International Investment: Canadian Developments In A Global Context

INVESTMENT CANADA
INVESTISSEMENT CANADA

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International Investment: Canadian Developments In A Global Context

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International Investment: Canadian Developments In A Global Context is being circulated so as to help inform Canadians about the forces of globalization and the important role international direct investment, in particular, is playing in this process. Investment Canada will update this document periodically to incorporate recent data. The presentation is designed to be strictly factual and responsibility for interpretation of the data is assumed by the Research Branch of Investment Canada.

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Introductory Remarks

With the post-war globalization of world markets, international competition has greatly intensified. The business sector is having to restructure itself in order to meet this competition, and global corporations are becoming more dominant. Joint ventures, mergers, acquisitions and other forms of strategic alliances are breaking down the distinction between domestic and foreign firms. Indeed, foreign investment is rapidly becoming the strategic instrument by which firms are assuring themselves access to overseas markets. Foreign investment is also increasingly a means for facilitating access to new technology and skilled human resources.

This presentation commences with an overview of the key economic dimensions of globalization - that is, the growing interdependence of consumers, producers, suppliers, and governments in different countries. Globalization does not imply the sweeping away of national or cultural distinctions, but it does mean that government policies such as those towards foreign investment must be considered in the context of international trends.

Most industrialized countries have a relatively open policy towards foreign investment, or are in the process of liberalizing their policies. With the replacement of the Foreign Investment Review Act by the Investment Canada Act in 1985, the Government of Canada signalled its recognition that investment is central to economic growth and technological advancement. In addition to regulating foreign acquisitions, Investment Canada actively promotes Canada as an attractive place to invest - both by Canadians and non-Canadians.

Investors appear to have responded to this welcome. Domestic and international investment in Canada strengthened impressively, helping to sustain economic growth and to fortify Canada's long-term competitive position. Canadians have also recognized the need to participate in international investment, as evidenced by the fact that during the past decade overseas investment by Canadians grew at twice the rate of foreign investment in Canada.

Despite the increasing role of international investment in major industrialized countries, many Canadians continue to express concern about the possible implications of a more open economy. These concerns appear to be misplaced, for the benefits of globalization far outweigh the disadvantages. Nonetheless, the Government is sensitive to these concerns and Investment Canada has the statutory obligation to review acquisitions by foreign investors. Foreign takeovers are not approved unless the Minister responsible is satisfied that they will be of net benefit for Canada.

A Four Part Presentation: Key Themes

A. Globalization Of Markets

- the rapid growth in trade and investment, more rapid than the growth in world output
- the internationalization of financial markets
- the extensive industrial restructuring and reorganization of firms
- the increased international corporate and research networking
- investment as a strategic instrument

B. International Investment In Canada

- a significant increase in foreign direct investment, due primarily to retained earnings rather than cross-border flows
- a small increase in the degree of foreign control since 1985, following a significant decline after 1971
- the growing diversification in the sources of foreign investment; the importance of U.S. investment has declined while the importance of Japanese and Hong Kong investment has increased
- a growing proportion of foreign direct investment is for acquisitions; nonetheless, FDI in new businesses and expansions has continued to increase
- approximately half of foreign acquisitions in any one year involve the takeover of already foreign-owned assets in Canada
- 60 per cent of foreign investments are in manufacturing and trade, and over half are in Ontario

C. Investment Abroad By Canadians

- there has been a growing participation by Canadians in global investment; while less than 800 firms in Canada in 1970 undertook direct investment abroad, by 1986 (the latest data available) the number had almost doubled to 1,476
- less than 25 firms account for more than 50 per cent of direct investment abroad
- most CDIA concerns majority-owned affiliates; over 70 per cent is in the United States, and intra-industry investment is increasingly important

D. Canada's Net Investment Position

- since 1985, Canada has been a significant net importer of foreign direct investment

Part A: The Globalization of Markets

The "Globalization" of Markets

"Globalization" refers to the integration of markets on a global scale - to the growing interdependence of consumers, producers, suppliers and governments in different countries.

Illustrations of Globalization:

- more rapid growth in world trade and foreign direct investment than world output;
- increased openness of major economies;
- growing importance of regional trading blocs and intracorporate trade;
- distinction between traded and non-traded sectors is becoming less clear; services are increasingly entering into international trade;
- magnitude and speed of international capital flows;
- industrial rationalization worldwide and extensive reorganization at the firm level;
- international networking and other forms of strategic alliances among firms;
- the growing importance of European and Asian markets;
- heightened degree of international competitiveness and growing importance of knowledge-intensive industries.

Chart #1: Growth In World Trade And Direct Investment Abroad

- globalization, or the growing interdependence of markets and national economies, is the result of many factors - including the expansion of world trade and international investment;

- the growth in world trade and international investment has been more rapid than world output, and national boundaries are less and less important in defining markets;

- the slow growth in world trade in the early 1980s reflects the collapse of commodity prices and the 1981-82 world recession; in volume terms the pace of world trade has been much more vigorous than the chart would suggest;

- between 1970 and 1986 the value of world exports increased sevenfold and the volume more than tripled;

- the 1986-88 period was one of strong growth in world trade, expanding at more than 17 per cent annually; world merchandise trade expanded by 7.5 per cent in 1989 and its total value topped US$3 trillion for the first time;

- during the 1980s Canada's exports increased by 107 per cent, compared to the world average increase of 86 per cent; Canada moved from tenth to seventh position among the world's top exporters;

- during the past decade international direct investment (which conveys at least some degree of foreign control) has expanded much more rapidly than world trade; since 1986 the flow of foreign direct investment to the United States has more than doubled; the stock of FDI as a percentage of the total net worth of non-financial corporations in the United States increased from 6.3 per cent in 1986 to 8.9 per cent in 1989.

Chart #1

Growth in World Trade and Direct Investment Abroad (DIA)

Source: U.S. Dept. of Commerce & Int. Monetary Fund.

Chart #2: Growth In World Trade Relative To Growth In World Output

- since 1985 the growth in world trade has strongly outpaced the growth in world output;

- the increase in world trade has been accompanied by a change in the distribution of trading activity, in particular a decline in the dominance of the United States;

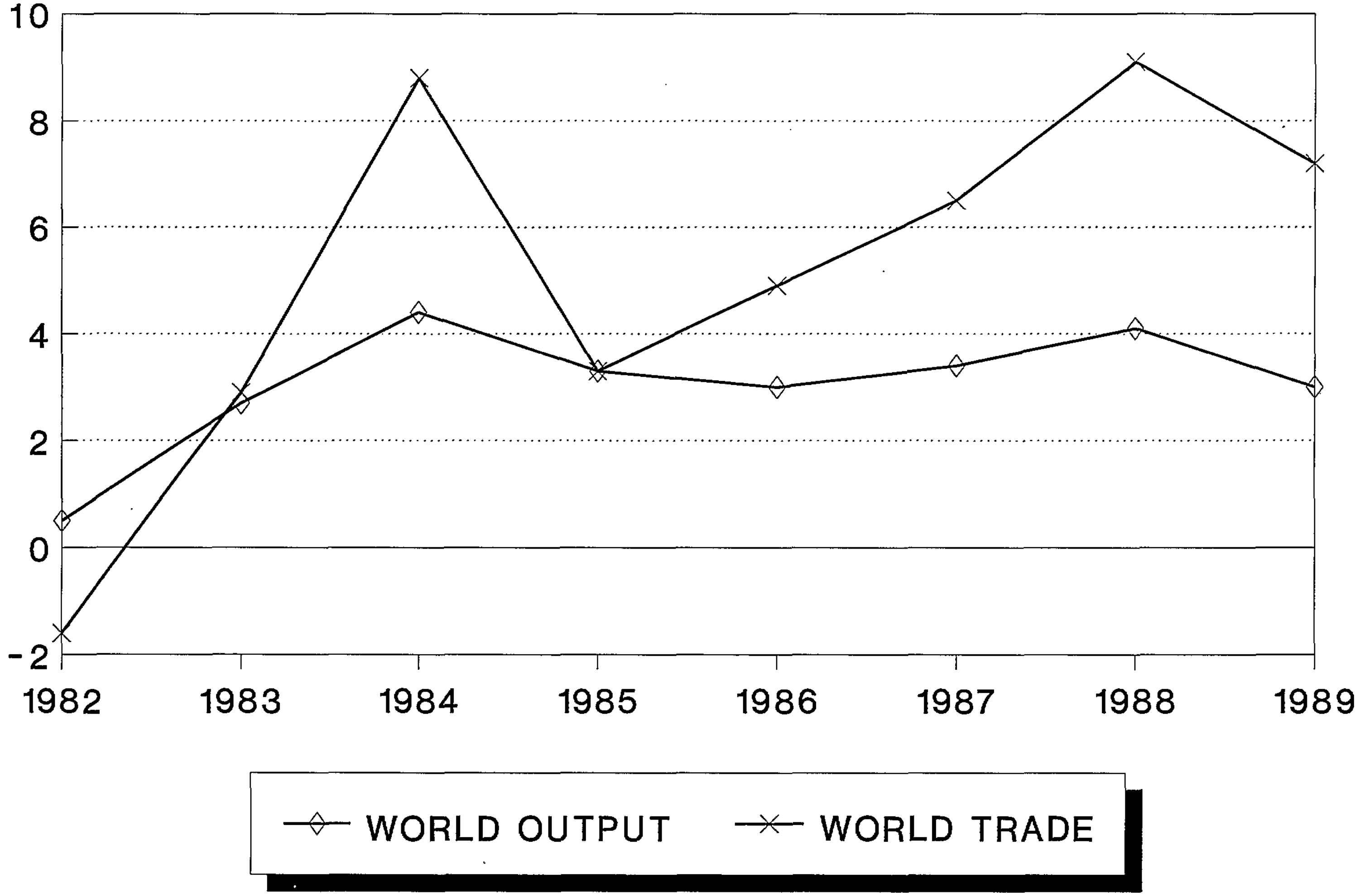
- in 1988 the United States lost its traditional position as the leading world exporter to West Germany (West Germany accounted for 11.4 per cent of world exports whereas the United States accounted for 11.3 per cent);

- Japan's exports have grown much more rapidly than world exports, and even developing countries have increased their share of world trade;

- there is a strong correlation between export growth and growth in gross domestic product; outward-oriented countries have tended to perform much more strongly than protectionist countries.

Chart #2

Growth in World Trade and Output
Annual Percentage Change



Source: World Economic Outlook, IMF

Chart #3: Exports Of Goods And Services As A % Of GDP

- the growth of world trade has resulted in major industrialized countries being much more open;

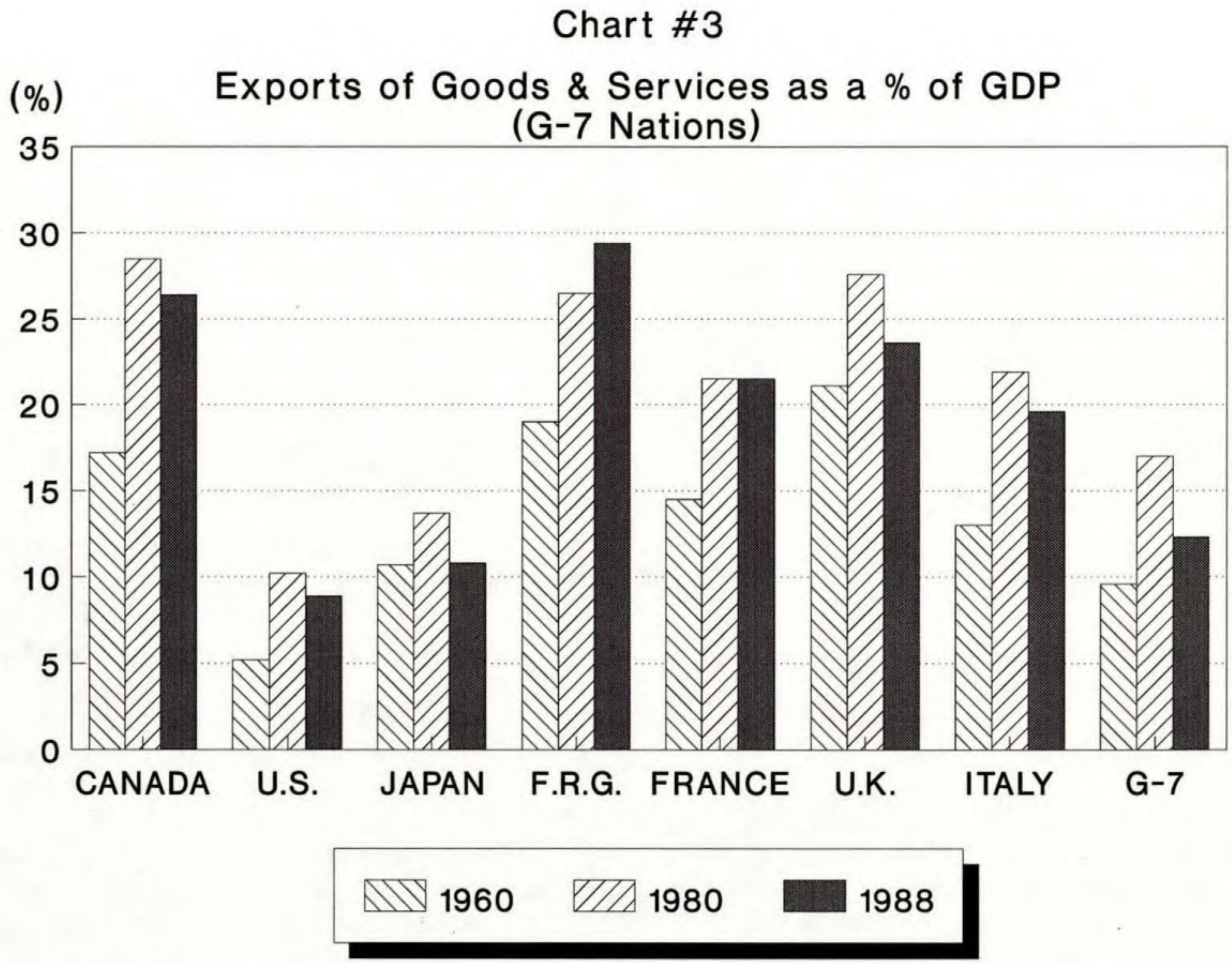
- all G7 countries, with the exception of Japan, have experienced significant increases in exports as a percentage of their gross domestic products; the individual country data are more meaningful than the aggregate G7 data, as the latter reflects U.S. exchange rate changes;

- Canada's degree of openness increased by almost 10 percentage points during the period 1960-88; it has one of the most open economies in the world;

- with the exception of West Germany, the G7 countries experienced some contraction in their degree of openness following the 1981-82 world recession;

- with the implementation of the Canada/U.S. Free Trade Agreement, the developments leading to Europe 1992, the liberalization of Eastern European markets, and the expected progress of the Uruguay GATT Round, there should be a continuation of the long-term trend towards increasing global interdependence;

- since world trade has been growing much more rapidly than world output in recent years, greater interdependence is the result.



Source: O.E.C.D. Economic Outlook

Chart #4: World Trade Flows

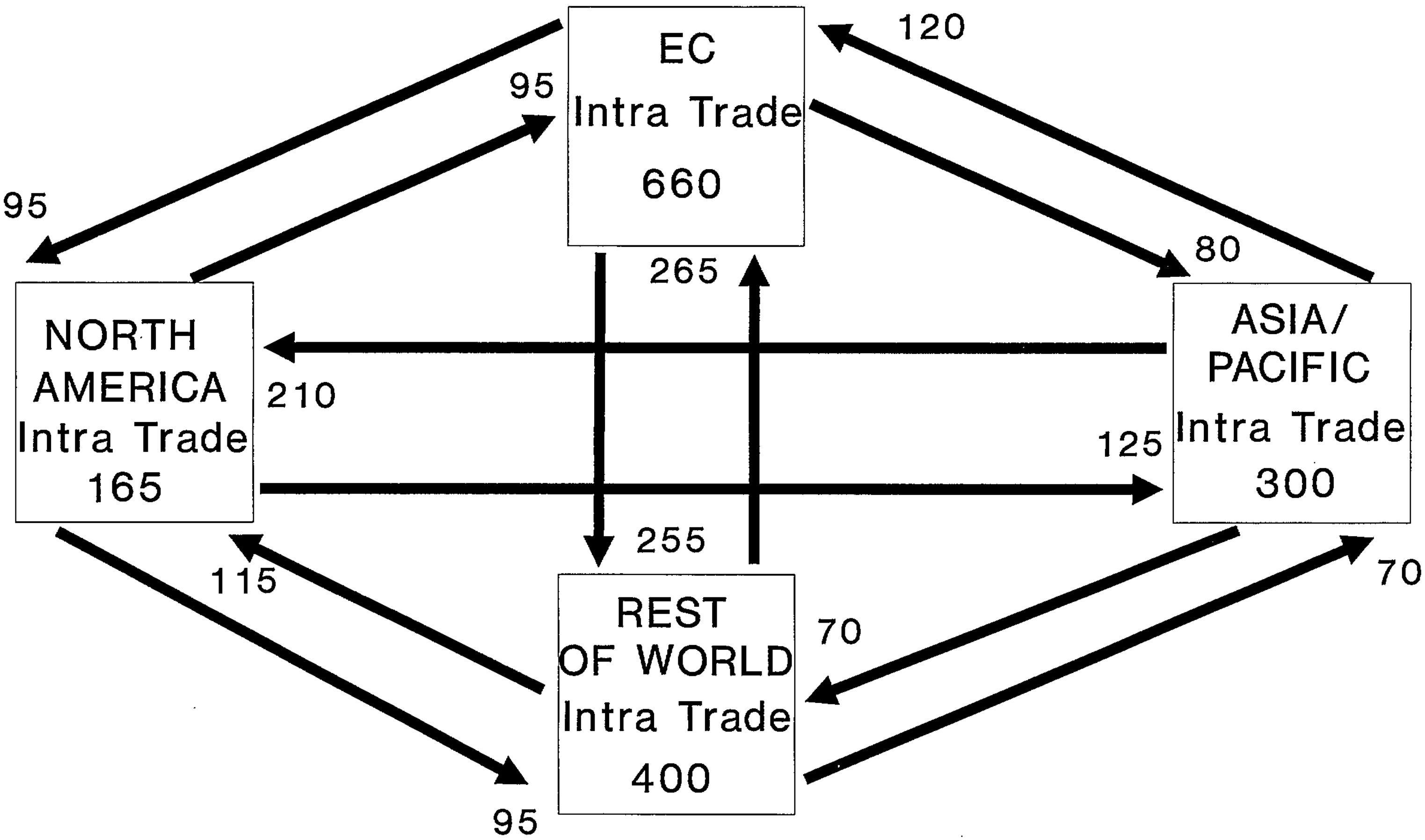
- yet another way of characterizing globalization is the emergence of countries or groups of countries that challenge the trade dominance of the United States;

- clearly, the participation of Asian and European countries in world trade is now much stronger than was the case in the immediate post-war period;

- western commercial ties have been extended to the Asia Pacific region and, with the recent developments in Eastern Europe, world trade promises to be even more diversified;

- the United States is a huge internal market, with some individual states being considerably larger than member countries of the European Community; intra-regional trade in North America is therefore considerably less than recorded in the European Community.

Chart #4
World Trade Flows
1989 (In US$ Billions)



(Figures have been rounded to nearest US$5 Bn.)

