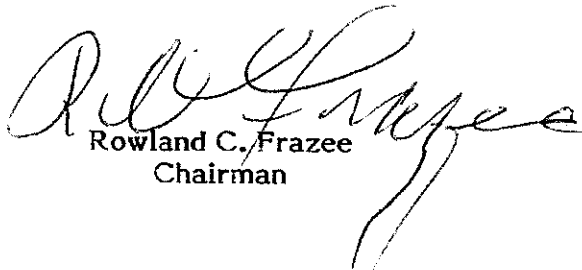
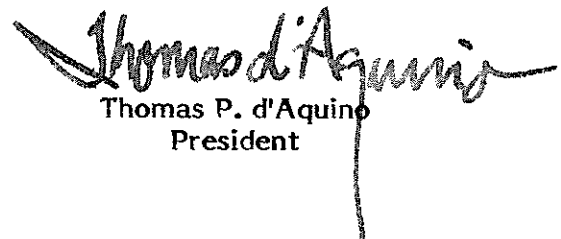


A RESPONSE BY THE
BUSINESS COUNCIL ON NATIONAL ISSUES
TO A PAPER TABLED BY
THE RIGHT HONOURABLE JOE CLARK P.C., M.P.
SECRETARY OF STATE FOR EXTERNAL AFFAIRS

COMPETITIVENESS AND SECURITY:
DIRECTIONS FOR CANADA'S
INTERNATIONAL RELATIONS

JANUARY 1986
OTTAWA


Rowland C. Frazee
Chairman


Thomas P. d'Aquino
President

This paper reflects the views of the Business Council on National Issues and the work of the Task Forces on National Finance, the International Economy and Trade, and Foreign Policy and Defence. The Task Forces are chaired respectively by Messrs. Darcy McKeough, Alfred Powis and Peter Cameron.

The Business Council on National Issues is composed of chief executive officers of 155 leading Canadian companies, representing all sectors of the Canadian economy. The Council is the means by which business leaders in Canada have chosen to contribute personally to the development of public policy and to the shaping of national priorities.

The corporations which make up the Business Council administer in excess of \$650 billion in assets which produce annually more than \$240 billion in revenues. The member companies employ more than 1.5 million Canadians.

Business Council task forces are active in the areas of economic policy, international trade, industrial and competition policy, taxation, social policy, government institutions, and foreign policy and defence.

INTRODUCTION

Predicting the future is always a hazardous activity, and no field is more challenging to grapple with than international affairs. Consideration of a nation's foreign policy requires applying a long-term strategic view to the lessons of history, to the predicted global trends of tomorrow, and with even greater difficulty, to the perceived policies of other nations. All of these factors are beyond the control of national policymakers.

It is with a recognition of these limitations that the Business Council on National Issues welcomes this opportunity to respond to Competitiveness and Security: Directions for Canada's International Relations. It should be stated at the outset that we believe that Competitiveness and Security raises a host of important policy issues that must be addressed as Canada proceeds to fashion its external policies in future years. But rather than responding to all of the issues raised in the paper, we will concentrate on a few select developments which we believe have special significance for Canada. These will be presented under two broad headings: Canadian Security and Sovereignty, and Competitiveness and Economic Policy in a Changing World. Because the Business Council on National Issues has recently pronounced at some length on the subject of Canada-United States trade and economic relations, the second half of this paper will mainly focus on key multilateral economic issues of concern to Canada.¹

The first step is to position Canada within the global environment. Viewed from this perspective, it is clear that Canada holds a remarkably privileged position with a high standard of living, an educated work force, and freedom from the devastation of war or overpopulation. Yet Canada is more than the sum of its natural or socio-economic descriptors; it is also rich in its values -- a liberal, Western, capitalist democracy with a history of stable government, an enviable record in human rights, and a longstanding concern for the struggling and less privileged.

