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*MAJOR RESEARCH PAPER: Foreign Direct Investment of Chinese State-Owned Enterprise in  
Canada – A Continuation of Canada's FDI Narratives*

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## **Abstract**

This paper seeks to build on the work of Mattlin and Rajavuori (2023), who found that causal narratives played a key role in the shifting perceptions of foreign direct investment (FDI) from Chinese state-owned enterprises (SOEs). These shifting perceptions, in turn, led to a *riskification* of FDI from those firms. That is to say, FDI underwent a process similar to securitization, where the end goal is risk management rather than the total annihilation of the threat. This paper will attempt to use the same analytical framework to discover if FDI in Canada has undergone a similar riskification process, and, if so, if similar causal narratives are to blame. I find that, much like with the Nordic countries examined by Mattlin and Rajavuori, Canada has *riskified* FDI and changed how FDI controls are applied to Chinese SOEs due to the proliferation of causal narratives, rather than a change in the risk of FDI from said firms themselves, and that this riskification of FDI is a continuation of a much broader historical trend rather than an entirely new phenomenon.

## Introduction

The potential threat posed by Chinese foreign direct investment (FDI) has become an increasingly covered media topic of late. Of particular concern is the FDI from Chinese state-owned enterprises (SOEs), as these actors are often seen as being more easily influenced by their home states, as being behold to non-market objectives, and otherwise posing a threat to the prosperity and national security of the host countries. This was particularly evident when The Honorable François-Philippe Champagne, Canada's Minister of Innovation, Science and Industry said in a 2022 November statement "While Canada continues to welcome foreign direct investment, we will act decisively when investments threaten our national security and our critical minerals supply chains, both at home and abroad" (ISED, 2022). However, as some authors have pointed out, it is unclear how much of this shift is being inspired by the real dangers of FDI, and how much is the result of the causal narratives surrounding FDI from SOEs (especially Chinese SOEs) (Mattlin & Rajavuori, 2023, p.2).

Of course, FDI remains vital to the Canadian economy: According to Global Affairs Canada's (GAC) 2021 Annual Report, FDI improves productivity, boosts supply chain integration and international trade, increases domestic competition among domestic firms, and has overall increased employment in Canada's manufacturing sector (GAC, 2021, pp.33-38). Seeing as SOEs (and in particular, Chinese SOEs) are becoming some of the most important participants in FDI frameworks (Cuervo-Cazurra, Grosman, & Meginson, 2022, p.79), it appears inevitable that host countries will attempt to navigate the perceived risks of FDI from SOEs if they wish to continue to reap the significant benefits awarded to them by FDI.

The goal of the present paper is to examine how perceptions of FDI from Chinese SOEs have changed in Canada and attempt to place these changes in the larger historical context of

FDI controls put into place since Confederation. More specifically, I argue that the recent shift in perceptions is not being driven by a change in the empirical risk level of investment from China, but rather from a perceived change in that risk as China moves to expand its role on the global stage.

This paper is divided into two sections. The first section is a historical analysis of FDI controls in Canada since Confederation, where I will attempt to determine to what extent historical events fit into the riskification framework proposed by Mattlin and Rajavuori (2023). In the second section, I shall attempt to place the current FDI control paradigm within the larger historical context in order to determine if it is a historical outlier.

## **Literature Review**

The literature on FDI from SOEs is ultimately quite nuanced but unified. In short, most researchers studying FDI from SOEs seem to agree (with some exceptions, such as seen in Cuervo-Cazurra, Grosman, and Meginson, 2022) that, while there are some risks involved with the practice, there are measures that can be put in place to mitigate the risks, and that the encouragement of inward FDI should remain an important policy goal for host countries. This section will explore the literature on the history of FDI (and FDI from SOEs in particular) to then explore the risks of FDI and how they have changed over time, as well as the policies proposed to mitigate them. Next, we will explore the benefits of FDI. Finally, we will examine the literature on the evolving public perception of FDI from SOEs, and whether public fears are well-founded.

*A History of Outward Foreign Direct Investment and State Enterprise*

Although State-owned enterprise has existed for at least since the late Renaissance period, State-owned enterprises as we know them truly came into force in the wake of the Great Depression and the early 1940s as governments worked to attempt to mitigate the economic disasters brought on by that period (Wright et al., 2022, p.6). These early firms, however, were not yet focused on expanding to international territory, as they were mostly created in order to address local market failures and address the needs of the citizenry while also promoting development (Wright et Al., 2022, p.6).