Source: GATT, OECD

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Chart #5: The Increasing Importance Of Non-U.S. Markets For Canada

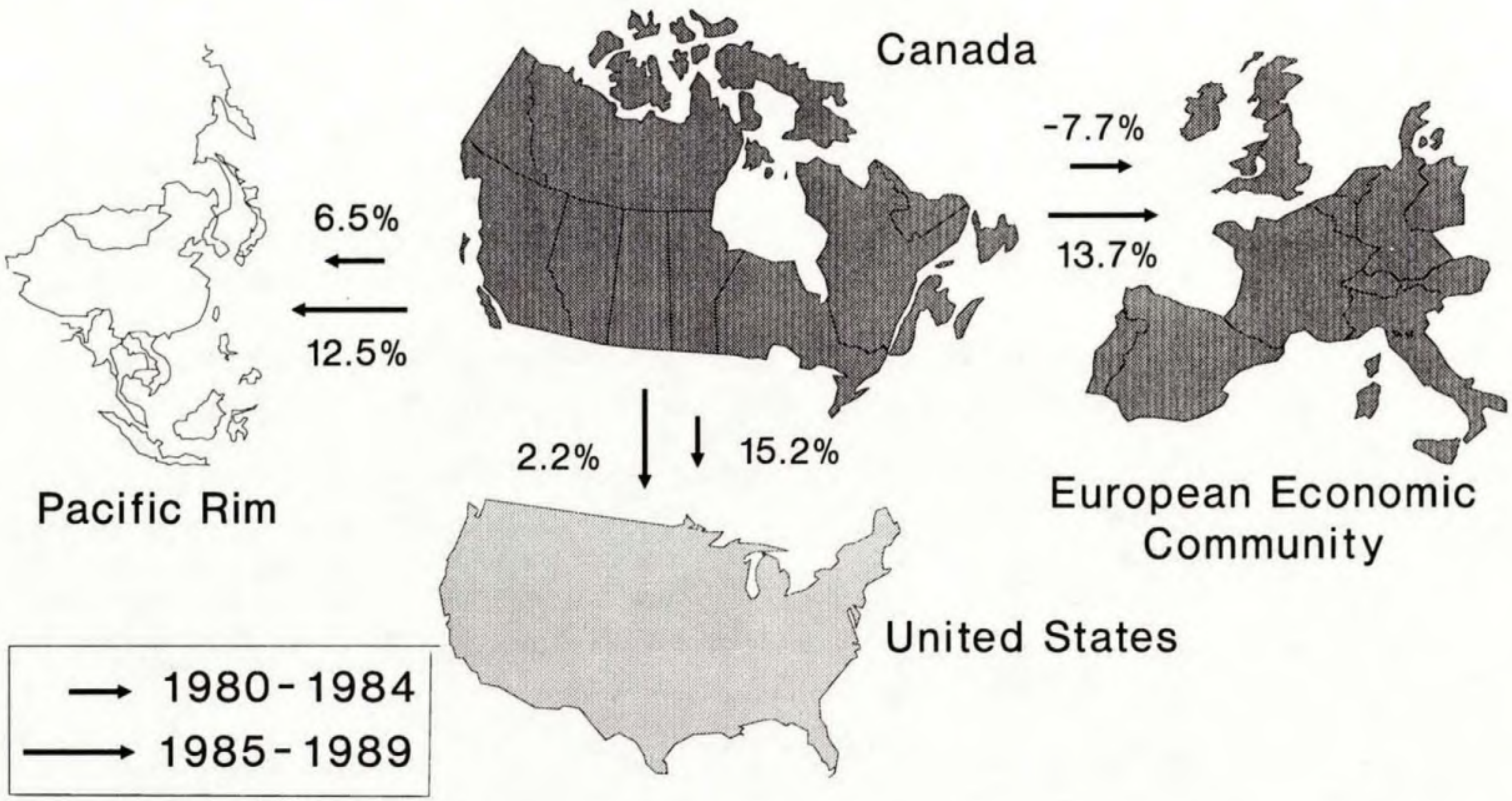
- it is noteworthy that since 1985 Canada's dependence on the U.S. export market has been decreasing; Canadian exports to the EC and to Pacific Rim countries have been growing at double digit rates since 1985, while exports to the United States grew by less than one per cent annually between 1985 and 1987 and by only 3.6 per cent annually between 1987 and 1989;

- in 1985 the United States accounted for 77.9 per cent of Canadian exports whereas in 1989 it accounted for only 73.3 per cent; the European Community now accounts for 8.5 per cent of Canadian exports (up from 5.9 per cent in 1985) and Pacific Rim accounts for 11.9 per cent (up from 8.6 per cent); this declining dependence on the U.S. market for Canadian exports contrasts with the growing dependence during the first half of the 1980s;

- because the United States currently accounts for 73% of Canada's exports, it will continue to offer the greatest absolute dollar increase in export opportunities for Canada, even though the growth is sluggish compared to overseas market.

Chart #5

The Increasing Importance of Non-U.S. Markets for Canada
Average Annual Export Growth



Source: Statistics Canada

Chart #6: Trade Among Regional Blocs

- potentially slowing the process of globalization, but also acting as a stimulant in many ways, has been the growing importance of regional trading blocs - most notably in North America and Western Europe;

- as is evident from the chart, the sum of intra-regional trade is much greater than trade between these blocs; of particular significance is the enormous degree of intra-regional trade among Western European countries;

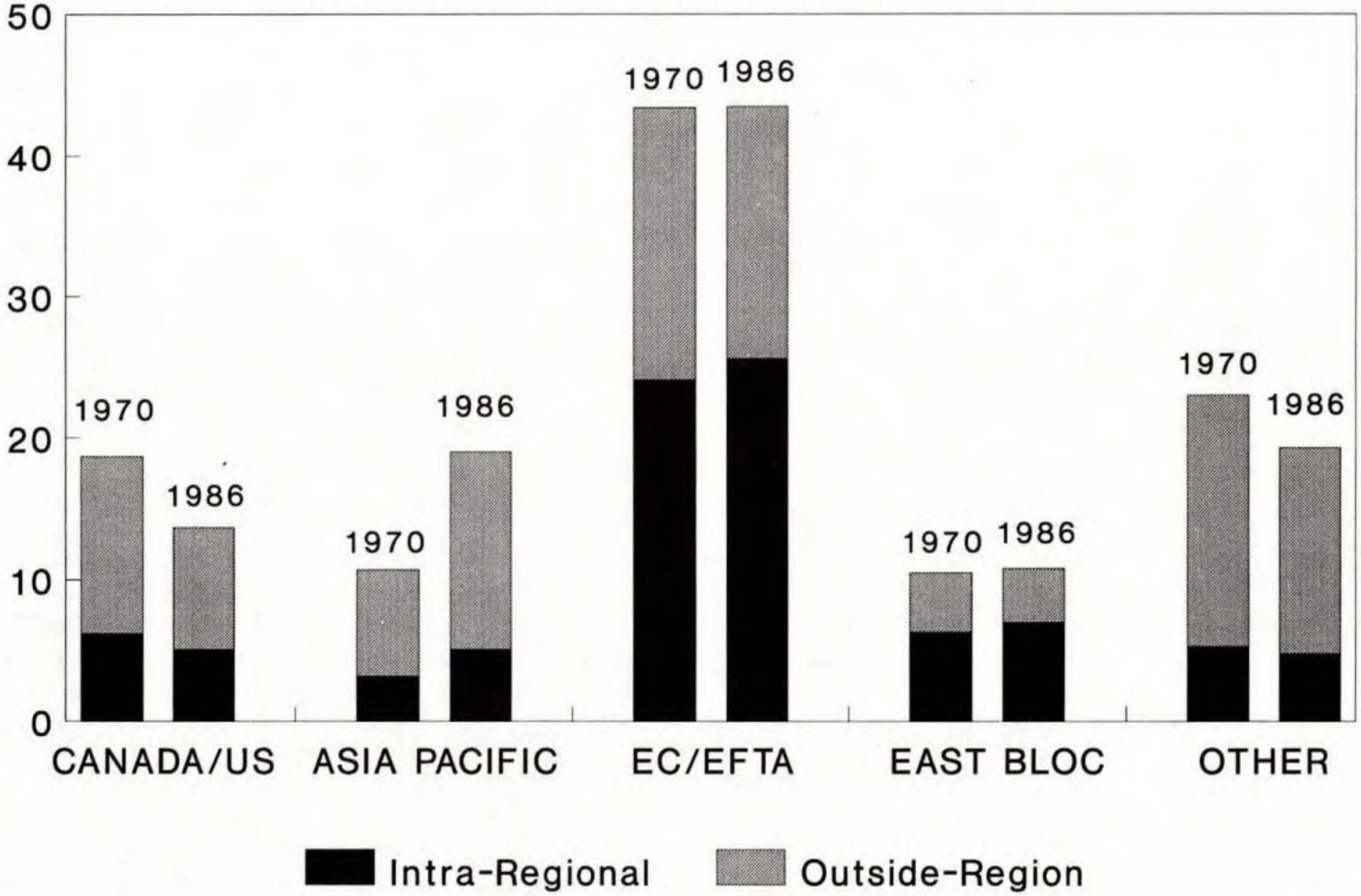
- in the case of both North America and Western Europe, the importance of intra-regional trade has grown in importance over the 1970 to 1986 period; this trend is expected to continue and may intensify with the advent of Europe 1992 and the possibility of a North American Free Trade Agreement (to include Mexico);

- in the case of the Asia Pacific region, intra-regional trade has grown less rapidly than the region's total trade; nonetheless, in terms of world trade, intra-regional Asia Pacific trade is growing in importance;

- extensive investment by Japan in ASEAN countries (Indonesia, Malaysia, Brunei, Thailand, Singapore and the Philippines), together with greatly increased development assistance, is resulting in the evolution of an East Asia trading area; intra-corporate trade is rapidly expanding;

- participants in the Asia Pacific Economic Co-operation ministerial meetings, which includes Australia, New Zealand, Japan, the ASEAN countries, South Korea, the United States and Canada, are endeavouring to formalize various aspects of their trade and investment interrelationships.

Chart #6
Trade Among Regional Blocs
Percent of World Merchandise Exports



Source: C.D. Howe Institute

Chart #7: The Growing Importance Of Intra-Corporate Trade

- another feature of globalization has been extensive industrial restructuring, including the growing preference for vertical integration; as shown later in this report, international merger and acquisition activity has been very strong during the past decade;

- consequently, intra-corporate trade now accounts for a very significant share of total world trade; some one-third of world trade in manufactured goods is estimated to be intra-company trade;

- to illustrate the importance of intra-corporate trade, the accompanying chart shows the degree of such trade between U.S. parent companies and their majority-owned foreign affiliates; in the first bar graph, affiliated exports are expressed as a percentage of total exports to the country or region in question; in the case of U.S. exports to Canada, nearly half of total exports are attributable to intra-corporate trade;

- the vast majority of U.S. intra-corporate exports is accounted for by the "big three" U.S. automobile manufacturers; the Automotive Products Trade Agreement of 1965 facilitated the large amount of affiliated exports in that sector;

- the second bar graph shows the degree to which intra-corporate trade among U.S. majority-owned affiliates accounts for U.S. imports; from the graph it is evident that intra-corporate trade accounts for more than a third of U.S. imports from Canada; most of this is in respect to the manufacturing of transportation equipment;

- in the case of trade between the U.S. and other countries (excluding Canada), intra-corporate trade accounts for more than 30 per cent of U.S. exports to the European Community and for 15 per cent of U.S. exports to ASIAN NICs; only in the case of Japan is such trade relatively limited; this reflects the relatively low level of U.S. direct investment in Japan; intra-corporate export trade with Japan is, however, growing rapidly, especially in the areas of chemicals, non-electrical machinery manufacturing and wholesale trade;

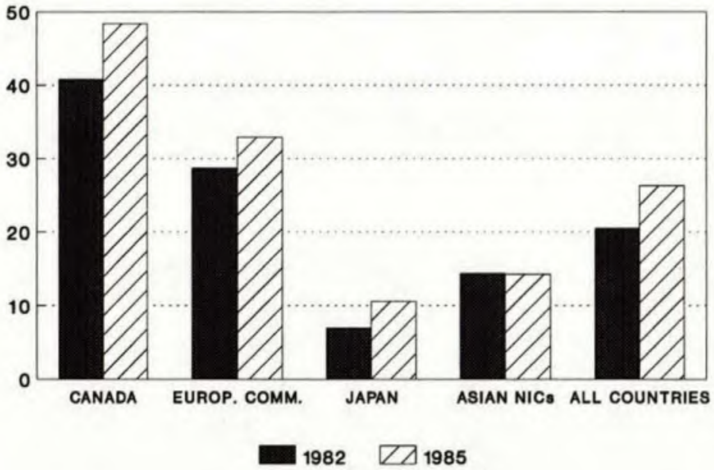
- data on intra-corporate trade between minority-owned foreign affiliates is scarce but this form of trade is also significant.

Chart #7

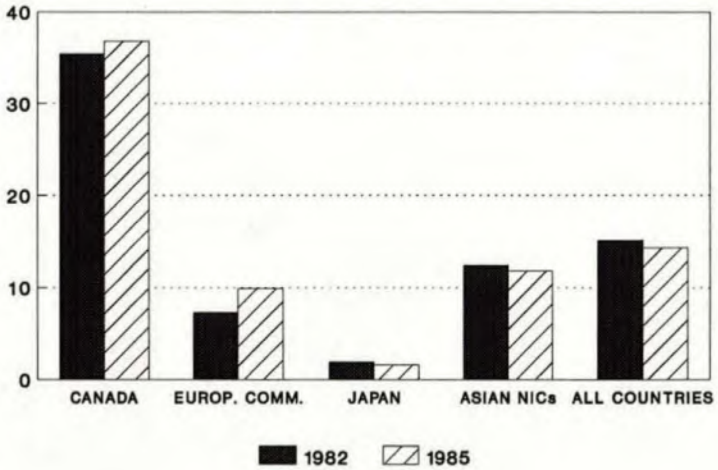
U.S. Merchandise Trade Between U.S. Parent Companies and Majority-Owned Foreign Affiliates as a Proportion of Total U.S. Merchandise Trade

(Percent Share)

Affiliated Exports



Affiliated Imports



Source: U.S. Department of Commerce

Chart #8: Trade And Investment In Services

- until recently it has been common to make a distinction between the traded and non-traded sectors, with most services falling into the latter category; this distinction is becoming less and less relevant, as more and more services are traded internationally;

- among G7 countries, trade in services accounts for more than 20 per cent of total trade;

- the growing inclusion of services in world trade is of major significance, given the dominant role in output and employment played by the service sector in industrialized countries;

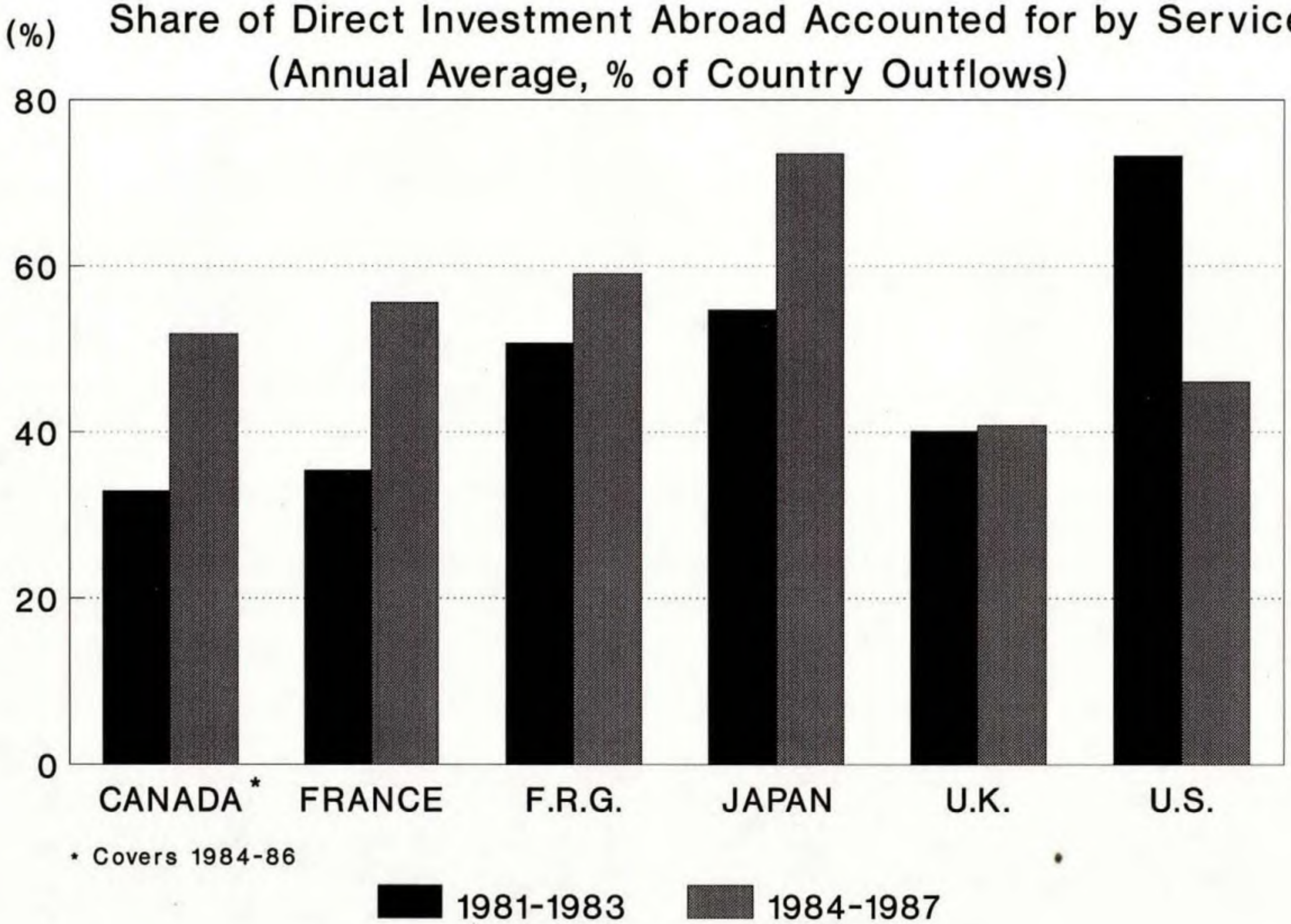
- trade in services accounted for 23 per cent of U.S. exports in 1987, compared to 20 per cent in 1975; Canada, by contrast, continues to have only a low share (10 per cent) of its exports accounted for by services;

- as shown in the accompanying chart, the lion's share of foreign direct investment concerns the service sector;

- the chart shows that for Canada, France, West Germany and Japan an increasing proportion of foreign direct investment has been in the service sector; for the United States, the share of manufacturing in total foreign direct investment outflows has increased, particularly to the European Community.