Canada is also a moderately-sized, open economy with an enormous stake in a liberal and effectively functioning global trading and economic system. With the world's ninth largest economy; with memberships in the Economic Summit, the North Atlantic Treaty Organization (NATO), the United Nations (UN), the Commonwealth, and La Francophonie; with a respected history of international activism including well established programs of development assistance and sixteen UN peacekeeping operations; and with cultural links to many countries through our two founding races and rich cultural mosaic -- with all of these enviable features, Canada is a nation with considerable potential for influence in the world. Though not a super power, Canada's middle-power status creates both global opportunities and responsibilities.² Despite the natural proclivity to compare Canada's attributes with those of the United States -- where Canada tends to suffer a 10 to 1 disadvantage -- it is important to stress that relative to most of the nations of the world, Canada has attained an impressive degree of economic well-being, stability and influence.

CANADIAN SECURITY AND SOVEREIGNTY

A continually changing international environment creates varying threats and opportunities for Canada's national security. Our economic prosperity, our form of government, and our values are subject to constant challenge. The federal government has a clear responsibility to take a leadership role in defining Canada's security interests, in recognizing and explaining threats to those interests, and in developing appropriate policies to protect and further Canadian security. In the past, Canada's geography protected the country from the horror of war and conquest. Now, however, the universal destructive nature of nuclear warfare has put Canada at risk and made the search for a credible defence posture more necessary. Canadians recognize that Canada cannot realistically expect to safeguard its security by acting alone. The strong support evident among Canadians for NATO and NORAD, and for Canada assuming a fairer share of the Alliance burden, indicates a widespread understanding and acceptance of the need for defence cooperation between Canada and its allies in the free world. The fact that such broad, public support for collective defence efforts continues to exist in Canada should not be overlooked when the parliamentary hearings to review Competitiveness and Security take place. Many groups will be calling for a radical alteration of this country's postwar national security policies. The evidence clearly suggests that their views are not representative of those of our citizens as a whole.

The Soviet Threat

The most salient threat to Canada and the community of democracies is posed by the Soviet Union's continually expanding military power.

The underlying strategic trend of the last twenty years has been the steady erosion of the military balance between East and West, a balance which has been a major factor in the maintenance of peace. Across most dimensions of military capability, the Soviet bloc has now equalled or surpassed the NATO alliance, and the trend toward increasing Soviet military power shows little sign of being reversed. As noted in Competitiveness and Security, in the nuclear sphere the Soviets at the very least have now attained a position of rough parity with the West in strategic forces, and enjoy a clear superiority in theatre nuclear forces in Europe. It is widely recognized that the conventional forces of the Soviet bloc are considerably stronger than those of NATO. The Soviet Union has also developed a very impressive capability to project its growing military power worldwide. In the area of naval forces, the massive increase in Soviet strength in recent decades is particularly striking in view of the Soviet Union's comparatively minor dependence on the oceans for commerce.³ This military build-up has been accomplished at high cost to the Soviet economy, with an estimated 12-14% of its Gross National Product (GNP) being devoted to defence.⁴ The priority attached by Soviet leaders to defence and security has resulted in the development of an offensively postured and equipped military force, particularly in the area of conventional and theatre nuclear forces in Europe.⁵

The evidence of vastly strengthened Soviet bloc military capability is clear. What is less transparent, however, are Soviet intentions. In international relations it is not possible to determine the intentions of other countries with absolute certainty. Of necessity one must infer policy motivations from observable facts. The history of East-West relations indicates that military power has been the principal mechanism of Soviet expansion and the key to the consolidation of its external power. The Soviet Union's role and influence in world affairs are inextricably linked to its steadily increasing military power. Indeed, it is primarily in the military

sphere that the U.S.S.R. enjoys an unambiguous status as a superpower. It can be argued that a natural historical insecurity regarding Western intentions gives rise to exaggerated Soviet defensive concerns.⁶ But its huge military build-up and its reliance on force and coercion as instruments of both domestic control and diplomacy suggest that Western governments would be ill-advised to view the Soviet Union as a purely defensive power. The fact is that it does represent a real threat to Western security and to Western global interests. In short, regardless of the motivations of Soviet leaders, the potent capabilities of the Soviet Union and its profoundly anti-democratic values must be treated as a threat to the Western democracies.

Collective Security and Canada's Defence Policy

Canada's postwar security policy has essentially rested on three complementary strategies: deterrence of aggression through collective security arrangements within NATO including bilateral arrangements with the United States for North American defence -- for example NORAD; pursuit of reciprocal and verifiable arms control agreements; and commitment to the peaceful settlement of international disputes through the United Nations and other appropriate agencies. The Business Council on National Issues supports these strategies. As emphasized in Competitiveness and Security, these various approaches to security are mutually supportive rather than incompatible. Thus, Canada's full participation in NATO and NORAD in no way threatens or invalidates our interests in arms control or our occasional participation in UN peacekeeping initiatives.

