendency toward geographic dispersal of corporate functions have provided some spectacular opportunities for companies like Magna Industries and for a number of call centre operators. Some of the Canadian sites might not have been used without the stability that NAFTA offers. As well, some existing firms in areas such as architectural services, Internet security and animation have developed continental markets. Yet, this process of diversification seems to be slower than what NAFTA optimists had expected. It will take more than one decade to see how this opening of the US market in product and service areas heretofore closed to Canadians will prove to be of great advantage.

Plumbing

It is only when we descend into the workings of the North American economy, into the realm of the "plumbing" of the structure that the scope and possibilities of integration begin to appear. Yet, as Heisenberg's uncertainty principle proclaims in quantum physics, the more we know about the particles the less we know about their momenta and vectors —the same holds true for the basics of economic integration in the North American region. As some wit once put it, "The Devil's in the details": good words about government policy and corporate strategy mean little if the pipes do not connect and the numbers do not add up.

The complexity of the continental economy is daunting and this paper has room for only a few details, covered in a fairly superficial manner. Nine topics will be considered:

1. Transportation
2. Electrical energy
3. Communications
4. Finance
5. Labour
6. Corporate Taxation

7. Health
8. NAFTA Holdbacks

Transportation

There are four tradable modes of transportation: air, road, rail and water. There are three important facets of these modes to consider: ownership, cabotage and infrastructure. These can be arranged in a 12 - cell diagram:

Table 4 : Modes and Problems

	Ownership	Cabotage	Infrastructure
Air	C,I	N,C	C,I
Road	I	I	I
Rail	I	I	I
Water	C	N	C,I

C = coordination
I = integration
N = none

With some exceptions, the North American transportation system is largely integrated. The most significant exceptions occur in cabotage applied to air and water transport. Cabotage means the right of a carrier to pick up and transport people or goods between two points in a foreign country. Airlines are prevented from exercising cabotage, which means, for example that Air Canada cannot load and unload passengers travelling between San Francisco and New York without first taking them outside the US. Similarly, American Airlines cannot transport people between Calgary and Toronto without first landing in the United States. Airline alliances, such as American / Canadian as well as Air Canada / United, coordinate their flights through the practice of "interlining" so that a passenger from Dallas to Halifax can "fly American" the whole distance, even though Canadian operates the flight between Toronto and Halifax, giving the route in this sector both a Canadian and an American flight designation.

The Jones Act in the US acts to restrict cabotage in shipping between US ports in order to protect American shipping lines. This restriction distorts cruise ship routes and activity on the Pacific coast.

There are integration shortfalls in the air mode in terms of ownership restrictions on both sides of the border. These have been especially contentious in the Canadian Airlines / American Airlines relationship. It must be recognized that ownership issues are also intimately bound up in cabotage issues as well. Other integration issues relate to air infrastructure, in particular to air navigation control. As satellite positioning systems become more sophisticated, there is less need for large national air navigation offices or companies. At some point, the navigation technology and national air sovereignty will collide.

Road and rail systems have become more integrated with the recent decision by US regulators to allow some cabotage by Canadian truckers and the approval of the CN / Illinois Central merger, which creates the only railroad that connects both oceans and the Gulf of Mexico.[20] However, the CN is now majority owned by Americans. Water infrastructure integration may be moving forward with the proposed extension of the US intracoastal waterway south from the Rio Grande into Mexico.

Electrical Energy

The Canadian and American electrical grids have been integrated for most of the 20th century and sales of power have been an important feature supporting and sustaining the Canadian energy industry. The desire for greater integration has interacted with greater decentralization in the US system and this development promises in turn to produce potentially massive changes in what has been largely a public monopoly in Canada. Essentially, computerization has given intermediaries the ability to market "virtual" power to customers not physically connected to the power generation companies.

This is leading to an unbundling of US (and by necessity, Canadian) power companies into separate generation, distribution and marketing companies. As the big Canadian provincial monopoly companies are broken up, there is less reason for them to remain in public hands, or even in Canadian hands.