Chart #8

Share of Direct Investment Abroad Accounted for by Services
(Annual Average, % of Country Outflows)



Source: United Nations Centre on Transnational Corp.,
Based on National Data

Chart #9: International Capital Flows

- the liberalization of international capital markets lagged considerably behind the progressive liberalization of trade in goods and services; since 1974, however, there has been an explosion in international capital flows;

- while individual trade among Triad countries amounts to some $600 billion annually, foreign exchange transactions amount to some $600 billion daily;

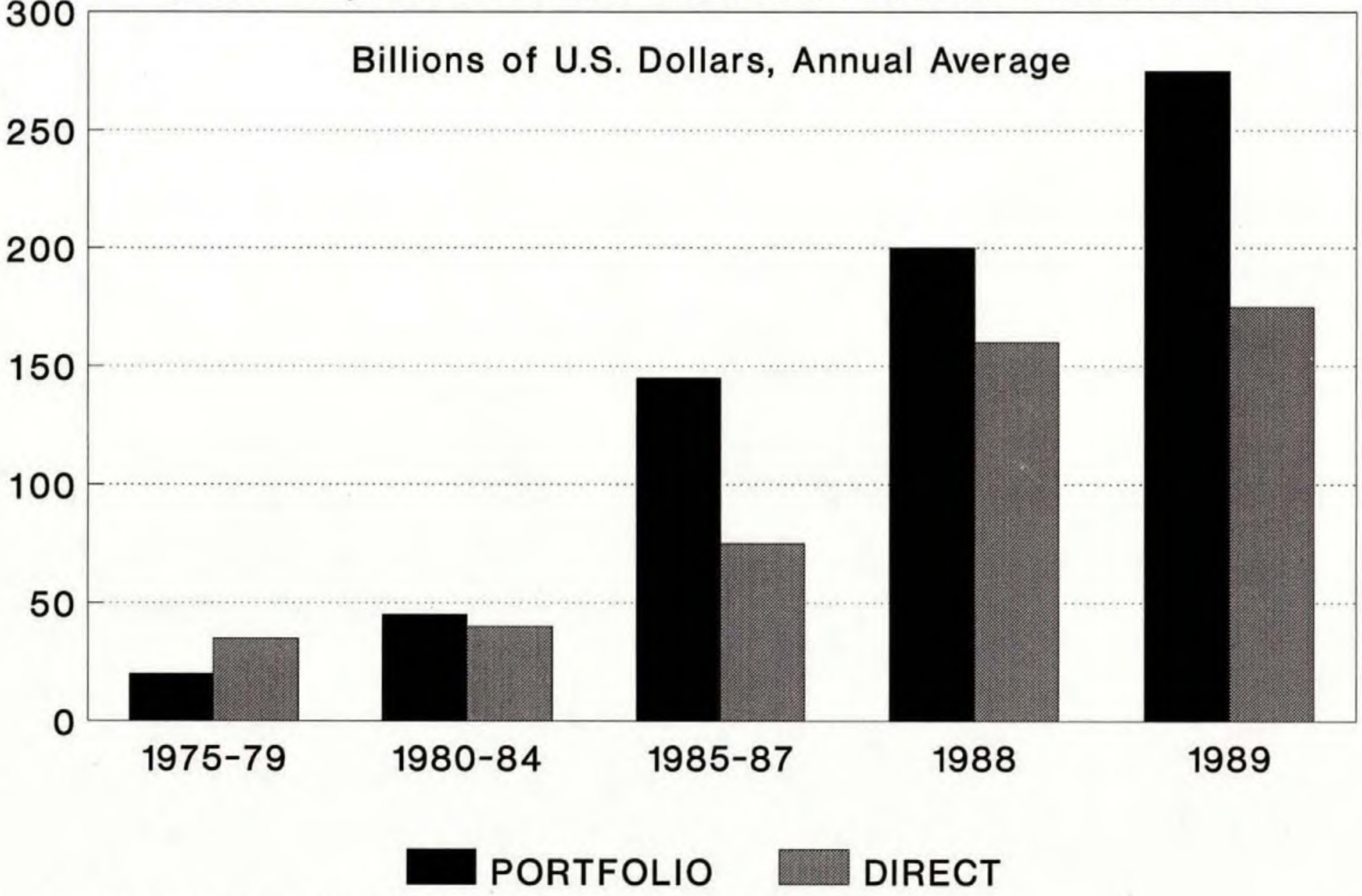
- deregulation in the United States (e.g. to allow bank-intermediated recycling of OPEC's huge surpluses), the floating of dollar exchange rates, technological advance, investor and borrower interest in diversification, Japan's financial maturation, and Europe's push toward Economic and Monetary Union have all contributed toward a second "wave" of globalization;

- while the integration of capital markets will contribute to global economic efficiency, it also carries the risk - unless monitored and managed carefully - of exacerbating the degree of global instability;

- of particular note in this latter regard is the extraordinary growth in portfolio investment; portfolio investment is predominately in bonds, and it is largely driven by a desire for high but secure yields; portfolio investment, as distinct from direct investment, is defined as meaning no significant control or corporate ownership is conveyed to the investor - even if the investment is in equity assets; the general rule is that the investment is classified as portfolio investment if equity ownership is limited to 10 per cent or less of the voting shares;

- from the chart it is clear that world portfolio investment has grown much more rapidly than direct investment.

Chart #9
Private International Investment
Gross Capital Outflows from Industrialized Countries.



G-10 plus Australia, Spain and Switzerland.

Source: BIS

Chart #10: World's Stock Of Direct Investment Abroad - Distribution By Major Source Countries

- direct investment conveys ownership and control participation, and it is this form of investment that is a growing complement to trade; direct investment facilitates access to markets, technology transfer, economies in research and development, the most productive use of human and capital resources, enhancement of the tax base and other benefits;

- the accompanying chart indicates the percentage shares held by major countries of the world stock of direct investment abroad (which totalled U.S.$1 trillion in 1987); for example, in 1987 U.S. investors accounted for 31.5 per cent of the world's stock of direct investment abroad; this contrasts to the 50 per cent share the U.S. had in 1967;

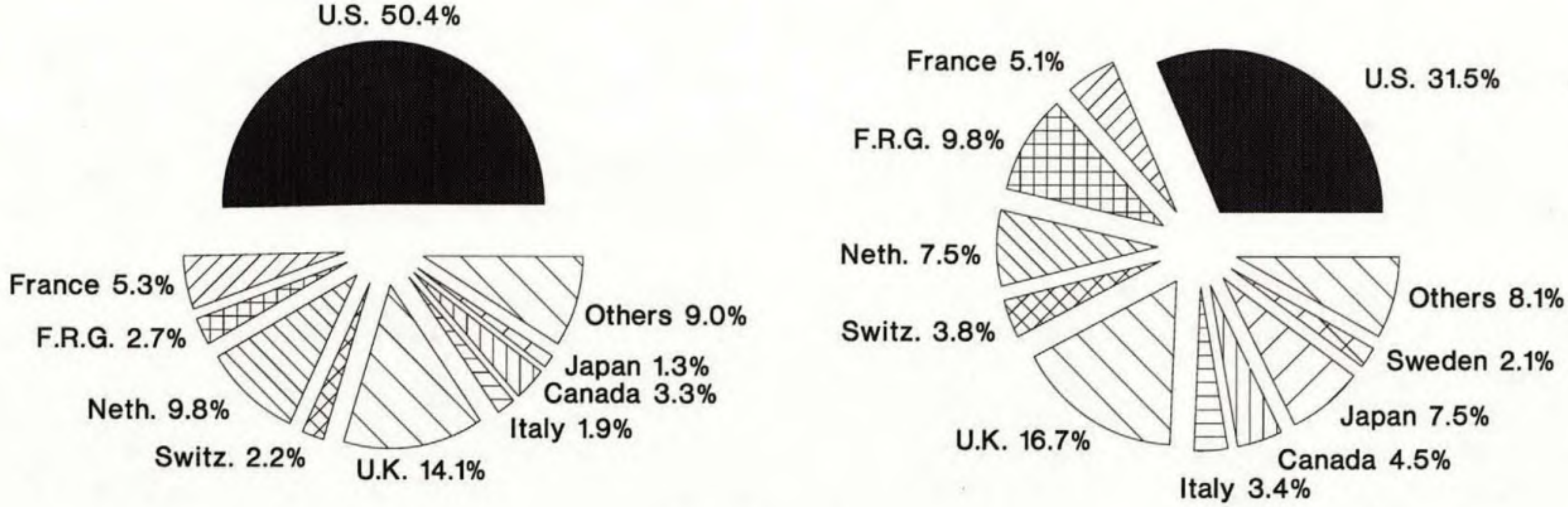
- Japan and West Germany have become major economic players; West Germany accounted for almost 10 per cent of the world stock of direct investment abroad in 1987, while Japan accounted for 7.5 per cent of the total;

- Canada's participation has also increased from 3.3 per cent in 1967 to 4.5 per cent in 1987;

- a much more balanced participation among western industrialized countries is emerging; the former dominance of the United States has ended, and Western Europe and Eastern Asia are more equal partners in the TRIAD.

Chart #10

World's Stock of Direct Investment Abroad
Distribution by Major Source Countries



1967 Total = US$ 112.3 Billion

1987 Total = US$ 1.0 Trillion

Source: U.S. Department of Commerce

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Chart #11: World Flows Of Outward Direct Investment

- world flows of direct investment are much more volatile than the world stock; the country distribution of the latter changes slowly over time, reflecting the protracted period it took to build the stock; flows, on the other hand, reflect savings rates, fiscal deficits (or surpluses) and current account balances; these underlying factors may change very rapidly and, if sustained, may lead to a significant alternation in the size and distribution of the world stock of direct investment abroad;

- the accompanying chart shows that the country source for direct investment flows has changed much more dramatically than the world stock;

- whereas during the 1971-80 period the United States accounted for 44 per cent of world cross-boundary direct investment flows, during the 1981-88 period it accounted for only 22 per cent of these flows;

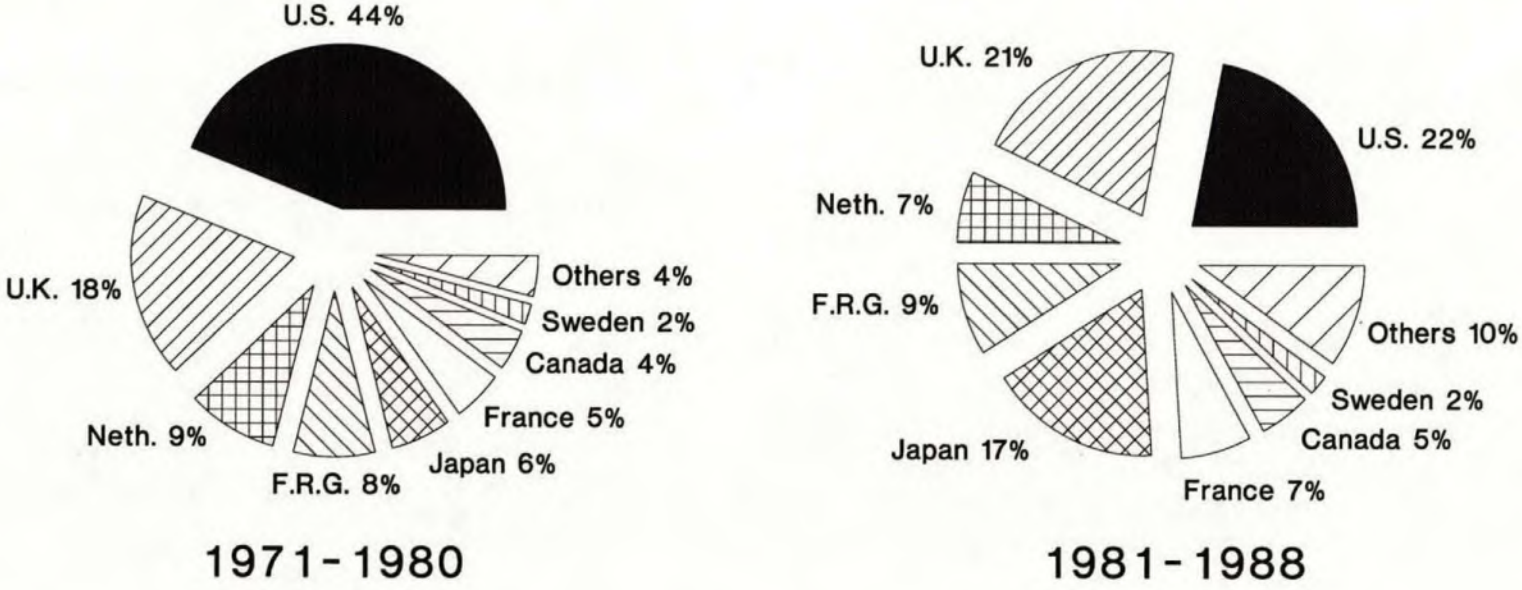
- the United Kingdom was almost an equal player to the United States during the 1980s; this appears to reflect industrial restructuring which, because of relative market sizes, is more easily internalized in the U.S. economy than is the case for other G7 countries;

- the most dramatic change has been in respect to Japan; whereas it accounted for 6 per cent of world cross-boundary direct investment flows during the 1971-80 period, during the 1981-88 period it accounted for 17 per cent of the flows; more recent data will no doubt show that Japan's position has continued to climb;

- Canada's percentage contribution has grown by 25 per cent and it ranks closely with France.

Chart #11

Share of Outward Direct Investment Flows
Major O.E.C.D. Countries



(Cumulative Direct Investment Flows)

Source: Department of Economics & Statistics, O.E.C.D.

Chart #12: World Stock Of Inward Direct Investment

- the previous two charts were from the perspective of the home country; that is, each country's contribution to foreign investment;

- the accompanying chart presents investment data from the perspective of the host country; that is, the share of the world stock of direct investment absorbed by each country;

- clearly, there have been some dramatic investment developments over the past two decades;

- whereas in 1967 the United States absorbed less than 10 per cent of world direct investment, in 1987 it absorbed 25 per cent of the total; West Germany's share also more than doubled, from 3.4 per cent to 8 per cent; France experienced an increase (from 2.8 per cent to 3.9 per cent) in its share of the world total while Japan's share remained largely unchanged at less than 1 per cent;

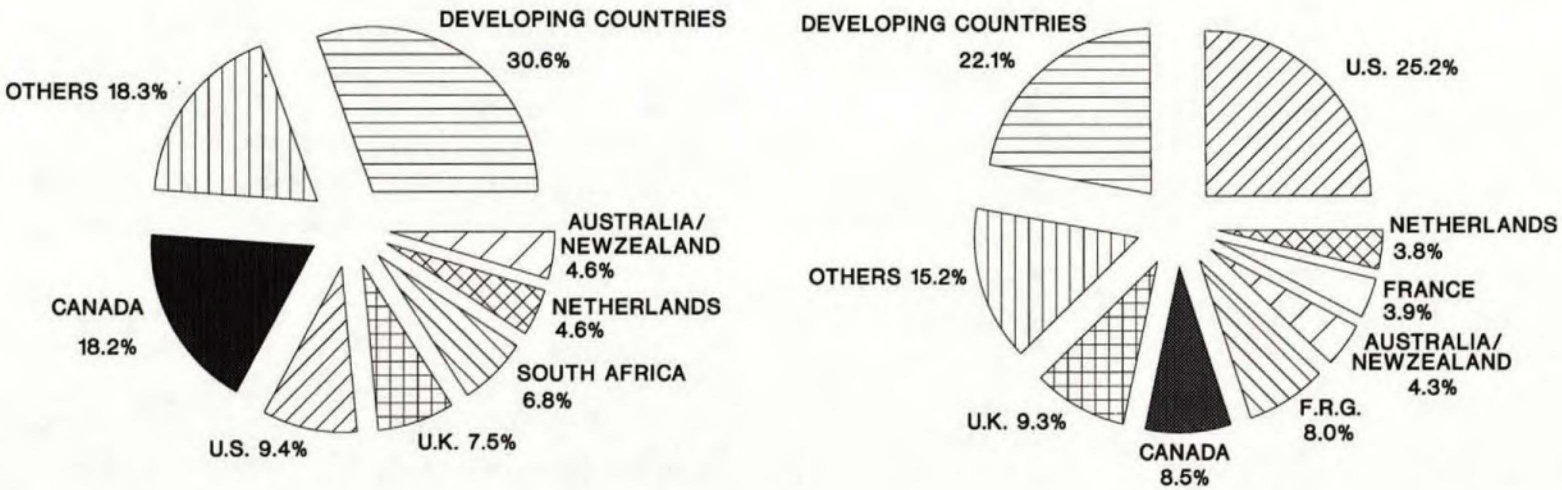
- developing countries as a group experienced a significant drop in their share of the total (from 30.6 per cent in 1967 to 22.1 per cent in 1987);

- apart from South Africa, however, the most significant individual drop of any country was experienced by Canada; its share dropped from 18.2 per cent to 8.5 per cent; while some may interpret this drop as worrisome, it simply reflects the fact that Canada had an unusually large share in 1967; apart from whether it would have been desirable to sustain this share, the stock of world direct investment abroad has grown so enormously it is only to be expected that Canada's share would fall sharply; had it not fallen, the stock of foreign investment in Canada would be double current levels, as would the degree of foreign control and ownership; also, the decline may be overstated due to the fact that the "old" FDI fails to reflect current book values (a large share of Canada's FDI dates back many years);

- comparing Charts 11 and 12, it is apparent that the relationship between outward and inward investment has become much more balanced in several important instances (e.g. the United States, Canada and West Germany); the one important exception to this observation is Japan.

Chart #12

World Stock of Inward Direct Investment
Distribution by Major Host Countries/Regions



1967 Total = US$ 105.5 Billion

1987 Total = US$1.1 Trillion

Source: U.S. Department of Commerce

Chart #13: Merger And Acquisition Activity In Selected Countries

- the increase in foreign investment and the shifts in the flows reflect, among other factors, the growing rationalization of industries on a worldwide scale;

- this chart shows merger and acquisition activity in recent years in six of the G7 countries;

- due to difficulties in data comparison among countries, it is not possible to show the long-term trends; nonetheless, the chart does indicate the substantial number of mergers and acquisitions in Canada, the United States and the U.K. in both 1987 and 1988;

- the number of mergers and acquisitions in Canada relative to the number in the United States during the 1987-88 period was approximately 1 to 3, rather than the approximate 1 to 10 ratio that applies for many economic indicators; without more information about the size and dollar amounts of these mergers and acquisitions, however, it is difficult to draw inferences about the level of activity in Canada relative to other countries;

- data for 1989 show a considerable slowdown in merger and acquisition activity in the United States, in part because of the collapse of junk bonds and the growing concerns about debt/equity ratios;

- data for the first nine months of 1990 indicate that merger and acquisition activity has continued to fall; worldwide, there were 5,908 deals announced in the first nine months of 1990, down from 6,677 in the comparable period in 1989; the value of merger and acquisition activity fell 42 per cent, from $550 billion to $317 billion; the drop-off in activity has been most pronounced in the United States, where the value of merger and acquisition activity has fallen by 55 per cent;

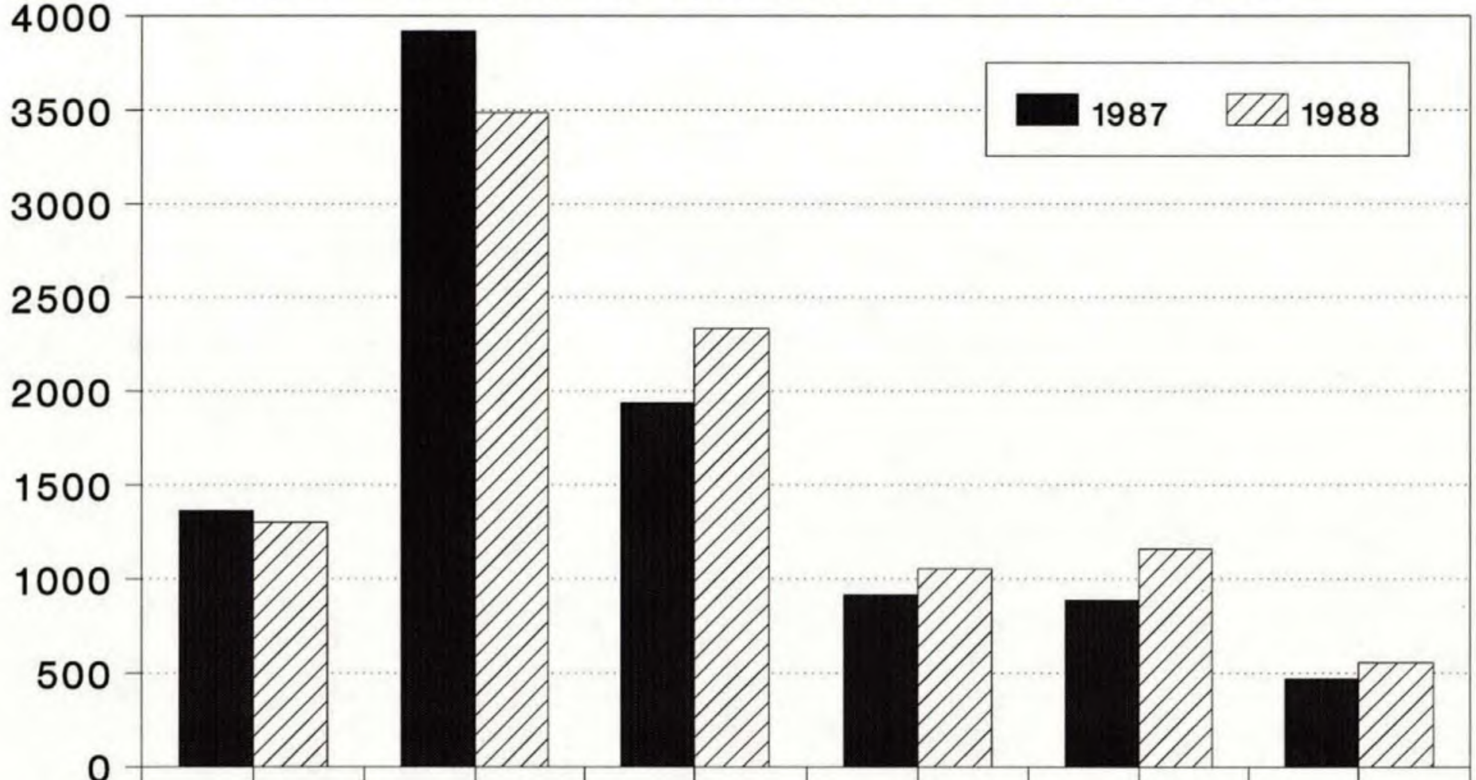
- merger and acquisition activity in the European Community and EFTA countries, in contrast, has intensified - albeit from a very low level; cross-border deals involving European companies more than doubled in the first nine months of 1990, rising to $37 billion from $18 billion a year earlier; large intra-European cross-border mergers and acquisitions reflect Europe's 1992 unification;

- Japan's manufacturing and financial sectors are already highly integrated, hence merger and acquisition activity may remain at a low level; also, foreign takeovers are rare because of institutional factors that tend to discourage outside participation in the Japanese economy.