For the Western world, national security in the second half of the twentieth century has become synonymous with deterrence. Although subject to occasional debate within the alliance, the NATO policy of deterrence

through flexible response is widely seen as appropriate in the present strategic environment. To be effective, deterrence requires that a potential aggressor be convinced that the costs of aggression will outweigh the gains. The advantage of NATO's strategy of flexible response is that adversaries are deterred both by uncertainty about the severity of an initial response to aggression, and by the possible escalation to an increasingly destructive response. Thus, should a massive Soviet conventional attack not be stopped by conventional forces, NATO could reply with tactical nuclear weapons, and if necessary with strategic nuclear weapons.

NATO's deterrence strategy has been criticized from a variety of perspectives. One major critique suggests that peace-seeking democracies should renounce a first-use nuclear option; while a second and more pragmatically oriented critique argues that due to the high cost of conventional forces, NATO should rely solely on nuclear retaliation as a less expensive defence alternative. Both of these suggestions are flawed. Relying solely on a massive nuclear response is no longer credible in an era of reciprocal nuclear vulnerability; nor would it permit a more measured response to other limited forms of aggression, for example minor military attacks, or political and economic threats. The former view, that NATO should renounce a first use of nuclear weapons, is also inappropriate, for in the face of a successful conventional Warsaw Pact attack, NATO would be precluded from escalating its response. The logic of this strategy demands that NATO maintain and deploy much more powerful and expensive conventional forces, sufficient to prevent a Soviet victory in a conventional European war. If this objective were attained, it might then prove possible for NATO to adopt a no-first use posture. Proponents of this policy should therefore be strong supporters of a major increase in NATO and Canadian conventional military capabilities.

Indeed, it is precisely this desire to raise the nuclear threshold that underlies the argument in favour of much stronger Western conventional forces, not just in Europe but in other important areas of the world as well.⁷ Unfortunately, as made clear in Competitiveness and Security, Canada's military capability and preparedness were allowed to deteriorate severely in the 1960s and for much of the 1970s as well.⁸ However, during this period there was no corresponding contraction of Canada's basic military and security commitments. Canada maintained its commitment to common defence within the NATO alliance on land, air and sea, with regard both to Europe and to North America, and to protect and promote its own territorial security and sovereignty. As a result, by the late 1970s and early 1980s, a yawning gap had come to exist between the various defence obligations accepted by successive Canadian governments on the one hand, and the military forces and equipment required to meet these commitments, on the other. Our deep concern over this unsatisfactory state of affairs prompted the Business Council to establish a special Task Force on Foreign Policy and Defence in 1981. After three years of extensive investigation, we published a document outlining the key problems confronting Canadian security policy in the current and emerging international environment, and proposed a fairly detailed plan designed to bring Canadian military capability up to a level commensurate with the country's defence commitments over a period of 10-12 years.⁹

Examples of Canada's military deficiencies are not difficult to find. As part of NATO, Canada maintains land and air forces in Europe -- the 4th Canadian Mechanized Brigade Group (4CMBG), and the 1st Canadian Air Group (1CAG). We have also designated further Canadian-based forces for deployment to Allied Command Europe (ACE) in the event of crisis, and agreed to commit an air-sea transportable brigade group (CAST) to Norway, and a mobile infantry battalion group and additional fighter squadrons to the

Northern European Flank. These forces face significant deficiencies. 4CMBG is seriously undermanned, and lacks appropriate air defence, chemical warfare and night fighting capabilities. The survivability of this formation for even a few days of active operations is very doubtful. 1CAG is not properly protected against enemy air attacks. It is lacking in hardened shelters, advanced low-level air defence systems and capabilities for maintaining and repairing runways.¹⁰ All of these problems demand corrective action. The new federal government has acted with dispatch to provide additional troop strength to our NATO force structure. However, over time it is evident that more must be done to close the gap between Canada's capabilities and the defence obligations we have undertaken through NATO. Other elements of our Armed Forces, for example our Maritime Forces, face even more serious deficiencies than our European-based and -tasked forces, and will also need to be strengthened significantly over the next decade or so. Unless action is taken to upgrade Canada's military capabilities, our ability to meet our NATO obligations will continue to be doubtful.