Communications

The maturing integration of wire-based telecommunications, cellular and satellite technology, the Internet and the entertainment media has served to fracture the North American communications industries in such a way that hundreds of mergers and take-overs are occurring in a variety of directions. No one knows what will eventually be the "winning" combination, but the speed of technological integration is outstripping the regulatory agencies' ability to deal with the situation. Canadian participation in the process has begun in earnest, most notably in the acquisition of 25% of BCE by Ameritech and the merger of the four Atlantic region telephone companies. Delivery of entertainment and music over the Internet effectively subverts CRTC rules on Canadian content in entertainment, and, while the technology for providing such services is neither mature nor widespread as yet, clearly it will become untenable to have Canadian content rules for traditional TV, but not for Internet "television". Yet, the amorphous nature of the Internet makes it difficult , if not impossible, to control only certain aspects of this medium.

Finance

The field of finance is far too complex to cover in a short section here, but there are a few points worth making. First, the integration of banking systems between Canada and the US is impeded by Canadian ownership rules and by the US Glass-Steagall Act. In different ways these act to narrow the reach of banks in the US and to prevent take-overs in Canada. The rise of computerization coupled with Internet e-banking means that increasing consolidation of firms is economically feasible, if not politically desirable. Increasingly, financial service institutions will be able to dispense with branches, agents, and other intermediaries to do business directly with customers. The success of automobile dealers in 48 US states is forcing auto sales to go through them rather than through the manufacturers is a ploy that is unlikely to be repeated in the financial service firms. [21] The rise of the e-stock day trader indicates how rapidly consumers are finding means to bypass traditional financial systems.

In some ways, financial integration is impeded by the existence of separate national currencies, especially in Canada and Mexico. Currency movements add to the transaction costs for Canadian and Mexican borrowers were they to work with continental financial institutions whose loans are denominated in US dollars. There are ways to avoid this risk by both lenders and borrowers, but it would seem that independent or at least autonomous currencies constitute a dis-integrative force in the financial markets.

Labour

One of the most noted features of our time is the worldwide imbalance between the demand and supply of skilled and unskilled labour. Inside the NAFTA zone, this imbalance has led to two different mobility regimes: for most types of skilled labour there is a relatively free, if not integrated, market. The prosperity of the middle and late 1990s has led to the migration of Canadian and Mexican skilled labour into the US. NAFTA allows some 21 categories of skilled labour to move freely between the participant countries. Other skill types have differing impediments, some ironically based on the resistance of their members to being included in the agreement in the first place.[22]

The plight of unskilled workers is much worse, as can be seen in dramatic fashion along the US / Mexico border. The levees and fences that mark the north shore of the Rio Grande at El Paso, Texas and the brown metal wall that divides the two Nogales (Arizona and Sonora) are testament to the American attempt to keep out unskilled Mexican labourers. Along the border in 1997, some 1.5 million people were apprehended and returned to Mexico, even as the unemployment rates in the border states effectively approached zero.[23]

This phenomenon is no different in other parts of the world. North Africans try to cross the Mediterranean to find work in the EU; Indonesians cross the Straits of Malacca to find work in Malaysia and Singapore; Taiwan actively discourages mainland Chinese "defections" across the Formosa Strait. Within regional organizations, only the EU has adopted a regime that promises labour mobility; the others have limited (NAFTA) or no mobility.

Corporate Taxation and Subsidies

There appears to be little integration in the area of corporate taxation and subsidies. Both Canada and Mexico use taxation rates to varying degrees as part of an incentive package to keep local companies competitive and to attract new investment. [24] Canada has opted to stress personal taxation over corporate taxation, with the result now that the partially tax-induced migration of skilled and knowledge workers to the US has become a minor political issue.

Besides its effects on skilled labour migration, the emphasis on personal taxation has had one other major corporate effect. The Canadian integration of health insurance payments into the taxation regime means that a disproportionate amount of health expenditures are put on the individual taxpayer relative to his or her counterpart in the US. The result is a corporate benefit that can be very significant: some estimates in terms of the automobile industry range from $500 / 700 per car assembled in Canada. Other firms benefit proportionately.