Chart #13

\# of Cases

Merger & Acquisition Activity in Selected Countries



	Canada	U.S.	U.K.	France	Germany	Japan
1987	1363	3920	1937	915	887	469
1988	1301	3487	2332	1053	1159	555

Source: Mergers & Acquisitions, July/Aug., 1989

Chart #14: Merger And Acquisition Activity In Canada

- merger and acquisition activity in Canada in recent years has been almost double the level in 1985;

- merger and acquisition activity in 1989 totalled $30 billion, up significantly from the level in 1988; foreign acquisitions accounted for $14 billion of the total but it is important to note that a high percentage (roughly 50 per cent) involved takeovers of Canadian-based but already foreign-owned firms;

- mergers and acquisitions in 1989 were characterized by a relatively high incidence of large transactions, including the following:

Acquirer	*Acquired Co.*	*Value ($M)*
Imperial Oil Ltd.	Texaco Canada	4,929
Stone Container Corp.	Consolidated-Bathurst	2,604
Noranda & Trelleberg AB	Falconbridge	2,129
Socanav & Caisse de Dépôt	Steinberg Inc.	1,330
BCE Inc.	Montreal Trust Inc.	857

- consistent with the worldwide drop noted earlier, the number of mergers and acquisitions in Canada in the first nine months of 1990 dropped sharply - by 24 per cent when compared to the number in the first nine months of 1989; in value terms, the drop was even more significant - 43 per cent;

- the sharp decline in value suggests that while corporations continued to restructure through strategic acquisitions and divestitures, there was a relative absence of large transactions;

- it is important to note that restructuring of the private sector in Quebec has evolved somewhat differently than in the rest of Canada; "Quebec Inc." refers to the goal of fostering large corporations linking financial and commercial interests, designed to keep ownership and head offices of key commercial enterprises in Quebec; Caisse de dépôt, the Mouvement Desjardins and other financial agents are participating closely with the Quebec business interests in this endeavour.

Chart #14

Merger & Acquisition Activity in Canada
1986-1989

Source: Mergers and Acquisitions in Canada, 1990

Chart #15: International Networking And Other Forms Of Strategic Alliances

- while mergers and acquisitions are the most visible evidence of industrial rationalization on a world-wide scale, there are many other forms of globalization;

- international networking has greatly intensified in high-technology sectors, in part to help defray the sky-rocketing costs of research and development;

- this chart provides an example of the extraordinary degree of networking and strategic alliances in high-technology sectors;

- Northern Telecom has extensive linkages with other firms in Europe, Asia, the United States and South America;

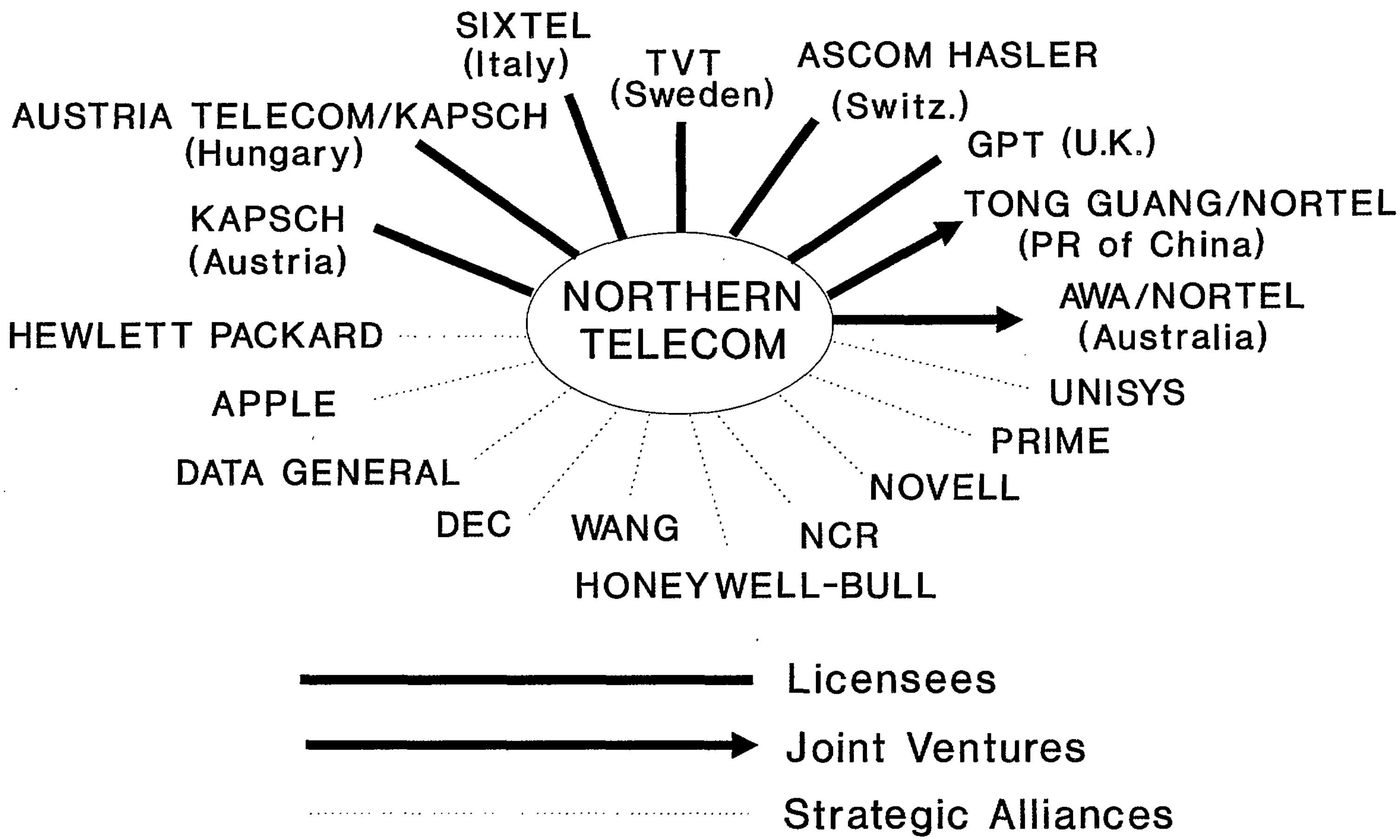
- the chart indicates Northern Telecom's licensees with firms in Europe, its joint ventures with firms in Australia and China, and its strategic alliances with 9 firms in the United States;

- according to a study of Canadian joint ventures (Michael J. Geringer, Trends and Traits of Canadian Joint Ventures, prepared for Investment Canada, February 1990), it was found that, compared to the United States, Canada has a high number of joint ventures per capita and their survival rate is high;

- corporations are striving to organize themselves in ways which will enable them to plan globally but still serve local markets effectively; there is considerable experimentation with alternative corporate structures, with much less emphasis on the traditional multinational structure.

Chart #15

An Illustration of International Networking
and Other Forms of Strategic Alliances



Source: Northern Telecom

Chart #16: Types of Business Structures

- in order to participate in international markets, four types of business structures have evolved over the post-war period; three of these represent traditional formations as firms outgrow their domestic boundaries; the last is a structure which appropriates the best characteristics of each of the others to evolve into a modern transnational organization;

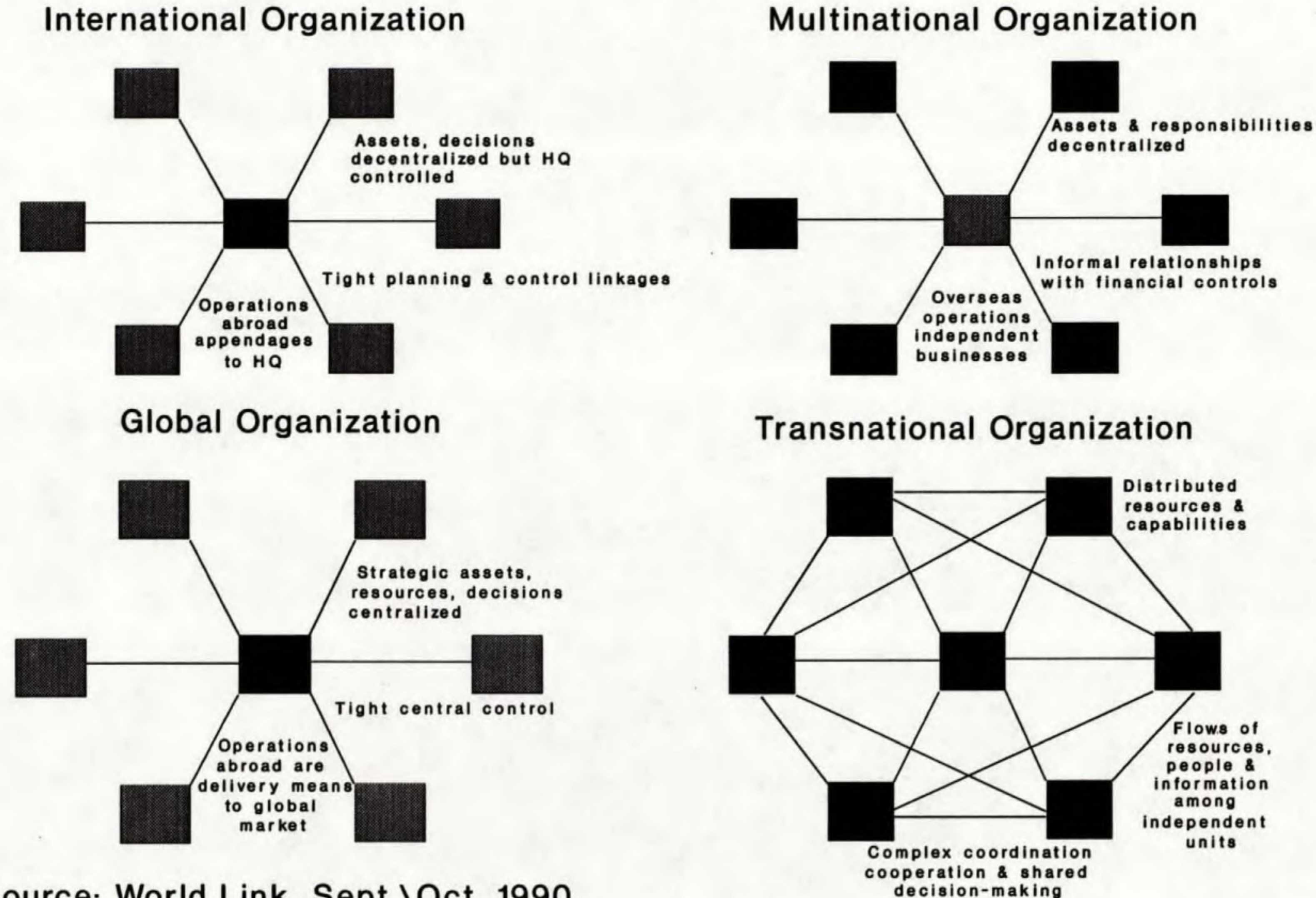
- the International Organization emphasizes professional management and the transfer of domestically-generated expertise to subsidiaries and affiliates abroad; central control is highly concentrated;

- the Multinational Organization developed as firms expanded into colonial markets; while there is scope for independent managers to be responsive to local differences, the basic configuration is that of a decentralized federation; there is little incentive to take advantage of scale operations;

- the Global Organization is a "wheel and spoke" design, based on close management teams built around a central hub; it is globally-integrated and based on economies of scale with all affiliates parts of a single integrated strategic unit; control is centralized;

- the Transnational Organization is a progression of the three other structures; it reacts to both local and global stimuli in an integrated network; subsidiaries are independent strategic assets, acting as outposts as well as sources of technology and skills; this type of organization has the combined positive characteristics of the other three forms.

Chart #16
Types of Business Structures



Source: World Link, Sept.\Oct. 1990.

Part B: International Investment In Canada

Important Changes Concerning International Investment In Canada

Major changes include:

- the steep decline in foreign control between 1971-1985, followed by a slight increase;
- the considerable increase in foreign direct investment in recent years;
- the growing importance of foreign capital inflows relative to reinvested earnings;
- the increasing share of foreign direct investment for acquisitions as compared to new businesses or business expansions;
- the declining importance of the United States relative to Asia and Europe as sources of foreign direct investment for Canada;
- the increasing importance of portfolio investment relative to foreign direct investment;
- according to Investment Canada data on acquisitions and new businesses (the latter tend to be underreported), a third of the total number of foreign investments in Canada over the past five years has been in the manufacturing sector; relatively few foreign investments have been in the resource sectors;
- again according to Investment Canada data, 60 per cent of all foreign investments since 1985 have been in Ontario; in value terms Ontario's share has been slightly less than 50 per cent and Quebec's share has been slightly more than 18 per cent.

Chart #17: Foreign Control of Corporate Assets In Canada

- the relative importance of foreign direct investment diminished considerably during the period 1971-85;

- according to data collected under the Corporations and Labour Unions Returns Act (CALURA), foreign control of non-financial assets in Canada declined from a peak of 37 per cent in 1971 to just under 24 per cent in 1985 and 1986; the most recent CALURA report gives data for 1987 and, for the first time, a new data series (extended back to 1983) for all industries including the financial sector; 1987 data indicate a slight increase in foreign control;

- a corporation is considered to be majority foreign-controlled if 50 per cent or more of its voting rights is known to be held outside of Canada or if a share of this magnitude is held by one or more Canadian resident corporations that are themselves foreign-controlled; in cases where the ownership of voting rights is insufficient to assign control, research is undertaken to determine if options, interlocking directorships or key privately-held shares exist that confer effective (or de facto) control; in 90 per cent of the cases control is assigned on the basis of majority voting rights;

- several factors, including Canadian acquisitions, government policy and Canadian corporate growth, have acted to diminish the relative importance of foreign control of Canadian corporations; this decline began well before the establishment of the Foreign Investment Review Agency and the National Energy Program;

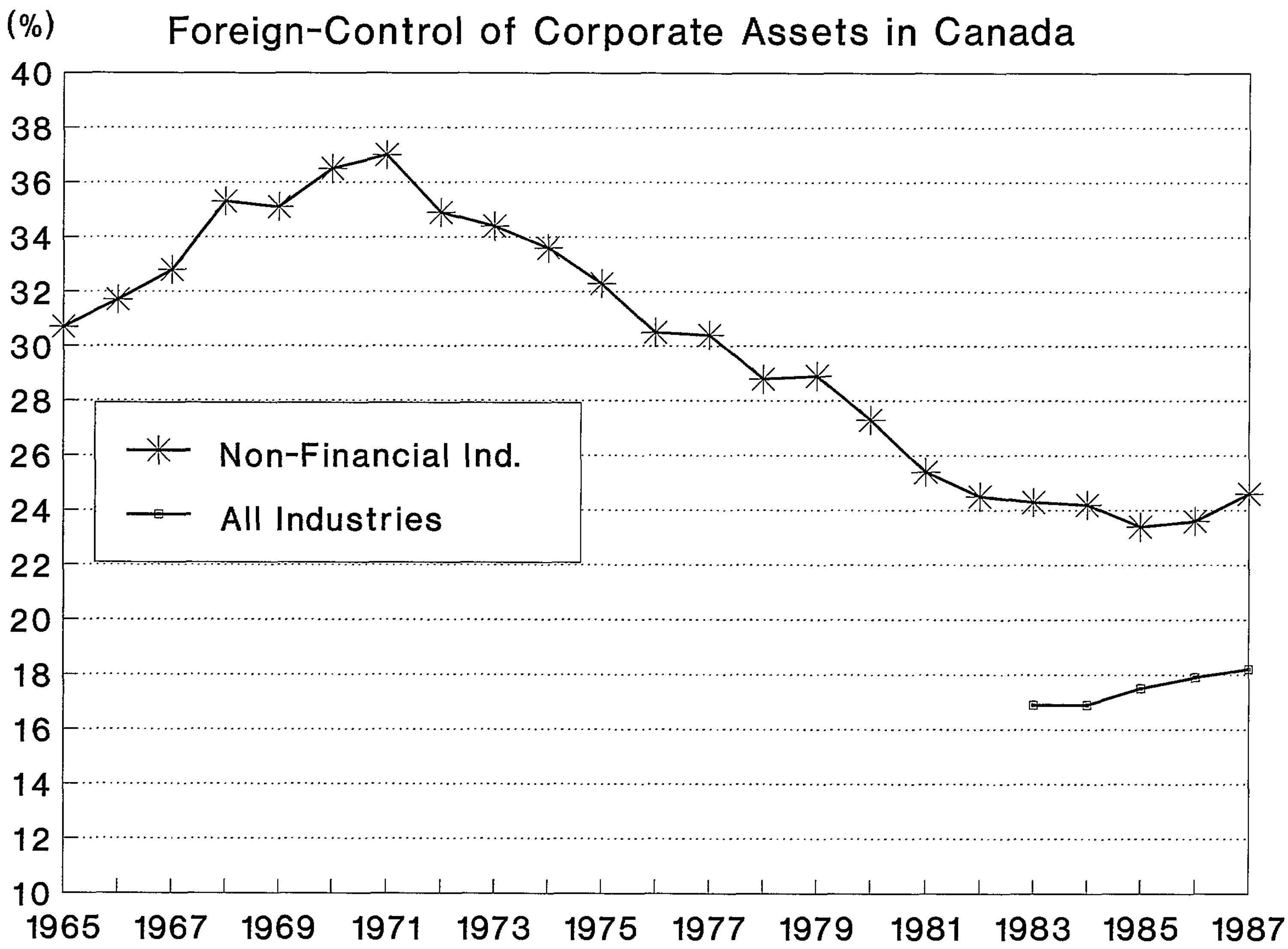
- the decline in foreign control was due to a decline in control by U.S. investors - by 0.8 per cent annually between 1971-81 and by 0.4 per cent annually between 1982-86; in contrast, control by other foreigners is increasing - by about 1 per cent annually; as of 1987, however, the share of total assets held by non-U.S. foreigners was still less than 10 per cent;

- foreign control of sales and profits has also declined sharply; foreign control of profits is in the 35-45 per cent range; as will be noted later, reinvested earnings have accounted for most of the growth in the stock of foreign direct investment in Canada;

- the new CALURA series for all industries indicates that, in terms of assets, foreign control increased by 1.3 percentage points between 1984 and 1987; this reflects, among other developments, deregulation of the financial sector in early 1984; in contrast to foreign control of assets, foreign control of revenues and profits for all industries has fallen since 1984 - dramatically so in the case of profits.