In addition, it is also necessary to consider Canada's ability to protect and safeguard its own territorial sovereignty. The sad fact of the matter is that we have virtually no military presence in our vast northern regions, and only a very limited capacity to conduct adequate surveillance or military operations in this huge area. Moreover, in light of Canada's extensive maritime interests as the nation with the longest coastline in the world and which borders three oceans, our current naval forces are far from capable of effectively enforcing Canadian maritime claims, particularly since the advent of 200-mile coastal state jurisdiction. This inability to properly enforce jurisdiction and undertake effective surveillance activities is most glaring in the case of the Arctic waters, over which Canada's claims of jurisdiction are not universally accepted, and where present Canadian military capabilities are almost non-existent.

In view of these many deficiencies in Canada's military capabilities, the Business Council has concluded that a balanced, two-phased program is required to gradually reverse the major decline in the capabilities of the Canadian Armed Forces.¹¹ Phase one would concentrate on re-equipping, while in phase two the priority would be to increase manpower resources. To meet Canada's defence requirements, the regular forces would rise from 83,500 to 115,000 over 10-12 years. The reserves would also be substantially strengthened. This program would not be cheap. It would necessitate a modest shift of government expenditure commitments away from other programs and in favour of national defence. However, by implementing this program Canada would be moving to assume a defence burden more commensurate with our size and wealth, and more in line with that accepted by other NATO powers.

Other Defence Issues

Two other defence-related issues deserve brief mention here. The first is the question of national preparedness. Not surprisingly, the decline in Canada's military capability has been more than matched by a deterioration in national preparedness, which may be defined as the ability to mobilize military and civilian resources in the face of emergencies or international conflicts.¹² By the end of World War Two and into the 1950s, Canada had an impressive mobilization capability.¹³ During the following decades, however, de-emphasis and general neglect of defence led to a complete atrophying of our rapid mobilization capacity, which is essential to our commitment to European defence.

Recently a shift has occurred in alliance thinking away from a "short war" strategy to "sustainment." Whereas formerly it was assumed that any conventional war would be of relatively short duration, it is now recognized that the deterrent effect of conventional forces is enhanced by the ability to maintain and increase their capability in the field over an extended period. This strategy yields two imperatives for Canada. First, there should be a plan and a structure within government to mobilize the country on short notice. Second, Canada needs the industrial capacity that can be mobilized to produce the necessary equipment required to keep armed forces in the field.

Although Canada's present mobilization capacity is deficient, modest progress is being made. At the level of government planning, in accordance with the 1981 Emergency Planning Order, National Emergency Agencies are being created in key sectors under the appropriate Ministers and with the coordinating assistance of Emergency Planning Canada. The Business Council views this step as prudent and useful.

However, we are concerned about the state of Canada's defence industrial base. Since the cancellation of the Avro Arrow Project in 1958 Canada has essentially opted out of the business of major weapons systems research and development. In addition, the reduction of military budgets in the sixties led to a drop-off in the acquisition of military equipment and a resulting reliance on the part of Canadian industries on foreign markets. With the establishment of the Defence Production-Sharing Agreement (DPSA) and the Defence Development-Sharing Arrangement (DDSA), a virtual free trade area in defence material was created with the United States. Over time, a limited modern defence industry has developed, geared largely to producing dual-military and civilian-use products, with expertise in areas such as communications, electronics and specialized aviation. But it is largely a build-to-print industry, lacking a significant independent research and development

base and responsive to foreign market opportunities, not to Canadian defence and strategic requirements. For many years DND research and procurement tended to emphasize this natural trend. Policies did not function in a way which would enhance our industrial base.

The problems affecting the defence industrial base are presently being reviewed by work groups in the departments of Regional Industrial Expansion, Supply and Services, and National Defence. The Business Council is pleased to see these issues being actively considered by the government and views this as prudent and useful. It is our concern, however, that the activities of these work groups may not receive the attention and coordination required from senior levels within government, and that as a result there is a danger of fragmentation of effort, policies and results.