In Canada and the US, the ability of the States and Provinces to manipulate tax levels has created ongoing tensions. The 1980s saw problems related to so-called "unitary" taxation, where states attempted to levy corporate taxes based on their proportions of the worldwide activity of companies. Lately, a Michigan law in the application of a corporate tax has upset Ontario companies doing business in that State.

Probably the most contentious tax issue between the two countries has focused on the royalty regime on wood cut from public lands. The softwood lumber disagreement has existed for the past 25 years, intermittently flaring up, especially when cross-border lumber competition becomes serious. Differing methods for allocating and charging for rights to cut timber on public lands in the two countries provide fertile conditions for recurrent claims of subsidy and injury.

While both countries maintain special tax regimes for research and development expenditures made by their resident companies, these differ according to the type of firm that is of special concern. In the United States, treatment of research and development expenditures is especially favourable to large multinationals that could do this type of work in other countries. In Canada, the focus seems to be more on smaller, local companies, if only because there are fewer multinational companies to encourage. R & D treatment in Canada for larger companies has tended towards a mix of tax benefits, outright subsidies and the provision of some research services.[25] In some cases, US defence requirements and contracting leads to similar effects in that country.

Incentives for corporate location in the US tend to take the form of tax abatements by local and State governments, rather than outright expenditures of public money. In general, the organizational culture of Canadian finance officials has resisted tinkering with the tax regime in this fashion, preferring instead to provide grant incentives, which are themselves taxable. The financial difference between the two regimes may be minimal in that both lower corporate input costs, but the differing incentive styles do create another venue for argument and counterclaims.

Health

There are three areas where health services, and expenditures are reasonably similar between Canada and the US. Treatments for specific conditions are about the same, the outcomes of both systems in terms of longevity are about the same and citizens in both countries are unhappy with the methods and levels of financing, coverage and administration. Beyond these, the systems appear to be converging in a number of ways.

The most obvious point of difference lies in the reliance of much of the Canadian health system on public taxation for its revenues and its direct control by provincial departments of health. The US system tends to rely on employer/employee contributions to insurance plans. Yet, the role of government in health expenditure in the US has been growing, while Canadian health officials have been delisting (or privatizing) specific services as a reaction to budget restrictions. The growth of large health service corporations (HMOs and others) in the US provides some parallel to the provincial departments of health. A rough estimate of Canadian public/private expenditures on health is 70/30, with the US at 40/60, and they are converging.

NAFTA Holdbacks

In the FTA and NAFTA negotiations, each side had particular economic sectors that it wished to protect. Roughly, these were cultural industries in Canada, defence procurement in the United States and the petroleum industry in Mexico. All of these areas contained tradable good and services and were politically sensitive.

Over time, each area of protection has been eroded to some degree. The Mexicans, whose constitution prevents non-Mexican ownership or activity in the petroleum industry, have narrowed the definition of what is covered by this mandate, thus allowing more foreign activity at the edges of this industry. For instance, reprocessing used motor oil has been removed from the definition of the petroleum industry, both for economic and environmental reasons.

US concerns about national security have diminished since the end of the Cold War and some restrictions on foreign participation have been relaxed. As well, the country has come to rely more on foreign supplies for vital parts such as DRAM chips and it has become increasingly clear that restrictions on some type of foreign corporate activity make little sense when so many of the components for "American" equipment are purchased abroad.

Canadian cultural holdbacks have been maintained, but even here, the advent of cheap satellite TV receivers and the coming maturity of the Internet as an entertainment medium means that policies restricting magazine runs and advertisement revenue tax deductions are increasingly anachronistic and ineffective.

In the end, each of the countries has maintained its holdbacks, but changing definitions and circumstances and technology has rendered them less obtrusive and less meaningful.

Standards

Government control of standards in business is of ancient origin. Both the Code of Hammurabi and clay cuneiform records tell us that governments were involved in weights and measures for at least 6000 years. The involvement of NAFTA countries in standards is very great and the record of integration is mixed.