In the 1980s, however, with the advent of neoliberalism, states began to privatize their SOEs as such organizations were seen as being far less efficient than private for-profit enterprises (Cuervo-Cazurra and Li, 2022, p.288; Wright et al., 2022, p.6). This dramatic shift was in part due to the rise of stagflation and in part due to the end of the Cold War and the anti-state-capitalist sentiment that accompanied the period (Cuervo-Cazurra and Li, 2022, p.287-288). As Cuervo-Cazurra and Li (2022) write, however, this was a vital step in the evolution of SOEs, as it laid the groundwork for the proliferation of international SOEs (Cuervo-Cazurra and Li, 2022, p.288).

In the 2010s, however, a new type of SOE began to emerge – an internationalized SOE (Wright et al., 2022, p.6). These SOEs were riding a wave of renewed interest in the potential of SOEs, as well as intense scrutiny of the purported success of privatization from academics and development professionals (Cuervo-Cazurra and Li, 2022, p.288-289). However, SOEs did not emerge in this period unchanged. Privatization led to the creation of more nuance in state ownership. By this, I mean that state ownership became more complex than a mere “private-public” binary, but rather, State-ownership and influence began to manifest and exert itself in new and previously unheard-of ways (Cuervo-Cazurra and Li, 2022, p.288-289). This means that

states exercise a much more varied level of control over their enterprises than they had previously.

The present day, then, is a new era of state ownership and foreign direct investment. SOEs are becoming increasingly heterogeneous and varied, while the role they play across the globe is becoming increasingly important. This is particularly true for China, which has become the second largest source of FDI, the majority of which has come from SOEs since the 1990s (though private enterprise is taking an increasing share of FDI) (He, Jiang, and Benett, 2020, p.1563). With these new developments in outward FDI from SOEs, it is important now to examine the literature on the differences between FDI from private sources and FDI from SOEs.

#### *FDI from SOEs vs. FDI from Private Enterprise*

The role of state ownership in FDI strategies and internationalization, more broadly, is the subject of frequent debate in the academic field. Essentially, there are two schools of thought – one more popular, and one more academic. One view is that Chinese FDI is monolithic, and as such, OFDI strategies are unlikely to change regardless of ownership structure. Globerman and Shapiro (2009), explain this position, specifically regarding Chinese FDI in the United States: “[G]overnment ownership of large companies, or effective control through other means, is seen as allowing Chinese MNCs to pursue non-commercial objectives that, in turn, impose costs and risks on the United States. In effect, the motives of Chinese MNCs lie at the heart of concerns about Chinese acquisitions of US companies.” (Globerman & Shapiro, 2009, p.171). More specifically, the authors argue that SOEs are seen to have the following problems : (1) following non-business objectives which may perpetuate harm, (2) facilitating access to and control of natural resource supplies in order to guarantee Chinese access to the resource market at the expense of the host countries access, (3) lack of loyalty to the host country and/or influence of a

hostile government could create national security threats, (4) lack of transparency that renders decision-making and trustworthiness less scrutable, and (5) perpetuate unfair competition by receiving subsidies (Globerman & Shapiro, 2009, pp.171-176). While these ideas have in fact been contested by researchers, who also indicate that existing laws are sufficient to protect against potential abuse, (Globerman and Shapiro, 2009, p.180; Du, 2014, p.1159), the idea that Chinese SOEs are a fundamental security threat has endured in the popular consciousness.

On the other side of the debate, many scholars write that ownership structures play a key role in the strategies, and, indeed, the ability of firms to invest abroad. As Cuervo-Cazurra and Li (2022) point out, the different forms that ownership can take play an essential role in shaping the incentives of the organization (p.290-291). They identify four key characteristics that play a key role in the ability of multi-national SOEs : 1) industry (ie, SOEs that produce goods and services are less likely to internationalize than those that focus on industrial upgrading), type of state ownership (SOEs owned by central/federal governments are more likely to internationalize than SOEs owned by regional/provincial/municipal governments), level of state ownership (full and majority owned SOEs are less likely to internationalize than minority-owned SOEs), and managerial independence (more managerial independence favors internationalization) (Cuervo-Cazurra and Li, 2022). More simply put, Cuervo-Cazurra and Li (2022) argue that while home-country support favors internationalization, non-market objectives and more strict state control hinder it.

But state ownership does not only impact how likely individual organizations are to internationalize. State ownership also plays a key role in the development of the FDI strategies of individual organizations. Indeed, the specific motivations and goals of FDI are often strongly influenced by ownership structure (He, Jiang, and Bennett, 2020, p.1565). SOEs in the US for

example, are far more likely to “[...] focus on resource-seeking and market-seeking, with greenfield investments their preferred entry mode, potentially in order to overcome political obstacles restricting M&A in host states” (He, Jiang, and Bennett, 2020, p.1579). This means SOEs are more likely to seek to develop new markets or secure stable and low-cost access to strategic resources (Meyer, 2015, p.58). Private enterprise, on the other hand, was far more likely to focus on strategic asset seeking (in other words, developing their own long-term competitiveness and sustainability) (He, Jiang, and Bennett, 2020, p.1579; Meyer, 2015, p.58).