Accordingly, we strongly recommend that consideration be given to merging the present work groups into one interdepartmental Task Force; that as an immediate measure a committee be struck to coordinate the industrial preparedness work already underway; that the committee be composed of the Deputy Ministers of the relevant departments; and that overall political responsibility be vested in one designated Minister. We further recommend that an Advisory Committee on Industrial Emergency Preparedness be formed with strong private sector representation to aid the Government in its work in this area. The Business Council would be pleased to assist in putting forward nominees for this Committee.

The second defence-related issue is arms control. Continued support for NATO and an improvement in Canadian military capabilities by no means excludes the possibility that arms control can play an important role in enhancing Canada's security, as was clearly recognized in Competitiveness and

Security.¹⁴ Canada has long been active in international discussions and forums aimed at achieving arms control and disarmament accords, both in the United Nations and in NATO. For example, Canada has called for agreement among the nuclear powers to prevent or control the development of new nuclear weapons systems (e.g., in space); has participated since 1974 in the Mutual and Balanced Force Reduction Talks in Vienna between NATO and the Warsaw Pact; has participated vigorously in the Conferences on Security and Cooperation in Europe held in Finland in 1975 and in Spain in 1983 and also in the recent Stockholm Conference on Confidence Building Measures in Europe; and has called for the negotiation of an international convention to eliminate chemical weapons stockpiles and prohibit the development of new chemical weapons. Canada should continue to work for the development of verifiable arms control accords between NATO and the Warsaw Pact, between the superpowers, and more generally. However, it should be pointed out that Canada's present inadequate contribution to the NATO alliance cannot help but lessen our credibility within the alliance on arms control matters. In particular, Canada's voice would carry more weight if the Canadian contribution to NATO's conventional military capability were more proportionate to the country's economic and political standing in the world.

COMPETITIVENESS AND ECONOMIC POLICY IN A CHANGING WORLD

The remainder of the twentieth century promises to be a period of major challenge for the Canadian economy. The severe problems presently evident in the international economy, from rising protectionism to the Third World debt crisis, will continue to form an unstable and somewhat ominous backdrop against which Canada must evolve its policies toward the external economic world. Intensified competition from developing and industrialized countries alike will put increasing pressure on a host of Canadian industries in the years ahead. A central economic challenge facing Canada will be to meet and adapt to this growing competition. Another challenge will be to work to strengthen the existing system of multilateral economic institutions and arrangements that have provided a measure of predictability, stability and order in the world economy since the late 1940s. Canada has a special interest in this area, having been a leading participant in the construction of the postwar international economic system in the early years following World War Two.

More than most nations, Canada has a major stake in the preservation of a stable, orderly and open world economy. Canadian policy must be made in full awareness of the variety of ways in which the international economy shapes and constrains Canada's options and opportunities. Few if any of the key domestic policy objectives embraced by most Canadians and successive national governments will be realized if Canada's competitive position in the world deteriorates. As a moderately-sized, open economy heavily dependent on foreign trade and capital flows, Canada has a strong interest in promoting open global markets and well functioning international institutions and rules. This perspective is clearly reflected in Competitiveness and Security, and the Business Council wishes to record our concurrence with the emphasis put in

that document on the need for improved competitiveness and a strengthened multilateral economic system.

Trade

With close to 30% of GNP derived from exports of goods and services, Canada is vitally concerned with both foreign market access and the effectiveness of international institutions and arrangements concerned with trade. (Comparable figures for the export dependence of the United States and Japan, Canada's two largest trading partners, are approximately 10 to 14 percent, respectively.) Up to 3 million Canadian jobs depend on international trade. Moreover, the importance of exports to the Canadian economy has been increasing over the past three decades. In 1965, merchandise exports amounted to 15.6 percent of Canada's GNP; today, the figure exceeds 25 percent. As the international economy grows more interdependent and Canadian industry seeks to achieve greater efficiencies, Canada's reliance on foreign trade will continue to increase in the years ahead.