An oddity lies in the allocation of telephone long-distance country codes. Canada and much of the Caribbean are unique in sharing the US country code (1). All other countries, including Mexico, have their own codes. Even the countries of the EU, which are otherwise highly integrated, have their individual country codes.

Physical measurements in all the NAFTA countries should relate to the metric system. The US adopted the metric system formally over 200 years ago, but it has never been implemented across the board. Both Canada and Mexico use it in business as well as daily life, though there is a lot of interchangeability in Canadian usage. The metric system is quietly used by much of US business, but it has only gradually crept into consumer purchasing (2-litre pop bottles, for instance).

Canadian and American patenting systems differ in their legal framework with the US persisting in its system of first-to-invent being granted patent rights, while the rest of the world follows a first-to-file system. The difference can seem minor, but the US tends to favour the innovator rather than someone's ability to put an application into the system. Patent rights, in any case, still tend to be national only, so that application has to be made in all countries where the inventor desires protection.[26]

Canada and the US also differ on the nature of building codes, which affect building product specifications and practices. Canadian provinces have gradually agreed to a National

Building Code, which allows for interprovincial trade in building supplies. The US has no national code and in many cases, building codes are local, which adds to the complexity of exporting building materials into different jurisdictions. While this practice is an impediment to trade, it affects US suppliers as well as Canadian exporters.

Many internationally traded products are today governed by various ISO standards, which purport to assure purchasers that globally recognized quality standards are being met. Various international standards councils are venues for international competition over these and other standards' contents and requirements, as these do have the effect of favouring some national production processes over others. Canada has played a minor role in these deliberations and even in North American regional councils, it has a tended to acquiesce in American standards designations. The result has been a high degree of standards integration between the two countries.[27]

Canada still maintains its own product approval agencies in areas of food, drugs and electrical equipment. It has maintained different automobile emission requirements and has attempted to regulate gasoline additives. There does not appear to be any consistency in leading or following the US on any decisions affecting the adoption or rejection of different products.

Canada and the US have used varying phyto-and phylosanitary rules in regulating trade. The case of fishing is full of examples. US rules related to the conservation of (Canadian) lobster stocks prevent the importation of lobsters below a certain size. Canadian rules for the conservation of fish stocks in border lakes require that fish caught by anglers in Canadian waters can only be kept if the anglers are staying in Canadian accommodations. Presumably this means they become subject to Canadian fishing regulations, which can be then enforced on shore. The West coast salmon "war" of the early 1990s related to Canadian use of conservation rules to force US salmon fishermen to offload their catches at Canadian ports, which had the incidental effect of protecting onshore processing jobs. US attempts to boycott or ban Mexican fish product exports derived from the use of drift nets, that incidentally caught and drowned dolphins, were negated by WTO decisions.

Conclusion

It seems that there is continuing movement toward closer economic integration in NAFTA, but it is not completely clear. Helliwell's study of border effects shows that integration has not proceeded as far in North America as in the EU, though there has been some change. Corporate policy and attitudes among transnational corporations in NAFTA seems to indicate that integration will be deepening. Yet, the record at the "plumbing" level is rather mixed.

Technology is eroding some distinctions between Canada and the US, but in many other areas, practices seem as far apart as ever. It would seem to make sense that an effort be made to develop a large and detailed checklist of factors of the kinds illustrated above in order to track the evolution of integration at this level.

The aim of this paper has been to illustrate the variety and complexity of behaviours, products, attitudes, policies and services that would have to be harmonized before one could meaningfully talk about integration. The creation of the NAFTA zone and its extension in practice into a number of areas beyond the original intent of trade has given a push to these societies toward greater integration. Studies of globalization and technological development seem to suggest greater integration is taking place in all parts of the world. But, until we have considered the huge variety of potentially integrative aspects of micro-and even submicro-economic and business behaviour, the conclusion that North America is becoming more economically integrated is still only guesswork.