Chart #17

Foreign-Control of Corporate Assets in Canada



Source: Statistics Canada

INVESTMENT CANADA INVESTISSEMENT CANADA

Chart #18: Foreign Control By Sector

- with the exception of the financial sector, foreign control has declined in all major industry categories;

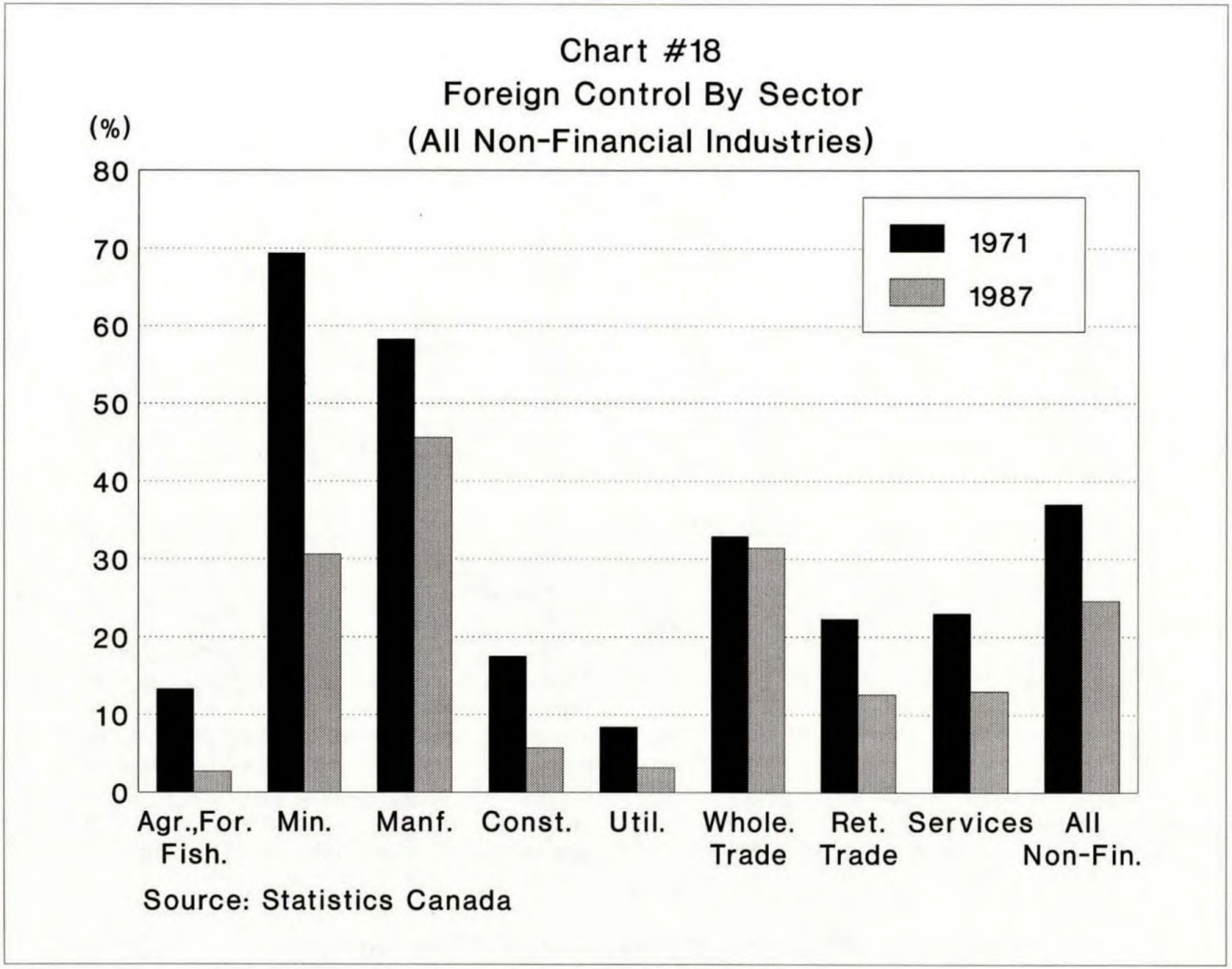
- the decline between 1971 and 1987 was pronounced in the case of the mining sector; however, since 1987 there has been a significant increase in the degree of ownership and control of the oil and gas industry; Canadian ownership in this sector has fallen by 4 percentage points and Canadian control by 12.3 percentage points; more than half the slippage in ownership and control was due to foreign takeovers involving Canadian oil and gas companies in financial distress; the most notable of these was Amoco's takeover of Dome Petroleum;

- with the exception of the oil and gas sector, the decline in foreign control has been most marked in natural resource based sectors; foreign participation has shifted, in relative terms, to Canada's manufacturing and service sectors;

- foreign control of Canada's manufacturing sector is currently about 46 per cent, compared to almost 60 per cent in 1971; Chart 19 following provides a detailed breakdown of developments in the manufacturing sector;

- the industrial distribution of foreign-controlled assets varies considerably depending on the country of control; wholesale trade accounts for some three-quarters of all Japanese-controlled assets while manufacturing accounts for 70 per cent of all British-controlled assets;

- foreign-controlled firms in Canada appear to perform better than Canadian-controlled firms; in 1987, U.S. controlled firms (in the non-financial sectors) generated $1.33 in revenues (sales) for each dollar of assets, compared to $1.10 for other foreign firms and $1.08 for Canadian firms; profitability ratios are also generally better for foreign-controlled firms.



INVESTMENT CANADA INVESTISSEMENT CANADA

Chart #19: Foreign Control Of The Manufacturing Sector

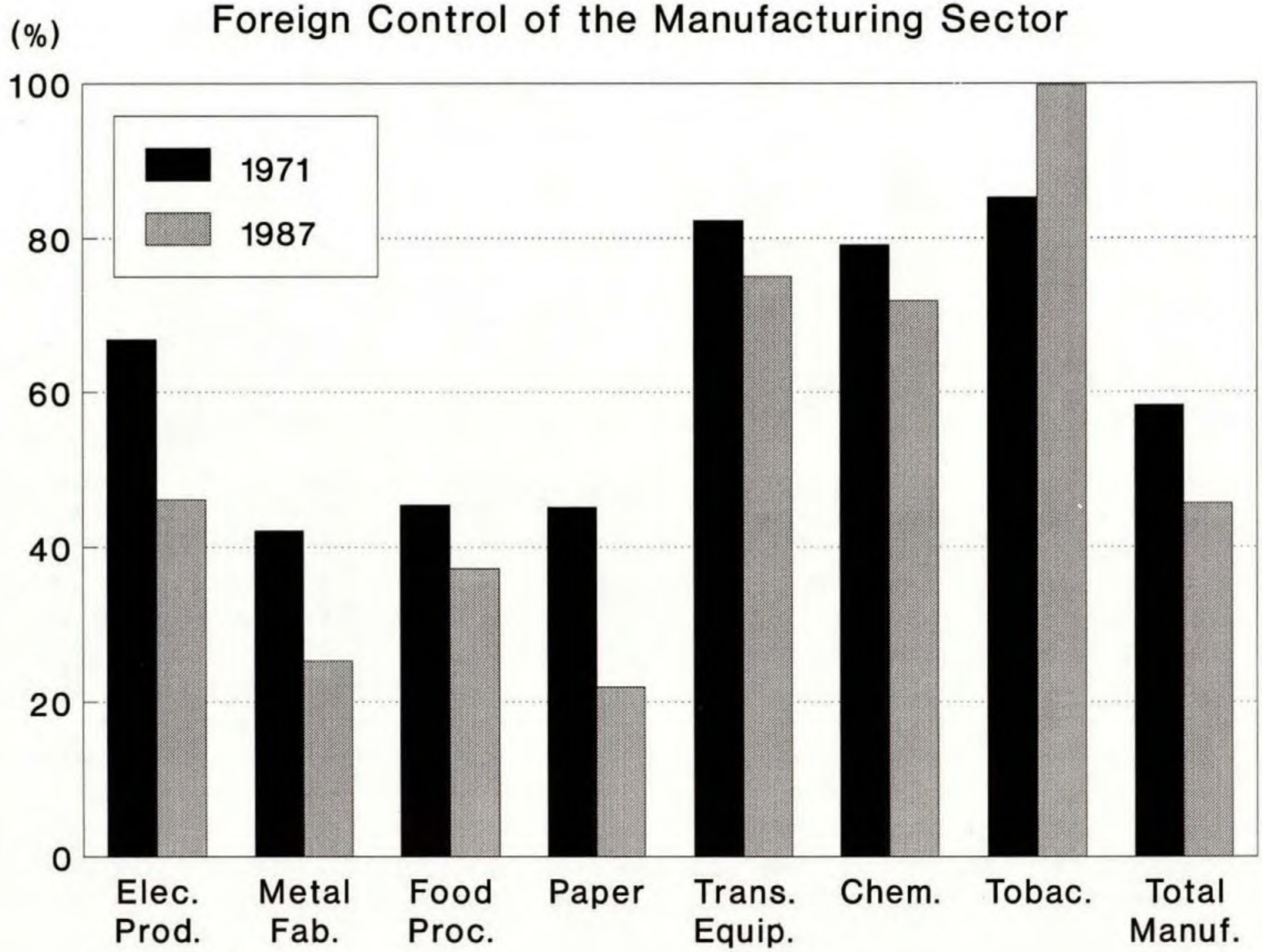
- the degree of foreign control of Canada's manufacturing sector varies considerably from sub-sector to sub-sector: almost 100 per cent for the tobacco industry; 75 per cent for transportation equipment; 72 per cent for chemicals; 46 per cent for electrical products; 17.4 per cent for leather products; 13.5 per cent for furniture products; and about 12 per cent for clothing;

- the metal fabricating and paper sectors have relatively low levels of foreign control, at just over 20 per cent;

- the degree of foreign control is lowest in the knitting mills (7.8 per cent) and the printing and publishing (9.2 per cent) sectors;

- most manufacturing sub-sectors have experienced a decline in foreign control, but in some cases (e.g. tobacco) there has been an increase.

Chart #19
Foreign Control of the Manufacturing Sector



Source: Statistics Canada

INVESTMENT CANADA INVESTISSEMENT CANADA

Chart # 20: Industry Distribution Of Foreign Direct Investment In Canada

- the preceding charts have indicated the declining degree of foreign control in most industry sectors in Canada;

- the accompanying chart indicates how this change has affected the industry distribution of foreign direct investment in Canada;

- over the past three decades there has been a slight increase in the share of foreign direct investment accounted for by the manufacturing sector and a significant increase in the share accounted for by the service sector - especially by the financial services sub-sector;

- during this period the concentration of foreign direct investment in the natural resource sectors has declined considerably;

- these shifts are generally consistent with the evolution of the Canadian economy; the proportion of gross domestic product accounted for by the manufacturing sector has remained almost constant over the past three decades, despite a sharp drop in its importance as a source of employment; the importance of natural resource sectors has declined while the importance of the service sector has increased.

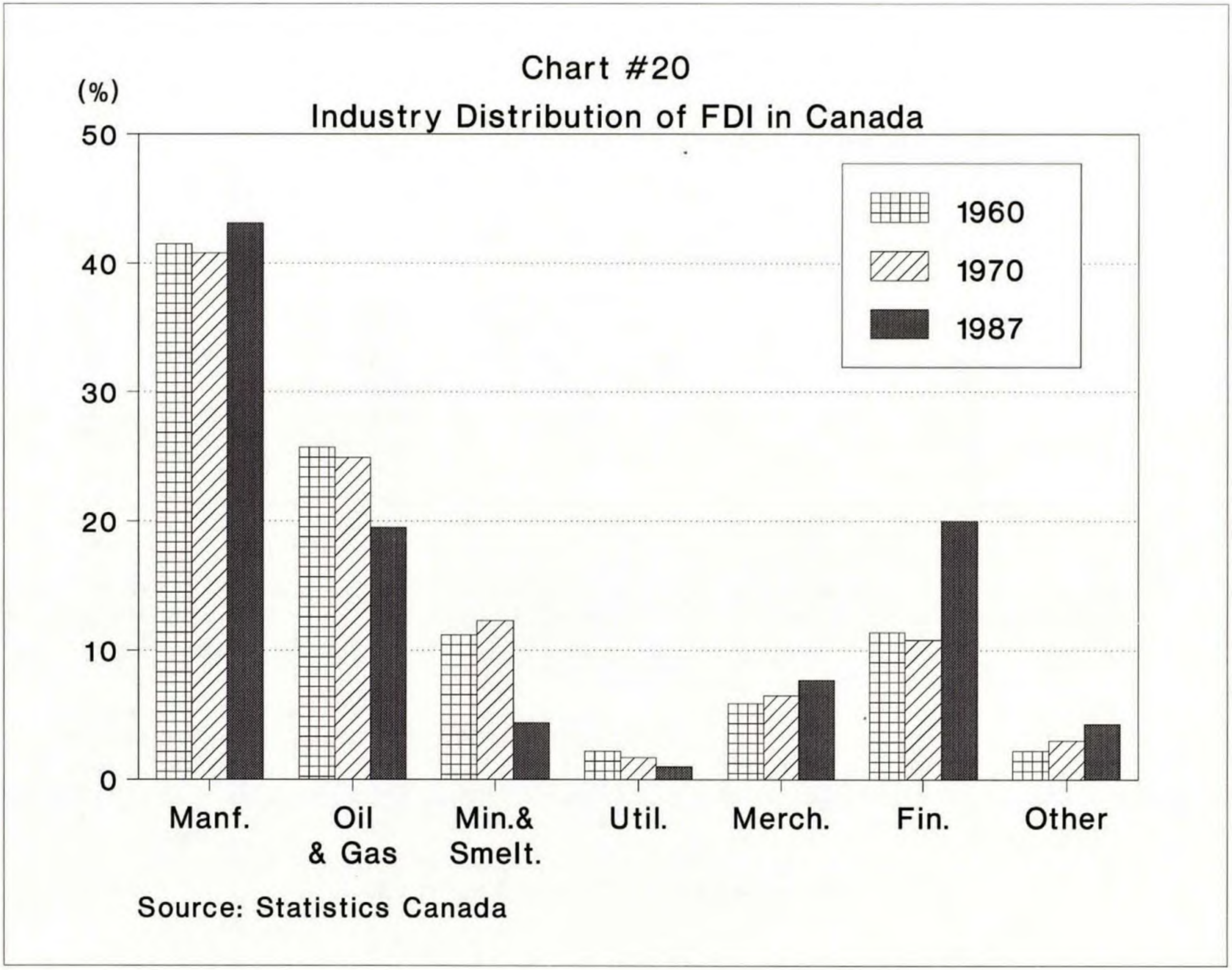


Chart #20
Industry Distribution of FDI in Canada
(%)
50
40
30
20
10
0
1960
1970
1987
Manf.
Oil & Gas
Min.& Smelt.
Util.
Merch.
Fin.
Other
Source: Statistics Canada

Chart #21: Gross and Net FDI Flows To Canada

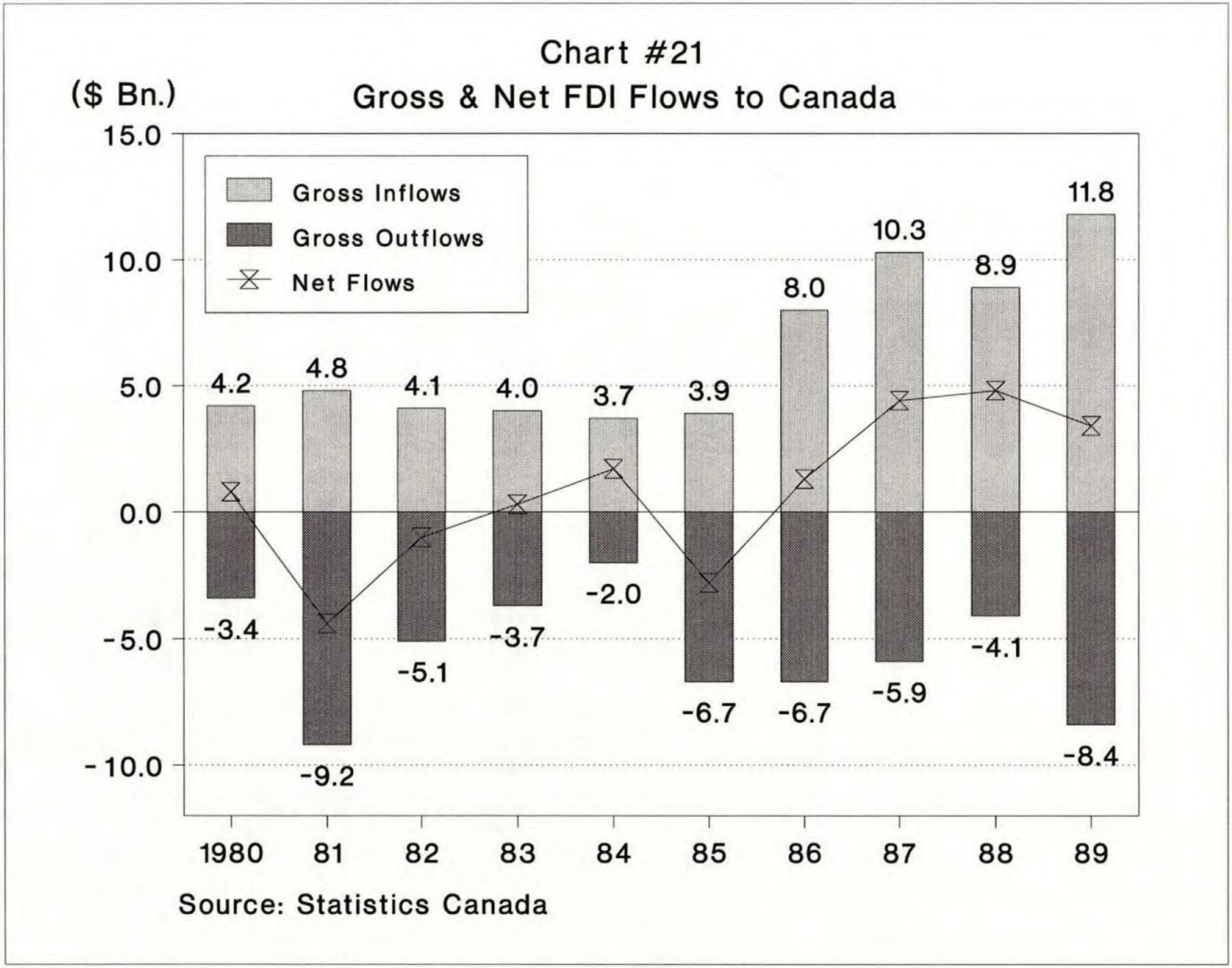
- while Chart #17 showed that the degree of foreign control has declined considerably since 1971, the decline has not been due to a decline in the amount of foreign investment;

- on the contrary, as shown in the accompanying chart, cross-border flows of foreign direct investment into Canada have doubled during the 1980s;

- the chart shows gross inflows, gross outflows and net flows of foreign direct investment to Canada; gross inflows are self-explanatory but it should be explained that gross outflows relate to divestitures of foreign investment in Canada and not to dividend payments abroad;

- since 1985, when Investment Canada was established, gross inflows have increased from less than $4 billion annually to more than $8 billion annually; gross inflows were $8.9 billion in 1988 and $11.8 billion in 1989;

- whereas the net, cross-border inflow of foreign direct investment (i.e. gross inflows less gross outflows) was negative during the first half of the 1980s, it is now strongly positive; some $5 billion entered Canada in both 1987 and 1988; in 1989, net cross-border flows dropped to $3.4 billion due to divestitures such as Texaco Canada.