In spite of the importance of trade to Canada's economic welfare, until recently the subject has not received the attention or priority it deserves, either by governments or the broader public. Canadians need to understand better Canada's enormous stake in the international trading system and in the gradual lowering of impediments to trade in most economic sectors. Canada's share of world exports has been declining. Reversal of this unfavourable trend will require a strengthened competitive position for Canadian industry as well as more assured access to foreign markets. Success in achieving these two related objectives will pay off in the form of higher per capita incomes and more jobs. Failure threatens to consign us to a deteriorating relative standard of living and a less vigorous Canadian economy.

Canada has long been a principal supporter of multilateral trade liberalization through the General Agreement on Tariffs and Trade (GATT), by far the most important international organization in the sphere of trade and commercial relations.¹⁵ Through the GATT negotiations, Canada has achieved improved access to foreign markets, and has also agreed to lower its own tariff and non-tariff barriers to trade. The seven rounds of GATT trade negotiations that have taken place since the late 1940s have been particularly effective in slashing tariff rates on industrial goods. By January 1, 1987, average tariffs on dutiable industrial imports will have declined to 5-7 percent in the European Community and Japan, to 4 percent in the United States, and to 9-10 percent in Canada. (Tariffs are considerably higher than this in some sectors.) GATT has also achieved some success in regulating and disciplining the use of non-tariff barriers (NTBs), such as subsidies, quotas, government procurement practices, and many other measures that impede trade. However, NTBs have proven much more difficult than tariffs to address through GATT negotiations. Finally, GATT has provided a useful mechanism to address and resolve commercial policy disputes among countries.¹⁶

A new round of GATT negotiations will soon take place, and the Business Council believes that Canada should continue to attach high priority to the further reduction of foreign trade barriers through the multilateral GATT system. There is a pressing need to deal more effectively with such difficult issues as safeguards, subsidies and barriers to trade in services.¹⁷ Another GATT round can help to head off the protectionist pressures now growing throughout much of the world and which pose a serious threat to the integrity and effectiveness of the postwar multilateral trade order established in the late 1940s and 1950s. It can also help to strengthen the GATT as an institution vital to the maintenance of a well-functioning trading system. But it is not likely to provide an appropriate forum for Canada to develop new

market access arrangements with the United States. Thus, we believe that bilateral trade discussions with the United States should also be pursued at the same time, and we commend the federal government for inviting the United States to enter into such discussions.

Economic Relations with the Third World

In the long term, Canada has several reasons to be concerned about the Third World -- political, economic and humanitarian. Famine and crushing poverty in any part of the world are disturbing. Canadians continue to be moved by the spectre of starvation and deprivation globally. Unfortunately, this problem is likely to remain acute in the coming decades, and Canadians will continue to search for ways to offer assistance.

Canada also has extensive economic linkages with developing countries. Canada is certainly affected by the Third World's serious debt problems. Simply stated, if the Third World cannot repay its debts, the banking system will be faced with enormous non-performing loans with dire consequences for the world financial and trading systems. While the crisis atmosphere of 1982 and 1983 has passed, recent events indicate that the debt situation remains fragile. Exports of several of the major debtor countries are only now beginning to rise dramatically -- Brazil and Mexico are striking examples -- and the absolute levels of debt remain very high. Continuing high real interest rates have made debt repayment an especially complicated problem for the international community.

Nevertheless, the world has managed the international debt situation well to date. Institutional cooperation, including the exchange of vital

information, has been improved over the pre-debt crisis situation. Not only the International Monetary Fund and private banks, but also the debtor countries themselves share responsibilities to the world community. More use of private, direct capital investment in the affected countries, thereby reducing their dependence on loans and aid, would be desirable. Aid from the wealthier countries to the poorest, especially in Africa, will also be required; the commitment of the Canadian government and people in this respect is commendable given the country's present economic circumstances. The indebtedness problem of developing countries cannot be solved overnight. Grand schemes to ameliorate the problem on a world-wide basis probably should be avoided. However, the careful proposals outlined by the U.S. Secretary of the Treasury, James Baker, on October 8, 1985 to the annual meeting of the International Monetary Fund may help to address the debt situation facing many developing countries in a constructive manner. A greater role for the World Bank and increased investment in Third World countries are certainly called for, and we believe that Canada should be active in exploring these and other ways to assist hard-pressed Third World economies. A sense of mutual responsibility, patience, and sensitivity to the political and social elements involved in the adjustment process of developing countries will clearly be needed on the part of both lenders and debtors in the years ahead.