Notes

[1] John F. Helliwell, How Much Do National Borders Matter? (Washington DC: Brookings Institution Press) p.13.

[2] See, for instance, Kenichi Ohmae, *Triad Power*, (New York: Free Press, 1985).

[3] Helge Hveem, "Political Regionalism: Master or Servant of Economic Internationalization?, in Bjorn Hettne, et al, *Globalism and the New Regionalism* (New York: St. Martin's Press, 1999) p.96.

[4] See, for instance, Bjorn Hettne and Fredrik Soderbaum, "The New Regionalism Approach" *Politeia* 17(3) 1998 pp. 11-12.

[5] I visualize this as Marx vs. Maslow.

[6] See his, *An Empire Wilderness: Travels into America's Future*, (New York: Random House, 1998).

[7] Helliwell, *op. cit*, especially chs 5-6.

[8] Bjorn Hettne, "Globalism and the New Regionalism: The Second Great Transformation", in Bjorn Hettne, et. al., *op. cit.*, pp. 11-13.

[9] Adapted from Hettne and Soderbaum *op. cit.*, pp. 12-14.

[10] Terrance Wills, "What's Canadian Culture Anyway?, National Post, 6 April 1999.

[11] *Ibid.*

[12] Canada, Royal Commission on the Economic Union and Development Prospects for Canada, Report *Volume 1*, (Ottawa: Minister of Supply and Services, 1985) Chapter 6.

[13] P.-P. Proulx and William Shipman, "Trade Relations Among Quebec, the Atlantic Provinces and New England", in William D. Shipman (ed.) *Trade and Investment Across the Northeast Boundary* (Montreal: IRPP, 1986)

[14] To my mind, this is a point that has been ignored in the past 15 years of debate about the FTA and NAFTA. The distortions created by the combination of the National Policy and the structure of US tariffs meant that Canadians were effectively disadvantaged in any industry that had immediate scale economies that required export and at the same time had a high value-added component. We did not have a "full-service economy" and until we do, it is hard to see how Canada has taken full advantage of the FTA and NAFTA.

[15] Stephen Blank and Jerry Haar, *Making NAFTA Work: US Firms and the New North American Business Environment* (Miami: North-South Center Press, 1998) pp. 56-61.

[16] *bid.*, p.42.

[17] *bid.*, p.51.

[18] *Ibid.*, p.49. The book describes a process whereby Ford used its Hermosillo plant as a flexible manufacturing laboratory. A similar approach was used by Pratt & Whitney in its plant in Halifax.

[19] Clive Allen, Senior Counsel to Nortel Networks, alluded to this process in his remarks to the Canada/US Law Institute, Case Western Reserve University, Cleveland OH, 18 April 1999.

[20] Atlantic Provinces Transportation Commission, *Tips & Topics* 39(4) April 1999 p.3.

[21] Presentation by B.F. Mathaisel, Chief Information Officer, Ford Motor Co., to the Canada/US Law Institute, *op. cit., 16* April 1999.

[22] Patricia Pearson, "Why the Border's Still a Barrier, *Globe and Mail* 11 May 1994.

[23] Mark Shaffer and Pat Flannery, "People Caught in Nogales go back to Mexico via Douglas", Arizona Republic 22 February 1999.

[24] There is no lack of materials on this subject. See, for instance, Mahmoud Iqbal, "A tax Comparison of Large Manufacturing Industries in Canada, United States and Mexico" (Ottawa: The Conference Board, 1994) and Finance Canada, *Report of the Technical Committee on Business Taxation* April 1998.

[25] Presentations by H. David Rosenbloom, Caplin & Drysdale, Washington DC, and David Burn VP Taxation, Northern Telecom Ltd. to the Canada/US Law Institute, *op. cit*, 17 April 1999.

[26] See, for instance, Canadian University Intellectual Property Group, "A guide to protecting Intellectual Property" www.uilo.ubc.ca/cuipg.htm

[27] Presentation by Prof. Tony Schellinck to the Dalhousie Faculty of Management research series, January, 1999.