INVESTMENT CANADA INVESTISSEMENT CANADA

Chart #22: Relative Importance Of Reinvested Earnings Versus Cross-Border Flows

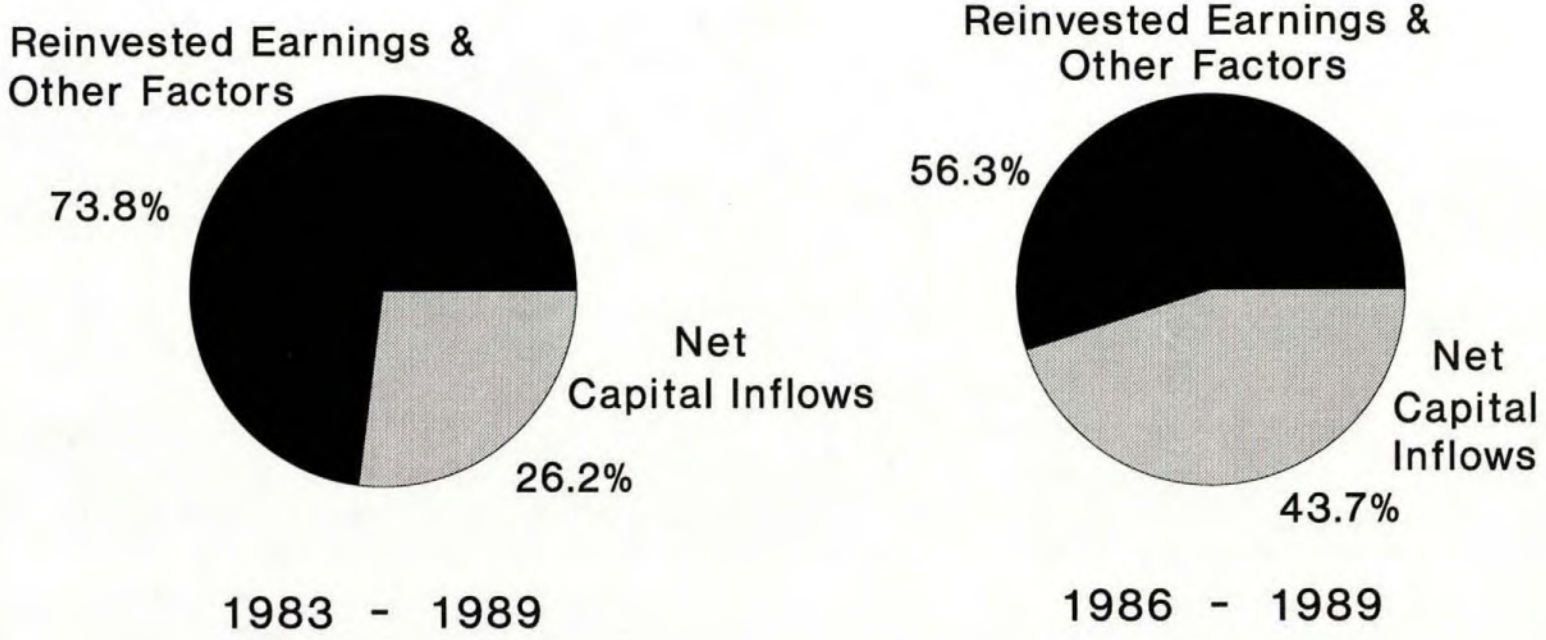
- as shown in the accompanying chart, cross-border flows of capital are not the most important factor contributing to the stock of foreign direct investment in Canada; for the period 1983-89, in fact, such flows accounted for only 26 per cent of the growth in the stock of foreign direct investment in Canada;

- reinvested earnings and other factors (notably the revaluation of the book value of foreign investment when it changes hands) are much more important in explaining the growth in the stock of foreign direct investment in Canada; they accounted for 74 per cent of the growth of the stock of foreign direct investment between 1983-89; the high level of reinvestment attests to the enduring benefits of foreign investment for Canada;

- the relative contribution of cross-border flows has increased sharply in recent years; during the 1986-89 period such flows accounted for 44 per cent of the growth in the stock.

Chart #22

Relative Importance of Reinvested Earnings
Versus Cross-Border Flows



Source: Statistics Canada

Chart #23: Relative Importance Of Foreign Acquisitions Versus Investment In New Businesses And Expansions

- during the early 1980s, acquisitions accounted for only about 7 per cent of total gross inflows of foreign direct investment; recently, however, acquisitions have accounted for more than 50 per cent of the total;

- according to Investment Canada data, almost half of all foreign takeovers involve Canadian-based firms that were already foreign controlled;

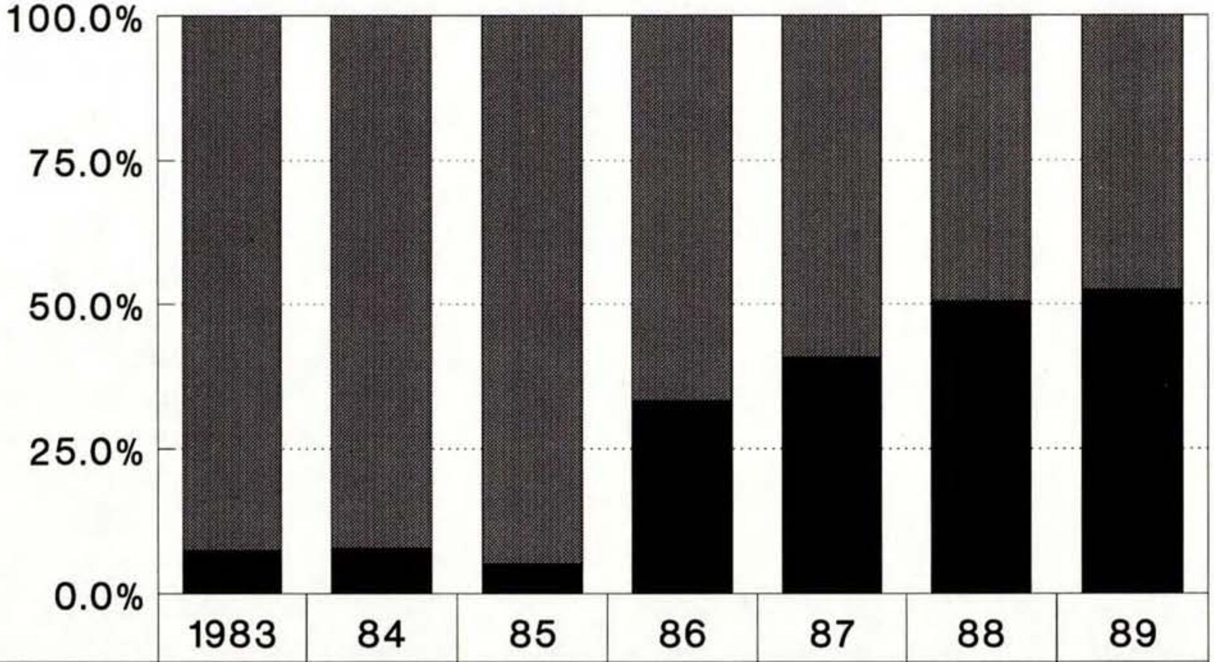
- in many cases, foreign takeovers of formally Canadian-owned firms are the result of Canadian overtures; this was the case, for example, in respect to the takeover of Connaught BioSciences by Institut Mérieux;

- foreign takeover activity has been predominantly in the manufacturing sector (34 per cent) and the wholesale and retail trades sector (27 per cent); foreign investment in transportation and storage, communication and other utilities, finance and insurance industries and real estate businesses has also been important (20 per cent);

- as noted earlier, foreign investment in the oil and gas industry has been considerable in recent years;

- while foreign investment in the real estate sector has attracted a lot of media attention, especially in the western provinces, its importance tends to be exaggerated; a study of housing prices in Vancouver has found that the main factor driving the rapid increase is demographic forces rather than (as often alleged) off-shore money.

Chart #23
Relative Importance of Foreign Acquisitions Versus New Businesses and Expansions



	1983	84	85	86	87	88	89
New Bus. & Expan.	3.7	3.5	3.7	5.4	6.1	4.4	5.6
Acquisitions	0.3	0.3	0.2	2.7	4.2	4.5	6.2
Gross FDI Inflows ($ Bn.)	4.0	3.7	3.9	8.1	10.3	8.9	11.8

Source: Statistics Canada

Chart #24: Provincial Distribution of Foreign Acquisitions and New Business Investments

- for information about the provincial distribution of foreign investment it is necessary to draw from Investment Canada records on acquisitions and new businesses;

- for statistical purposes, investments are attributed to the province with the largest share of employees of the business concerned; in the case of acquisitions, the acquired business is frequently active in more than one province, thus the accompanying chart does not fully reflect the provincial distribution of foreign acquisition activity;

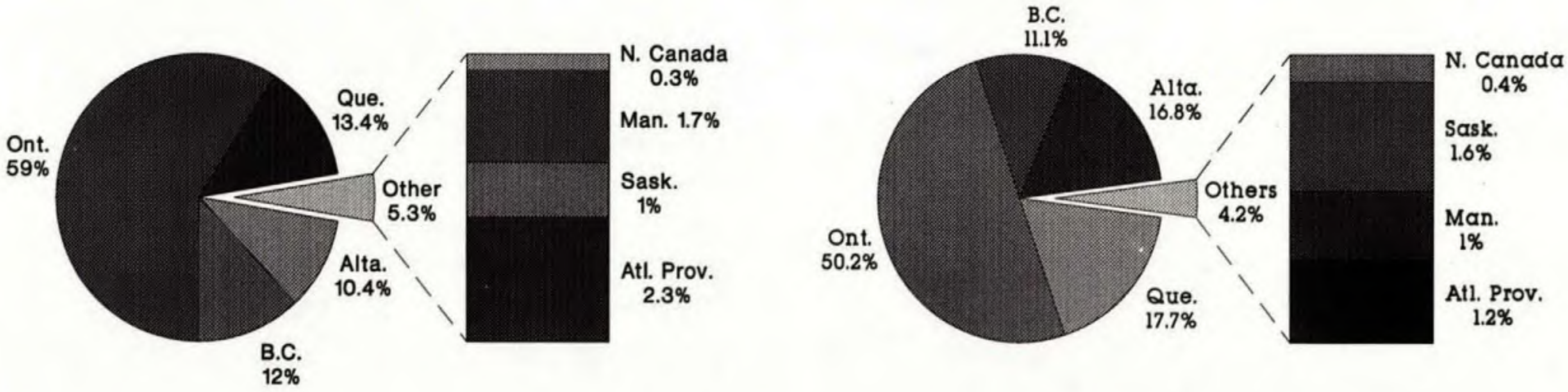
- bearing in mind the above caveat, and the fact that a significant number of foreign investments in new businesses are not registered with Investment Canada, the chart indicates that almost 60 per cent of all foreign investments are in Ontario;

- Quebec accounts for 13 per cent, while British Columbia accounts for 12 per cent and Alberta for 10 per cent;

- in value terms the distribution is more evenly spread across the country; Ontario's share is slightly less than 50 per cent and Quebec's is slightly more than 18 per cent; Alberta has a relatively high share in value terms because of capital-intensive investments in the oil and gas sector.

Chart #24

Provincial Distribution of Foreign Acquisitions and New Businesses (June 30, 1985 to June 30, 1990)



Number of Investments: 4,844

Total Value: $87.7 Billion

Source: Investment Canada

Chart #25: Distribution Of FDI In Canada By Area Of Ownership

- one of the most striking developments concerning foreign investment in Canada in recent years has been the decline in the relative importance of the United States;

- this chart shows the total stock of foreign direct investment in Canada in both 1983 and 1987, and the source countries for this investment;

- whereas the United States accounted for over 75 per cent of the total stock of foreign direct investment in Canada in 1983, only 4 years later this share had dropped to 71 per cent; preliminary data for 1989 indicate that the U.S. share has continued to decline - to about 68 per cent; this decline is all the more striking when compared to its position in the late 1970s, when it accounted for about 80 per cent of total foreign direct investment in Canada;

- in contrast, the shares accounted for by the United Kingdom, Japan and West Germany have all increased, as have the shares for several other countries - including, of course, Hong Kong;

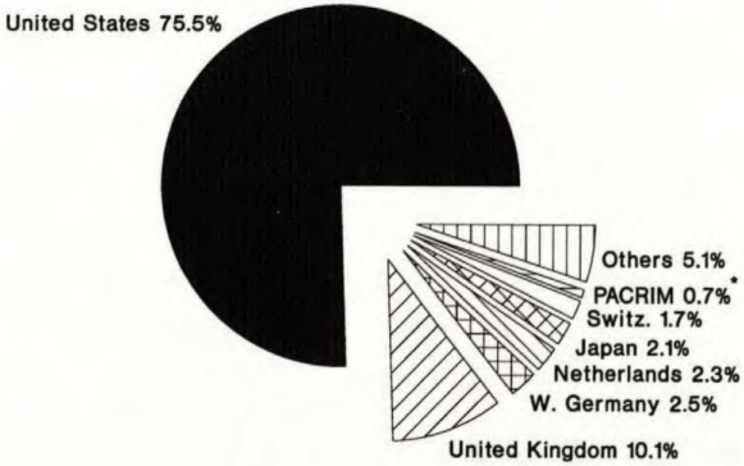
- despite their increasing importance, Japan accounted for slightly more than 3 per cent and Hong Kong for less than 1 per cent of the total stock of foreign direct investment in Canada in 1987;

- the total stock of foreign direct investment in Canada in 1987 was $102 billion; the preliminary estimates for 1988 and 1989 are $109 billion and $119 billion, respectively.

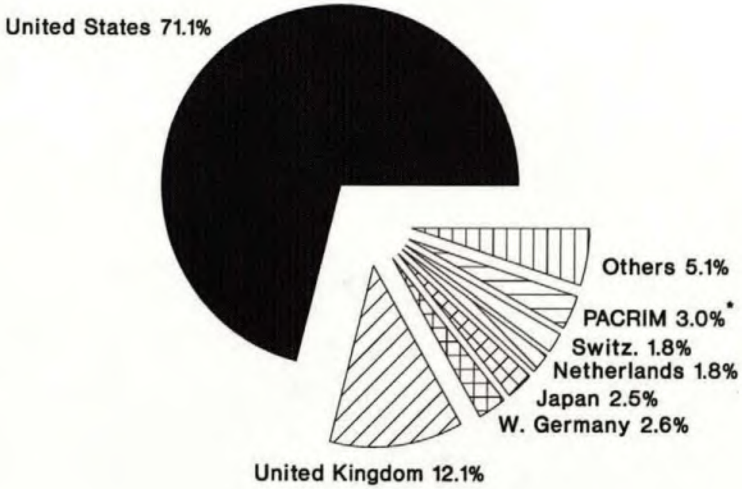
Chart #25

Distribution of FDI in Canada By Area of Ownership

1983 & 1987



1983 Total = $ 77.4 Billion



1987 Total = $ 101.5 Billion

* The Pacific Rim excludes Japan

Source: Statistics Canada

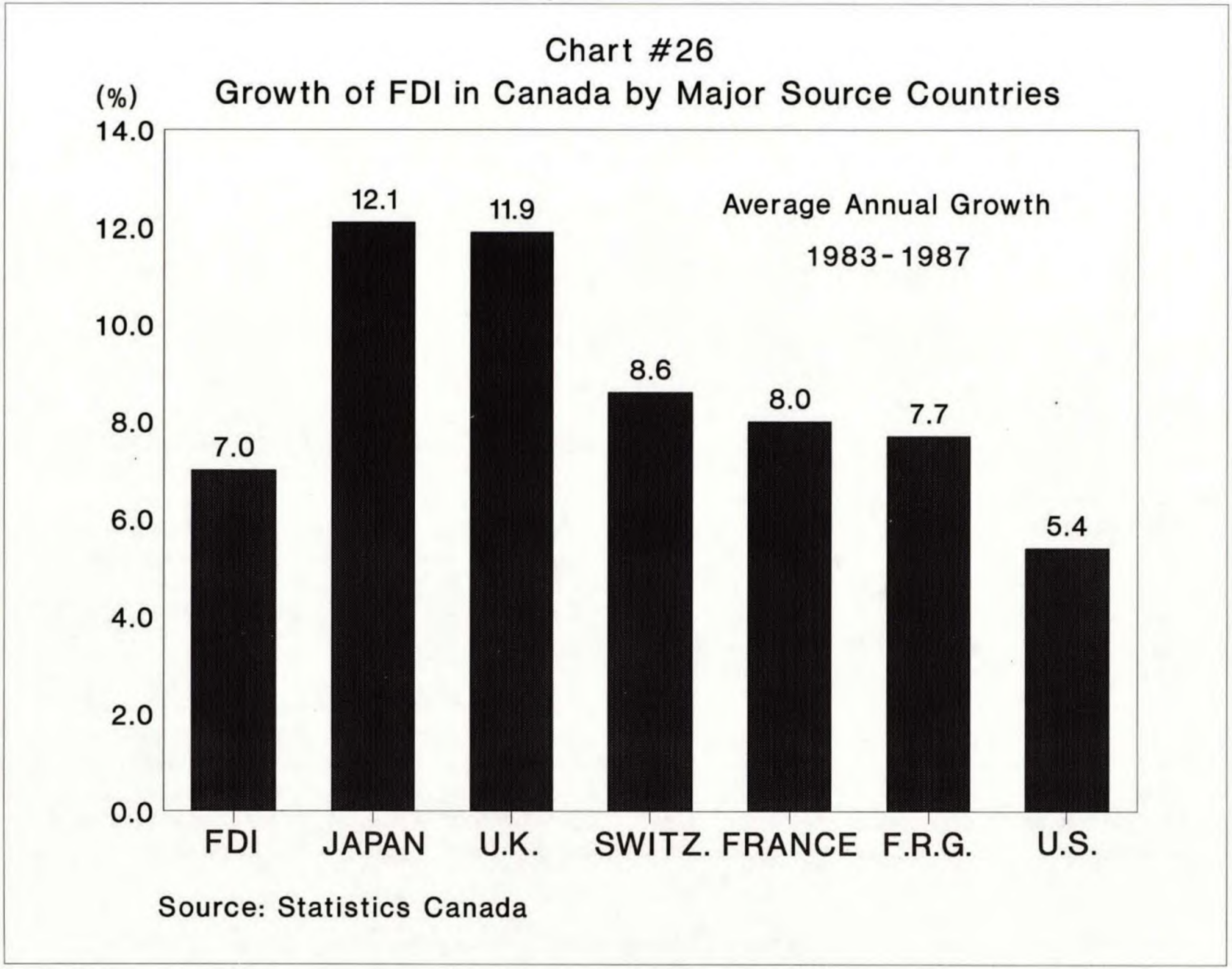
Chart #26: Growth Of FDI In Canada By Major Source Countries

- this chart illustrates the rates of growth of foreign direct investment in Canada by source country; in terms of the countries shown, Japanese investment has been rising most rapidly;

- whereas foreign direct investment in Canada grew at an average annual rate of 7 per cent during the period 1983-87, Japanese direct investment in this country grew at an annual rate of 12 per cent;

- in contrast, American investment in Canada grew by less than 6 per cent annually; European investment in Canada, particularly by the United Kingdom, has been much higher than the U.S. rate;

- investment from Hong Kong is not shown in the chart, as the growth rate is so high that it would overshadow the growth for other countries; during the three-year period 1986-88, the stock of Hong Kong investment in Canada doubled each year; despite this growth, Hong Kong accounts for only about 1 per cent of total foreign direct investment in Canada.



INVESTMENT CANADA INVESTISSEMENT CANADA

Chart #27: Book Value Of Portfolio And Direct Investment In Canada By Foreigners

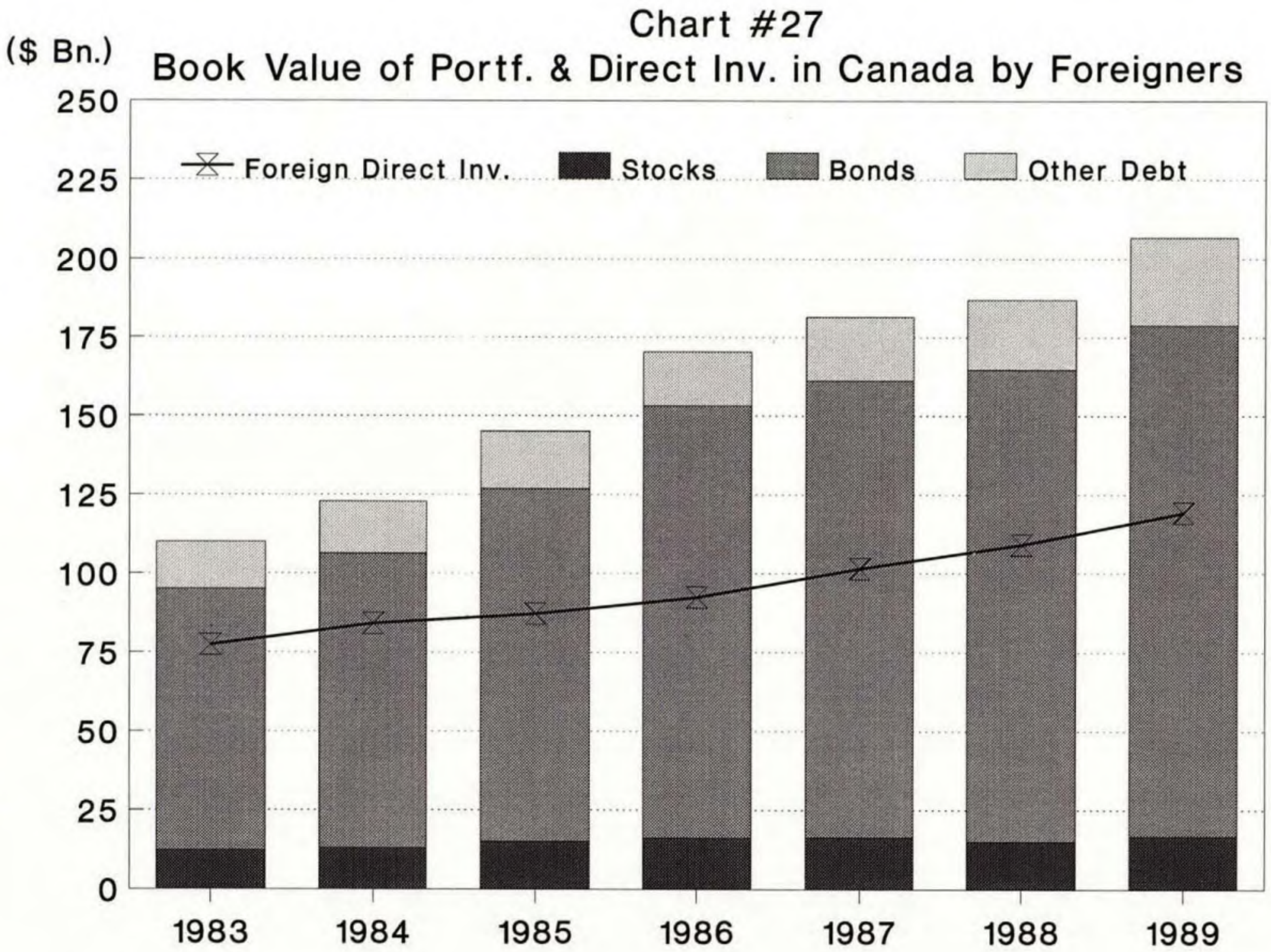
- another development of significance concerning foreign investment in Canada is the very large amount of portfolio investment; the bars in the accompanying chart show the components and overall level of foreign portfolio investment, while the superimposed line indicates the level of foreign direct investment;

- most portfolio investment is in bonds (approximately 80 per cent); in 1987, foreign bond holdings amounted to $145 billion; of this, U.S. investors accounted for 32 per cent, Japanese investors for 24 per cent and U.K investors for 5 per cent; four years earlier (i.e. in 1983) the U.S. accounted for 52 per cent and Japan for only 5 per cent;

- portfolio investment in stocks is distinguished from direct investment by the degree of control entailed; generally, a foreign investment limited to less than 10 per cent of the outstanding shares of a firm is classified as portfolio investment;

- as is evident from the chart, portfolio investment in Canada is increasing much more rapidly than direct investment; the stock of portfolio investment in Canada in 1989 was $207 billion;

- it should be recognized that Canada has a significant current account deficit, which necessitates an inflow of foreign capital.