Canada is also linked to the Third World as a market for exports. Over the last decade the Third World has been a rapidly growing market for the developed world. A few examples of the present percentage of exports going to the developing countries include: Canada-12%, U.S.A.-35%, Japan-45%, and for the developed countries as a whole, 25%.¹⁸ Thus our future growth and prosperity is linked, at least in part, to the Third World. On the other hand, as suppliers of raw materials and commodities, some developing countries

compete with Canada for export markets. Of course the Third World is not a homogenous entity. Several of the Pacific Rim "Newly Industrialized Countries" (NICs), such as Taiwan, Hong Kong, South Korea, and Singapore, are becoming increasingly developed, mature economies. These countries should become a more important focus of Canada's foreign economic policy in the future.

A final direct economic linkage is our substantial annual expenditure on foreign aid. Channelled through the Canadian International Development Agency, through multilateral assistance programs, and through voluntary agencies, our official development assistance is targeted to rise to 0.6% of GNP in 1990 and 0.7% by 1995. Present aid totals are approximately two billion dollars a year. This is a significant sum of money for Canada and the Third World, and we must ensure that the maximum potential benefit is achieved. As Canada's own economic and fiscal circumstances improve, the Business Council believes that Canada should aim to increase financial and other forms of aid, particularly to the poorest developing countries. At present, however, Canada's own difficult fiscal position militates against any significant expansion of foreign aid.

The Need for Greater Policy Coordination

In an increasingly interdependent world, many of the major economic problems facing Canada and other countries cannot be solved or effectively dealt with through unilateral national decisions. This is now generally understood by the governments and the peoples of the leading industrialized countries. Different views in the world's largest industrialized countries on the priority to be attached to various problems and policy objectives can

lessen the capacity for effective collective management of the international economy. The institution of annual economic summits, involving the heads of government of the seven major noncommunist industrialized countries and the European Community, reflects a recognition of the need to strive for a measure of consensus among the world's major economies on fundamental issues. However, recent experience suggests that the system of collective economic management has not been as effective as might be hoped. The severity of the 1981-82 recession, for example, was partly attributable to a lack of policy coordination by the leading industrialized nations. The instability evident in international foreign exchange markets in recent years has also proven difficult for the governments of the major industrial countries to deal with. What is needed among the leading economies is a greater degree of coordination and consensus on such key macroeconomic issues as fiscal policy, monetary policy, and exchange rates. Other issues, such as the rise of protectionism and the Third World's debt difficulties, also require a more coordinated response from the major economic powers.

Acting alone, there is little that Canada can do to strengthen global economic management or to improve policy coordination among the key industrialized states. However, a priority for Canadian international economic policy should be to seek such strengthening and improvement whenever we can. We must work with our major trading partners and fellow industrialized countries to grapple with economic issues that cannot be addressed effectively by countries acting in isolation. The recent successful effort by the five largest industrialized countries to institute a more coordinated policy on exchange rates offers but one example of the benefits that can flow from more effective collective economic management. Because of their preponderant economic influence and their similar values and economic systems, the leading Western industrial countries have the potential to act as

the guarantors and principal managers of the multilateral economic order. To do so properly, they must be more willing to examine carefully the international ramifications of domestic policy decisions, and to undertake actions in concert with their allies for the long-term good of the global economy. Acceptance of this principle should be a cornerstone of Canada's foreign economic policy in future years.

CONCLUSION

Competitiveness and Security reviews the key issues confronting Canada in the two spheres in which our involvement with the external world is most extensive and significant -- defence and security, and international economic affairs. Although the External Affairs paper does not say so explicitly, the implicit message it conveys is that the foundations of Canada's previous defence and foreign economic policies remain sound. The Business Council does not dissent from this view. The objectives which have heretofore guided Canadian security policy have included the maintenance of deterrence through effective collective security arrangements within the Western Alliance; the quest for reciprocal and verifiable arms control agreements; and the peaceful settlement of disputes through the United Nations and other mediatory instruments. In the present and emerging global security environment, there is no need to alter these objectives. Instead, what is called for is a greater Canadian effort in the area of defence and security policy, through the improvement of our seriously inadequate defence forces. Once this has been achieved, Canada's voice on many international security matters, including those relating to arms control, will carry more weight.