While it is clear that this debate is far from settled, it is all too clear that, in the public eye, FDI from SOEs poses a real threat to national security. The goal of this next section will be to explore the public perceptions of FDI from China and extrapolate the consequences.

#### *Public Perception of Chinese OFDI from SOEs*

Contemporary public discourse as well as new research has made it abundantly clear that public perception of FDI from SOEs and those from emerging economies (especially China) in particular. The reasons and rationale for this will be explained, as well as the potential hurdles that this shift in perception may pose for the development of good, objective IFDI policy.

Several authors (Ka & Xiaojun, 2019; Mattlin & Rajavuori, 2023; Cuervo-Cazurra, 2018) point out that public perceptions of FDI from SOEs are becoming more hostile. Studying public perceptions in the US, Ka and Xiaojun (2019) explain that negative media coverage regarding China is much more likely to inspire fear regarding externalities and security threats that could arise when dealing with Chinese SOEs (pp.502-503). Similarly, fear of emerging nations acts strongly fosters the development of nationalist sentiments, which also has a negative impact on the desire to maintain economic relations with China in that respondents became more likely to

feel China was competing economically with the US (Ka & Xiaojun, 2019, pp. 504-505). This strongly suggests that, as tensions continue to rise between the US and China, FDI from China will become less and less desirable.

Cuervo-Cazurra goes into more detail to explain the fears behind FDI from SOEs from emerging economies. He claims that fears of FDI from emerging economies can be organized into six categories according to logic (economic, political, and psychological) and the characteristics of the firm (the fact that the firm is from an emerging economy and the fact that it is a state-owned enterprise). (Cuervo-Cazurra, 2018, p.128). Cuervo-Cazurra also proposes policy solutions to address the fears and reduce risk. The fears and solutions are, in order:

- 1) Non-business objectives (state-owned, economic): the fear that FDI from SOEs can be used for non-market objectives, and, used to threaten national security (Cuervo-Cazurra, 2018, pp.140-142).
  - a. Solution: Exclude FDI from industries and sectors that may allow to pose a national security risk (Cuervo-Cazurra, 2018, p. 142).
- 2) Multi-level agency (state-owned, political): the multiple agents of SOEs mean that it is often difficult to tell in whose interest a decision was made, leading to a very opaque decision-making process. (Cuervo-Cazurra, 2018, pp.143-144).
  - a. Solution: Monitoring the SOEs in question and requiring transparency in the decision-making process (Cuervo-Cazurra, 2018, p.144).
- 3) Soft Power (state-owned, psychological): there is a fear that SOEs are used to exercise soft power abroad and flex their muscles in host countries (Cuervo-Cazurra, 2018, p. 145).

- a. Solution: Introduce controls to limit the ability of the firm to exercise soft power (Cuervo-Cazurra, 2018, p.146).
- 4) Acquiring Capabilities (emerging economy, economic): the fear that home countries will use the firms to extract valuable technologies from host countries (Cuervo-Cazurra, 2018, pp.147-148).
- a. Solution: Barring firms from exporting or extracting technologies (Cuervo-Cazurra, 2018, p.147)
- 5) Weak Governance (emerging economy, political): the fear that substandard institutions and governance practices will encourage unethical behavior and/or crime. (Cuervo-Cazurra, 2018, p.148)
- a. Solution: Monitor the firms strictly for potential signs of unethical behavior (Cuervo-Cazurra, 2018, p.149)
- 6) Status loss (emerging economy, psychological): the fear that firms from emerging economies would enable those economies to surpass that of the host country (or, at least, trigger a relative status loss) (Cuervo-Cazurra, 2018, pp.149-150).
- a. Solution: Limit expansion in cutting-edge fields and sectors (Cuervo-Cazurra, 2018, p.150).

Together with Ka and Xiaojun, this article explains well why the public is likely to have fears regarding Chinese FDI. Mattlin and Rajavuori (2023), on the other hand, illustrate the effect these public perceptions have on regulations. Studying the Nordic region, Mattlin and Rajavuori explore how the public perceptions of Chinese SOEs have ultimately led to Nordic countries adopting a risk management approach to accepting Chinese FDI (Mattlin & Rajavuori, 2023,

p.2). Essentially, the governments of Nordic countries have chosen to legislate in a way so as to reduce the potential risk, despite the lack of evidence that such harms have come to pass.

The goal of the present paper is to determine whether or not Canada has undergone a similar bout of *riskification*, if FDI from Chinese SOEs is rather being securitized, or if the issue has not undergone significant riskification or securitization, and instead remains politicized. Then, I will compare my findings with those of Mattlin and Rajuvuori (2023) and determine how their analysis of FDI controls in the Nordic context will differ from a similar analysis of the Canadian FDI context. The methodology used in this paper will be explored in the next section.