Source: Statistics Canada

Part C: Investment Abroad By Canadians

Important Developments In Investment Abroad By Canadians

- Canadian direct investment abroad (CDIA) is considerable; in 1989, the stock of CDIA amounted to $74 billion;

- in recent years Canadian direct investment abroad has been growing more slowly than foreign direct investment in Canada; throughout most of the 1980s, however, CDIA grew more rapidly that FDI;

- approximately two-thirds of Canadian direct investment abroad is located in the United States; with the exception of the United Kingdom, relatively little CDIA is placed in Europe; also, little CDIA is located in Japan;

- the industry distribution of CDIA is similar to the pattern of FDI in Canada; most CDIA (45 per cent) is in manufacturing; while the financial services sector accounts for over 20 per cent of CDIA, there has been some pullback in this area in recent years;

- acquisitions are an important dimension of Canadian direct investment abroad; in 1989 there were a record number (152) of Canadian acquisitions abroad.

Chart #28: Comparison Of Foreign Direct Investment In Canada And Canadian Direct Investment Abroad

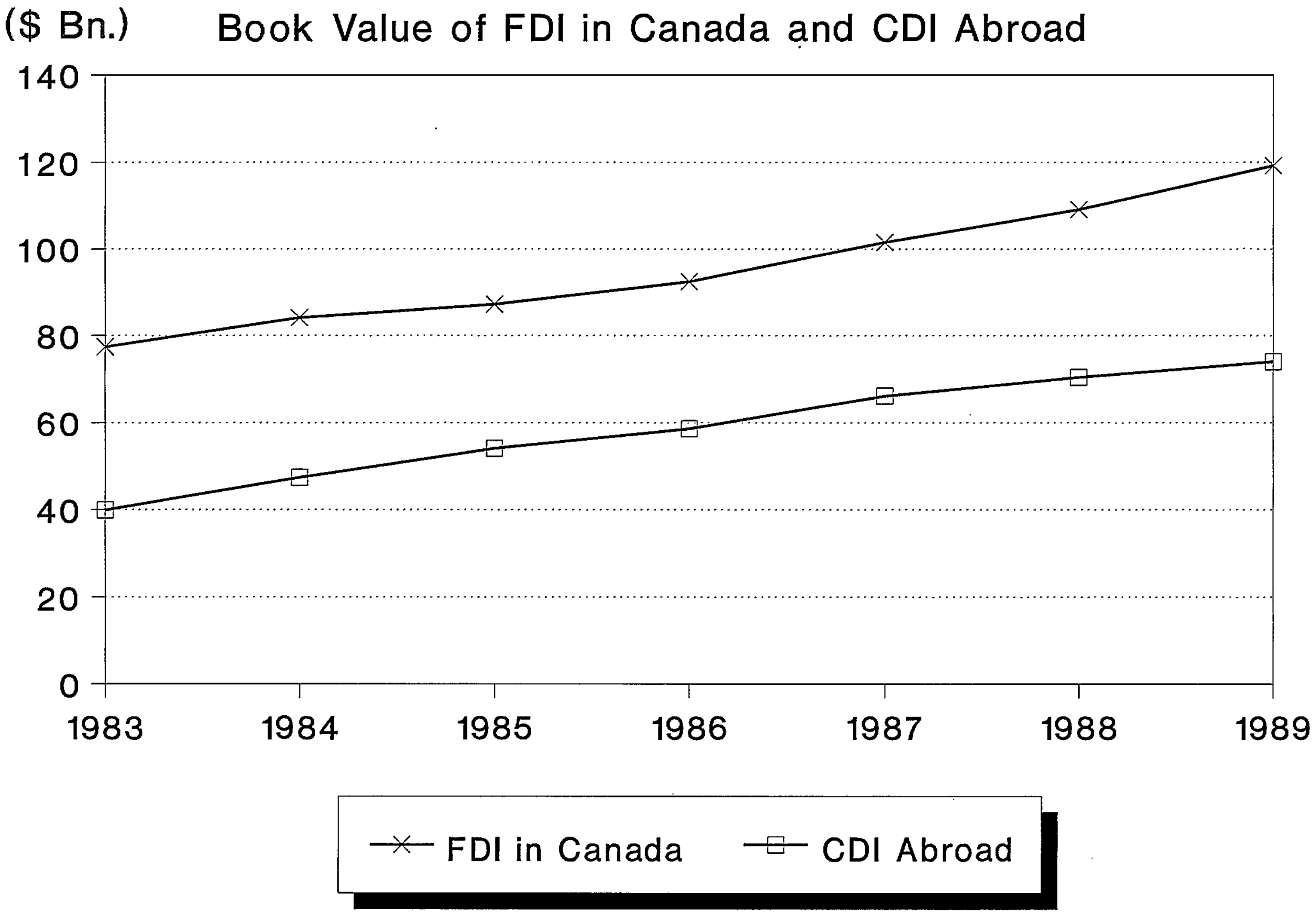
- the accompanying chart summarizes both investment by foreigners in Canada and by Canadians abroad;

- the stock of Canadian direct investment abroad in 1989 was $74 billion compared to approximately $16.4 billion in 1978 (the 1978 figure excludes CDIA in financial services); this represents a 351 per cent increase over this period;

- the stock of international direct investment in Canada in 1989 was $119 billion compared to approximately $50 billion in 1978; this represents a 138 per cent increase over this period;

- if past trends had continued, the Canadian stock of foreign assets would before long have exceeded foreign ownership of Canadian assets; the recent surge of foreign direct investment in Canada, however, has caused - at least temporarily - a widening in the gap between respective holdings of domestic and foreign assets.

Chart #28



Source: Statistics Canada

Chart #29: Gross And Net Flows Of Canadian Direct Investment Abroad

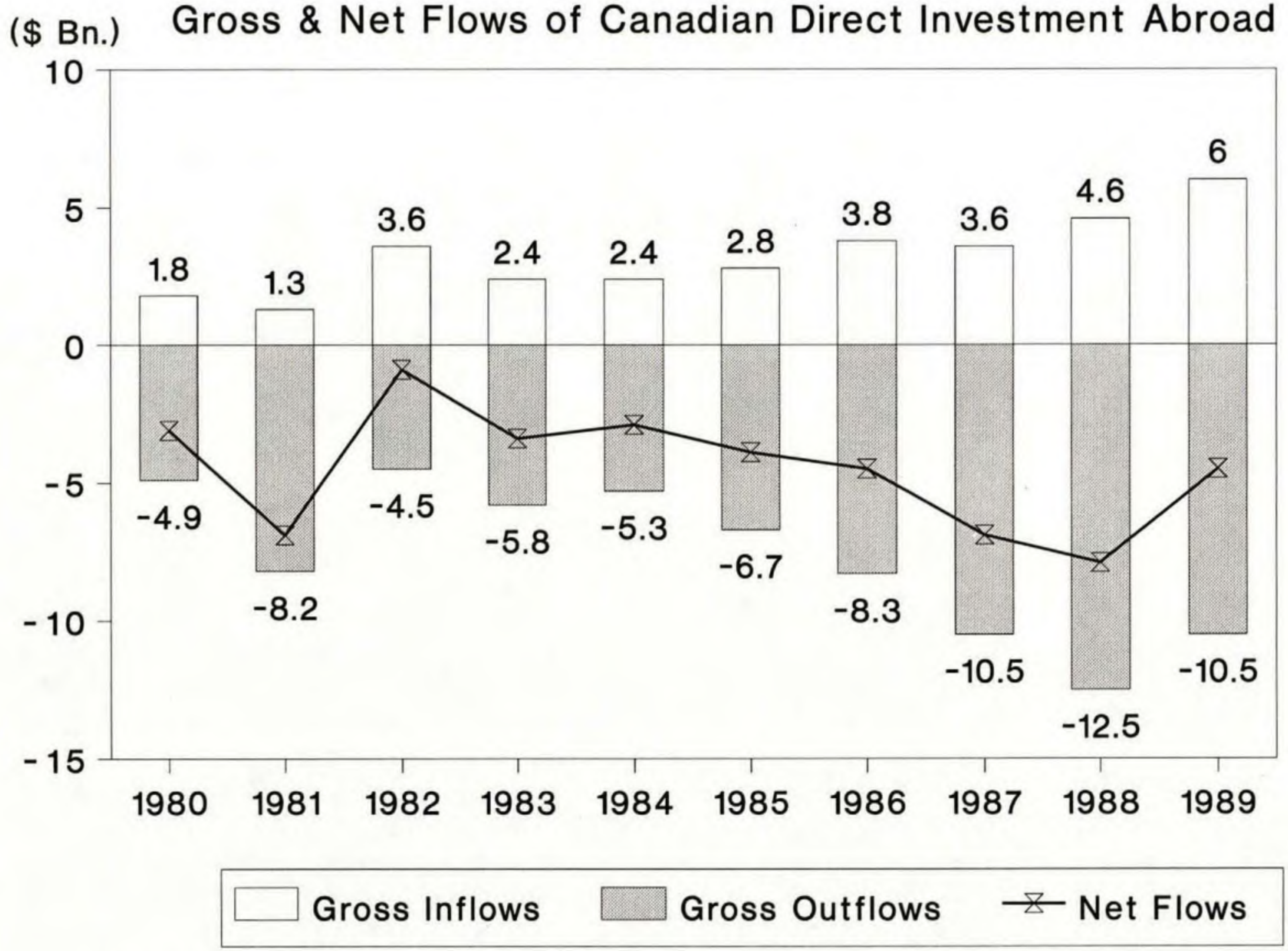
- increasingly, global business strategy demands that firms have a presence in major markets abroad, as well as trade and other forms of strategic alliances;

- foreign investment is helping Canada to be at the forefront of technology and other developments critical to remaining competitive;

- by the same token, Canadian investment abroad helps Canadian businesses to expand their markets and to network with key technology developments;

- gross outflows of Canadian direct investment abroad were $12.5 billion in 1988 and $10.5 billion in 1989; the chart shows that there has been a steady growth in investment abroad since 1984.

Chart #29
Gross & Net Flows of Canadian Direct Investment Abroad



Source : Statistics Canada

Chart #30: Country Distribution Of Canadian Direct Investment Abroad

- some two-thirds of Canadian direct investment abroad is located in the United States; this high level reflects the close integration of the Canadian and U.S. economies, including the considerable amount of intra-corporate trade;

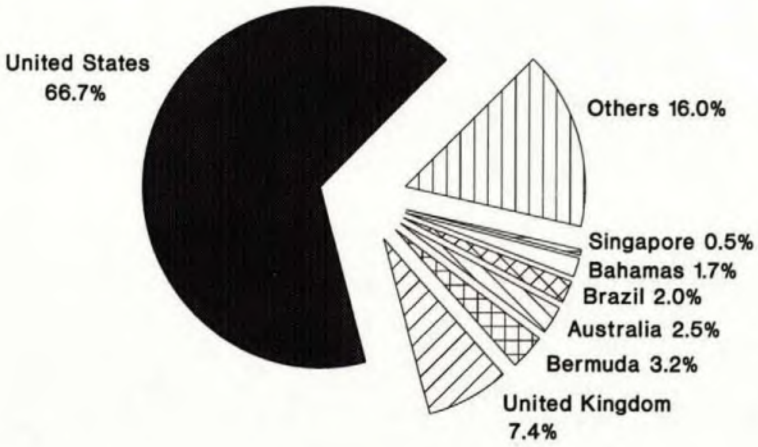
- smaller amounts of CDIA are located in the United Kingdom (10 per cent), and Singapore, Bermuda, Indonesia, Brazil, and Australia (each at about 2 per cent);

- the increasing importance of Japan and the European Community may require Canadians to invest more in future in these components of the Triad; little more than $200 million is invested in Japan by Canadians.

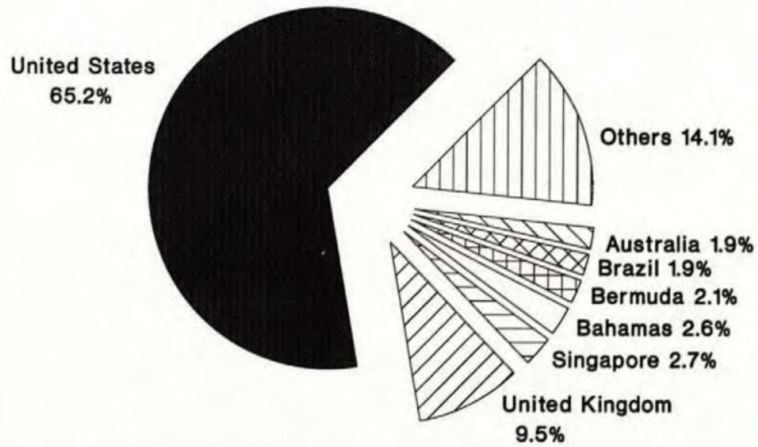
Chart #30

Country Distribution of Canadian Direct Investment Abroad

1983 & 1987



1983 Total = $ 39.9 Billion



1987 Total = $ 66.1 Billion

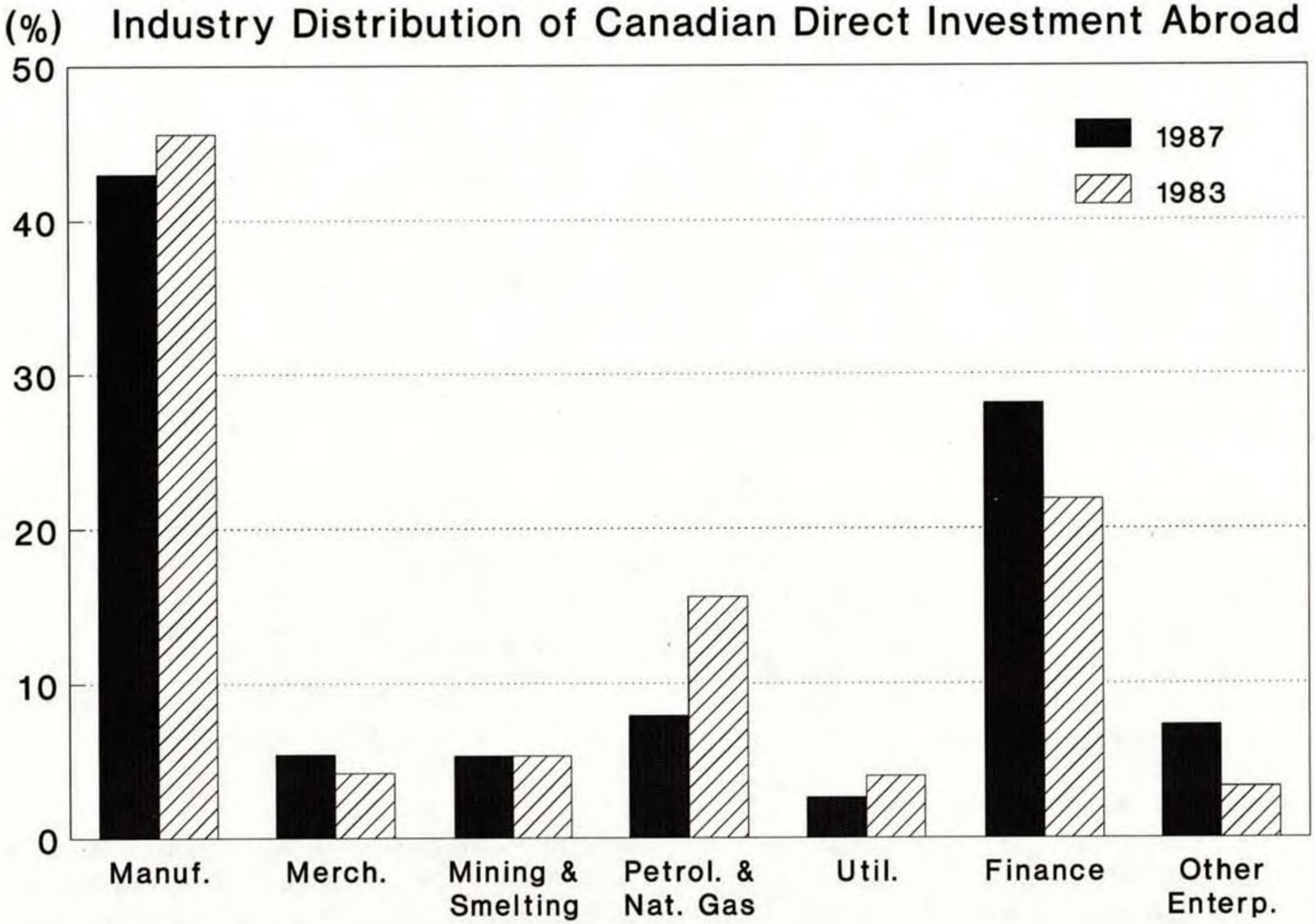
Source: Statistics Canada

Chart #31: Industry Distribution Of Canadian Direct Investment Abroad

- as indicated in the accompanying chart, some 45 per cent of Canadian direct investment abroad is in manufacturing;
- CDIA in financial services is also considerable; it should be noted, however, that there has been some pull-back from this sector in recent years;
- with the exception of the oil and gas sector, CDIA in natural resource sectors is relatively limited.