Similarly, the basic policies adopted by Canada toward international economic affairs have served the country well and should continue to influence the course we follow in the future. Strong multilateral economic institutions and the development of credible rules and norms to guide and manage the international economic behaviour of countries are unquestionably in the interest of a moderately-sized, open economy such as Canada. The most pressing multilateral economic challenge is to resist the onslaught of protectionist forces, which is threatening to unravel the liberal international trading system established in the late 1940s and based in large part on the

GATT. A new and successful round of GATT trade negotiations is a priority for the last half of the 1980s. It is to be hoped that such a round will lead to new international disciplines being imposed on non-tariff barriers and other trade-distorting devices and policies, as well as to the further liberalization of remaining tariffs. Another key international economic issue that will require the sustained attention of policy makers in Canada and elsewhere is the debt situation confronting many Third World countries. Flexibility and patience will be essential as efforts are made to develop arrangements that permit these countries to repay their loans without having to undergo intolerable social and economic dislocation. Finally, Canada should work with its major developed country allies and trading partners to strengthen the system of collective economic management built up by the industrialized countries in the decades following World War Two. Greater policy coordination, and an increased willingness to take into account the international ramifications of domestic policy choices, are urgently needed, and Canada should do what it can to achieve progress in this important area.

Footnotes

1. Business Council on National Issues, Canadian Trade, Competitiveness and Sovereignty: The Prospect of New Trade Agreements with the United States, September 1985.
2. Royal Commission on the Economic Union and Development Prospects for Canada, Report, Volume I, pp. 204-206.
3. See The Commission on U.S.-Soviet Relations, The Soviet Challenge: A Policy Framework for the 1980s (New York: Council on Foreign Relations, 1981).
4. There is some dispute concerning how rapidly the Soviet Union has been increasing its real defence expenditures in recent years, with some analysts suggesting 4-5 percent and others (including the U.S. Central Intelligence Agency) closer to 2 percent. See the NATO publication, NATO and the Warsaw Pact: Force Comparisons, p. 41.
5. Coit D. Blacker, "Military Power and Prospects," Washington Quarterly Volume 6 (Spring 1983), pp. 57-9; Harriet Fast Scott and William F. Scott, The Soviet Control Structure: Capabilities for Wartime Survival (New York: Crane, Russak, 1984).
6. Blacker, op., cit., pp. 57-61.
7. The International Institute of Strategic Studies, The Military Balance, 1983-1984, pp. 134-7.

8. R.B. Byers, "Canadian Defence and Defence Procurement: Implications for Economic Policy," in Denis Stairs and Gilbert R. Winham, eds., Selected Problems in Formulating Foreign Economic Policy (Toronto: University of Toronto Press; volume 30 in the research studies for the Royal Commission on the Economic Union and Development Prospects for Canada, 1985), pp. 138-40.
9. Business Council on National Issues, Canada's Defence Policy: Capabilities Versus Commitments, September 1984.
10. Canada, Standing Senate Committee on Foreign Affairs, Proceedings of the Sub-committee on National Defence, November 25, 1980, pp. 3:16, 3:17, 3:26.
11. Business Council on National Issues, Canada's Defence Policy, pp. 40-49.
12. William J. Yost, Industrial Mobilization in Canada (Ottawa: Conference of Defence Associations, 1983).
13. During this period, national defence mobilization plans envisaged that Canada would have an ability to provide a 100,000 man Navy capable of playing an important role in defence of the North Atlantic; a field army of six divisions with supporting arms and services; and a balanced air force.
14. Canadian Institute of International Affairs, The Other Road to Security: Canada and Disarmament, June 1982.

15. Frank Stone, Canada, the GATT and the International Trade System (Montreal: Institute for Research on Public Policy, 1984).
16. See John H. Jackson, World Trade and the Law of GATT (Indianapolis: Bobbs-Merrill, 1969).
17. Minister for International Trade, How to Secure and Enhance Canadian Access to Export Markets (Department of External Affairs, January 1985), pp. 11-16.
18. Margaret Biggs, "The Developing Countries in the International Trading System," in John Whalley, ed., Canada and the Multilateral Trading System (Toronto: University of Toronto Press, 1985), p. 72.