Chart #31

Industry Distribution of Canadian Direct Investment Abroad



Source: Statistics Canada

Chart #32: Acquisitions Abroad By Canadian-Controlled Firms

- as in the case of foreign direct investment in Canada, acquisitions abroad by Canadian-controlled firms figure importantly in building an international presence;

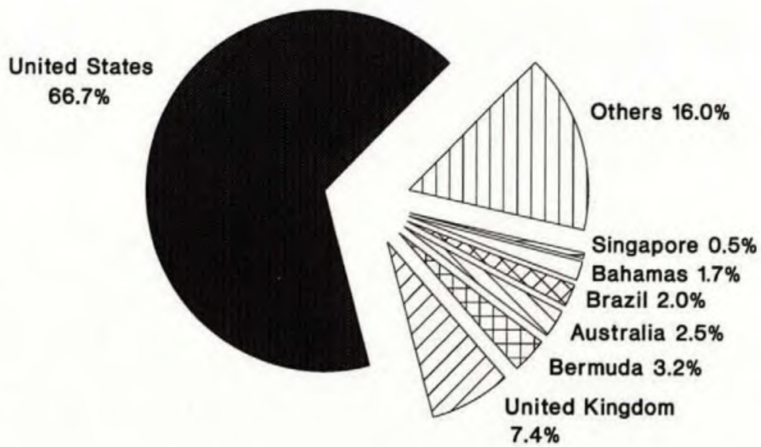
- the number of Canadian acquisitions abroad jumped considerably in 1989, to a record of 152;

- merger and acquisition activity worldwide slowed considerably in 1990, reflecting slower economic growth, increasing caution respecting levered buy-outs, and disappointment respecting the rate of return on investments from earlier mergers and acquisitions; it is to be expected that the number of Canadian acquisitions abroad will moderate to levels experienced between 1986-88.

Chart #30

Country Distribution of Canadian Direct Investment Abroad

1983 & 1987



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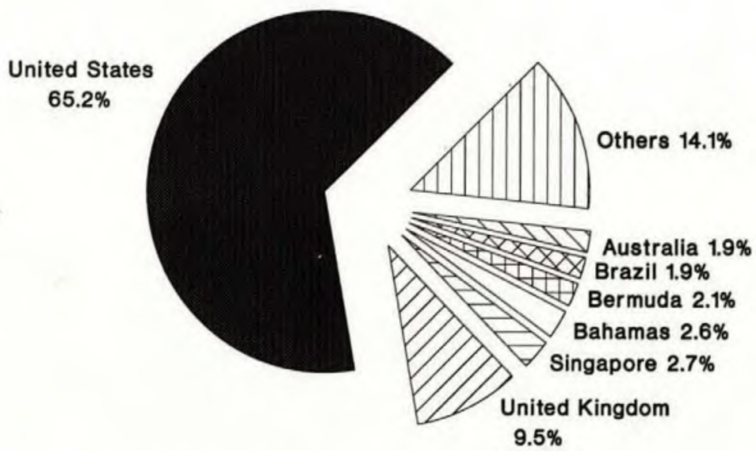

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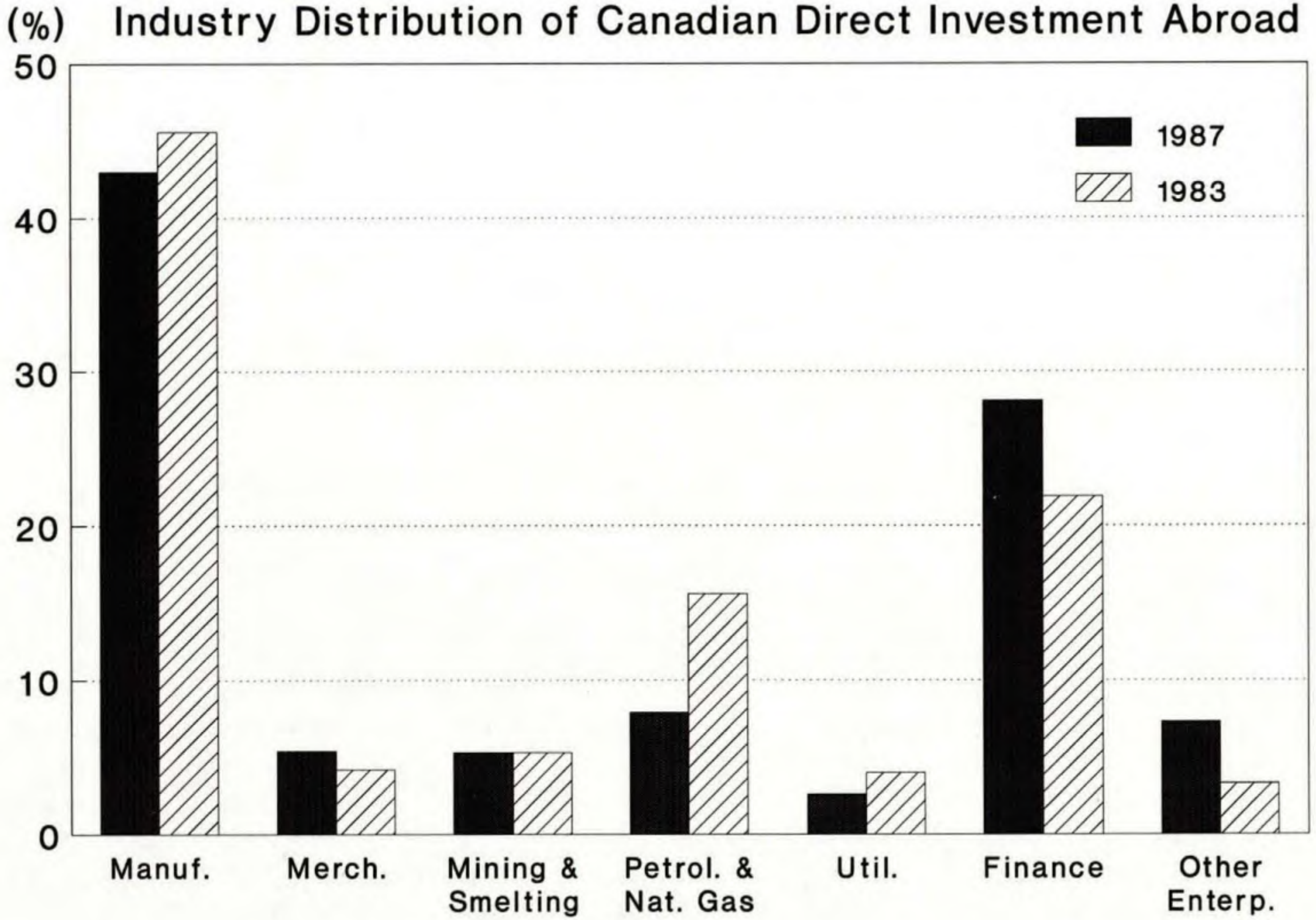
Chart #31



Source: Statistics Canada

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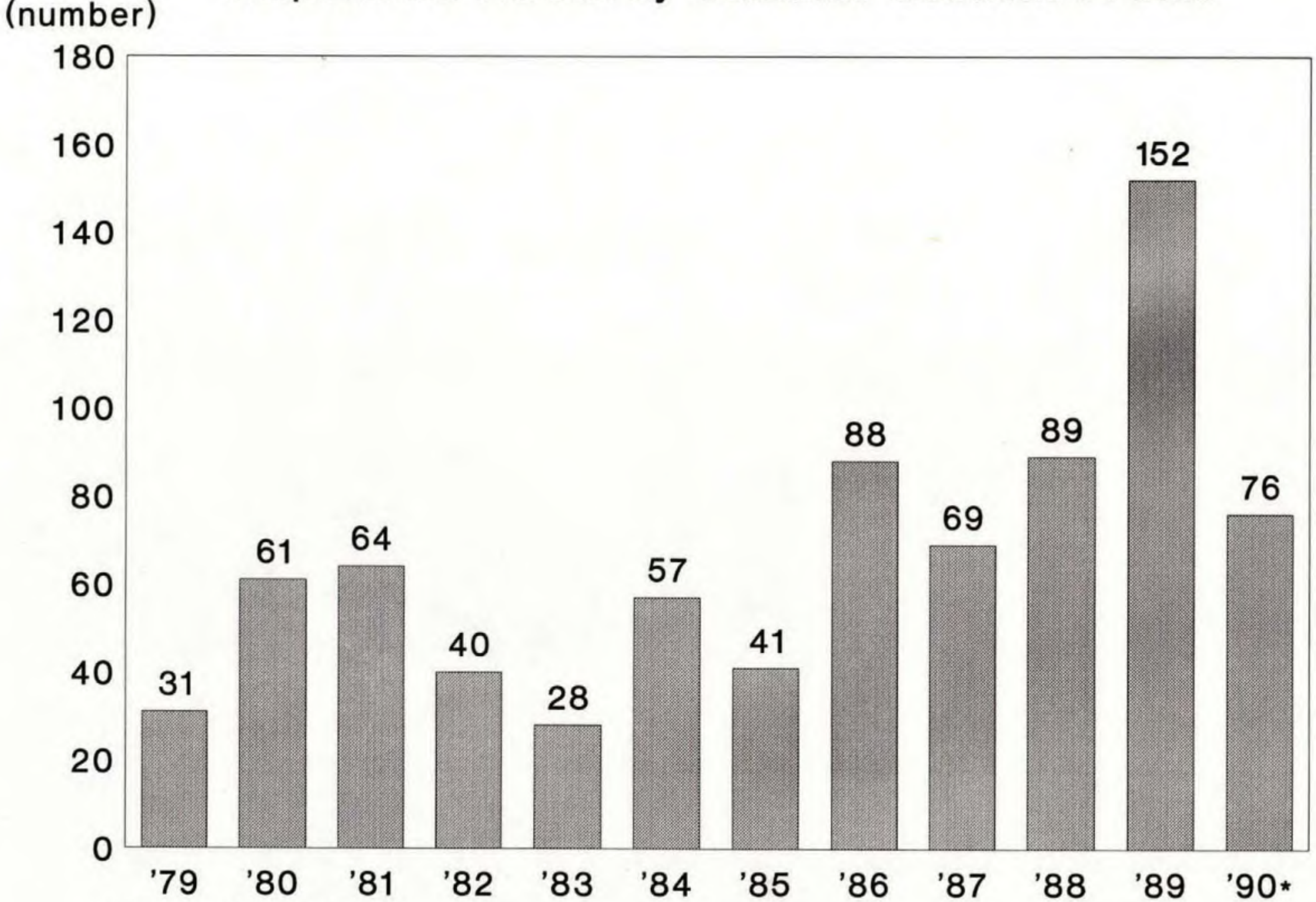


* Year to September.

Source: Automated Data Processing, Ann Arbor, Mich., USA.

Part D: Canada's Net Direct Investment Position

Chart #33: Canada's Net Direct Investment Position

•whether Canada is a net exporter or importer of foreign direct investment (as distinct from portfolio investment) depends on the relative importance of the following: the net inflows of foreign investment; the amount of reinvested earnings from foreign investments already in Canada; the increase in the value of foreign investments as the result of adjustments in the book value when assets change owners; the net outflows of Canadian direct investment; and the change in the stock of Canadian assets abroad due to reinvested earnings and adjustments in the book value;

•the accompanying composite chart summarizes all these factors; the top right-hand chart shows the net effect of cross-border flows while the bottom right-hand chart shows the net effect of reinvested earnings and adjustments to the book value of assets (in both cases by foreigners in Canada and by Canadians abroad);

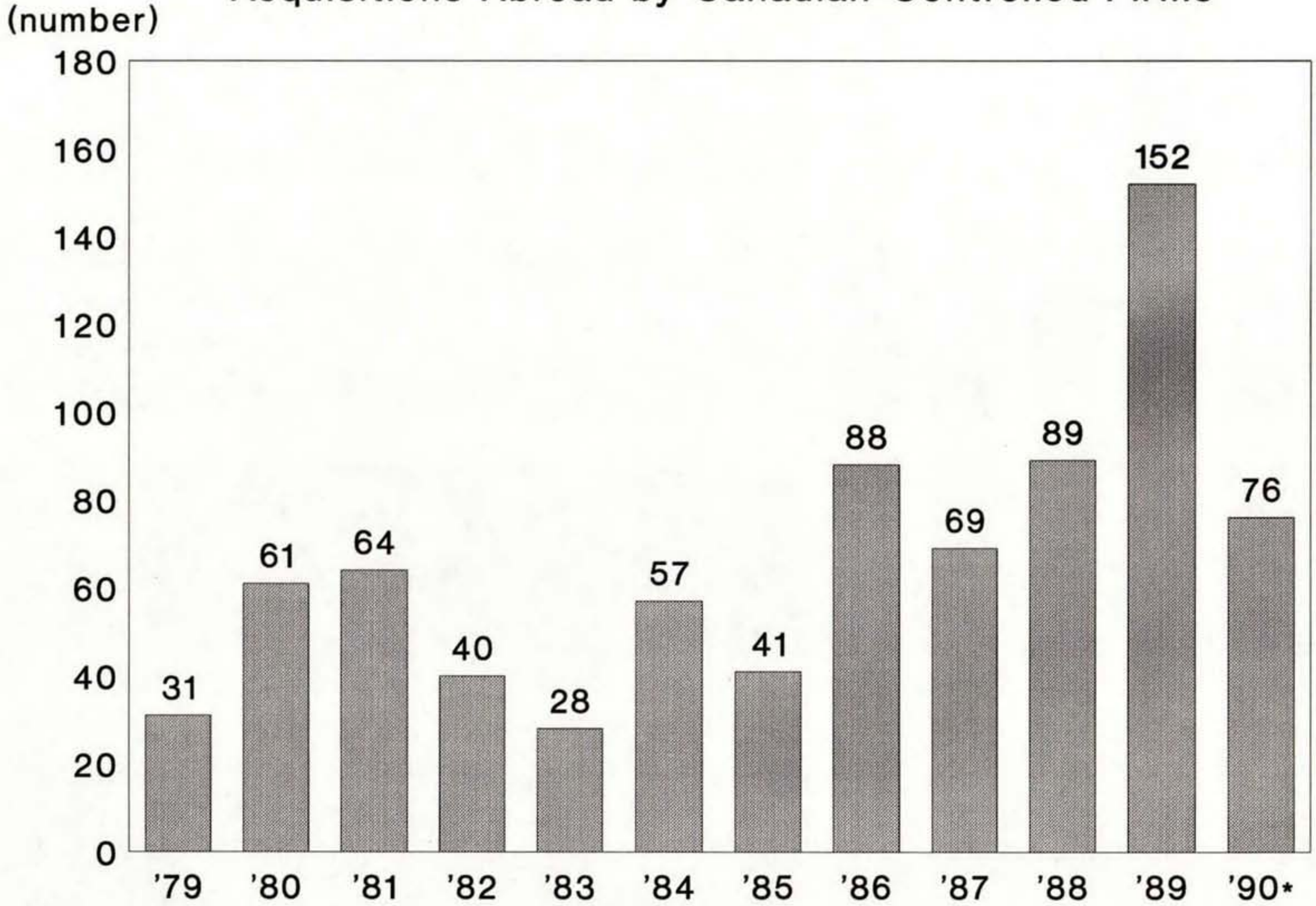
•the main chart shows the net effect of all these factors; for the most part during the first half of the 1980s Canada was a net exporter of foreign direct investment; since 1985, however, Canada has become - as had been the case over the post-war period up to 1978 - a significant net importer of foreign direct investment; in 1989 direct capital imports were $6.5 billion;

- not incorporated in the chart are dividends paid out to foreign holders of Canadian-based corporate assets; these payments amounted to $34.2 billion over the 1980-88 period; dividend payments do not affect the stock of foreign direct investment;

- also not incorporated in the chart are inflows of dividends, which amounted to approximately $16 billion over the same period.

Chart #32

Acquisitions Abroad by Canadian-Controlled Firms



* Year to September.

Source: Automated Data Processing, Ann Arbor, Mich., USA.

Part D: Canada's Net Direct Investment Position

Chart #33: Canada's Net Direct Investment Position

•whether Canada is a net exporter or importer of foreign direct investment (as distinct from portfolio investment) depends on the relative importance of the following: the net inflows of foreign investment; the amount of reinvested earnings from foreign investments already in Canada; the increase in the value of foreign investments as the result of adjustments in the book value when assets change owners; the net outflows of Canadian direct investment; and the change in the stock of Canadian assets abroad due to reinvested earnings and adjustments in the book value;

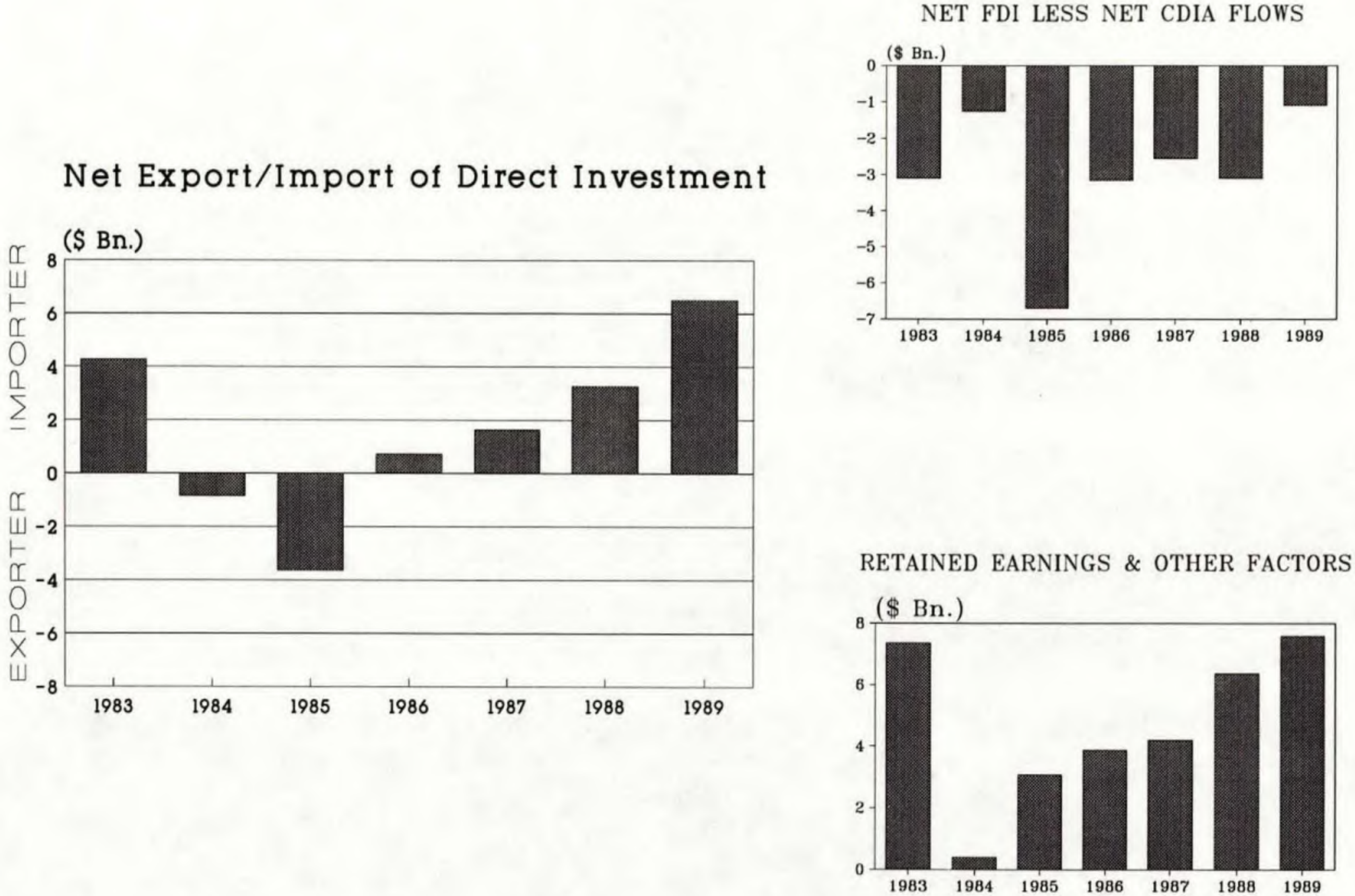
•the accompanying composite chart summarizes all these factors; the top right-hand chart shows the net effect of cross-border flows while the bottom right-hand chart shows the net effect of reinvested earnings and adjustments to the book value of assets (in both cases by foreigners in Canada and by Canadians abroad);

•the main chart shows the net effect of all these factors; for the most part during the first half of the 1980s Canada was a net exporter of foreign direct investment; since 1985, however, Canada has become - as had been the case over the post-war period up to 1978 - a significant net importer of foreign direct investment; in 1989 direct capital imports were $6.5 billion;

- not incorporated in the chart are dividends paid out to foreign holders of Canadian-based corporate assets; these payments amounted to $34.2 billion over the 1980-88 period; dividend payments do not affect the stock of foreign direct investment;

- also not incorporated in the chart are inflows of dividends, which amounted to approximately $16 billion over the same period.

Chart #33



Source: Statistics Canada