## **Methodology**

The present study is based on that of Mattlin and Rajuvuori (2023). Mattlin and Rajuvuori essentially attempt to combine three theories to explain the causes of shifts in public policy. These theories are 1) riskification, 2) formal epochs, and 3) causal narratives. Each of these phenomena and relevant theories will be explored below.

First, the riskification part of the theory is based on the framework proposed by Olaf Corry (2012). In his article *Securitisation and 'Riskification': Second-order Security and the Politics of Climate Change*, Corry attempts to disentangle the concepts of risk and security, as risk has become a way in which securitization theorists have attempted to explain the expansion of securitization to potential and non-existential threats (Corry, 2012, p.235). Corry explains that there are in fact three ways an issue may be constructed in public discourse. First, a subject may be 'politicized'. This means that the discourse around the subject has not been subject to security or riskification logics (Cory, 2012, p.249). This means that the discourse around the topic is mostly built around marginal utility and little or no concessions are made to mitigate risk or

threat. Second, a subject can be ‘riskified’. Riskification has three core characteristics – a focus on constitutive and ‘permissive’ causes, the possible governance of the conditions of harm, and a more open, transparent, and long-term oriented political environment (Corry, 2012, pp.246-248). In other words, riskification involves the discussion of the potential causes of harm, and the proposal of governance strategies to reduce vulnerability and hedge against risks with a long-term strategy. Securitization, on the other hand, involves the creation of a threat to a valued referent object, (for example, a State), a plan of action in order to deal with said threat, and the creation of an emergency politics scenario where exceptional decisions or measures are undertaken in order to eliminate the threat before it destroys the referent object (Corry, 2012, p.239). In short then, securitization is the creation of a frame that depicts a specific threat as being imminent and particularly dangerous, to the point that it necessitates the deployment of exceptional measures that upend the ‘normal’ political process to protect the referent object.

What separates Corry from his peers is that, rather than considering risk to be an expansion of securitization, Corry demonstrates that the process in which a subject becomes ‘riskified’ (in other words, constructed as being a risk) is a separate process from that of securitization (Corry, 2012, p.235). This is particularly relevant to discussions of State control of FDI from SOEs in emerging economies, as the danger posed by the practice is much more likely to be viewed as a ‘risk’ than a security threat, although it is abundantly clear that the practice is moving away from ‘normal’ politics.

The second building block of the Mattlin-Rajuvuori framework is normative change, and in particular, the punctuated equilibrium model used by Goertz (2003). Simply put, Goertz argues that new norms change rapidly in distinct periods, often in response to external threats (O’Neill, 2004, p.425). Otherwise, norms have a tendency to change in minor ways (O’Neill,

2004, p.425). As the Mattlin-Rajavuori model explains, the regulation and screening of FDI from SOEs in emerging economies is not the result of incremental change, but rather the result of a sudden shift in global perceptions. This shift in perception is characterized as a shift in ‘causal narrative’ (the third building block of the Mattlin-Rajavuori Framework), rather than as being the result of an external shock as theorized by Goertz.

Causal narratives are explored in the most detail by Eliaz and Spiegler (2020). In their article, the authors attempt to explain how narratives play a key role in political decision-making and the public consciousness and their anatomy. Eliaz and Spiegler define causal narratives as specific structures of political discourse that “map consequences onto actions” (Eliaz & Spiegler, 2020, pp.3786-3787). They are essentially used to impose a certain causal interpretation based on perceived correlations. This is particularly relevant to the development of FDI policies as it is clear that such a causal narrative is being used to justify FDI policy regarding SOEs from China, despite the fact that, as mentioned previously, the perceived harms of Chinese FDI are overblown – they are either incredibly minor, or they are accounted for in existing laws and policies (Globerman & Shapiro, 2009, p.180; Du, 2014, p.1159).

To attempt to capture the causal narratives that inspire the creation of policy, I will primarily be conducting a historical review of Canadian economic policy to examine how FDI has been characterized and attempt to identify the “causal narratives” that have inspired the policy decisions of each era.

The Mattlin-Rajavuori Framework is by far the most appropriate analytical tool for the present paper, as it combines three theories that allow for a historical analysis that goes beyond the mere analysis of historical events without context by examining how these historical events fit into the worldviews of the people who experienced them. Rather than merely drawing a

straight line from one historical event to the next, the Mattlin-Rajavuori framework allows us to examine how events played into the popular narrative, which can better explain the actions and decisions of various stakeholders by placing them in a larger context. In other words, looking at narratives and how they gained or lost support following historical events allows us to more clearly understand the historical continuity of economic decision-making. Riskification, itself, is also an incredibly useful concept when examining regulation, as it provides a lens through which we may attempt to determine the extent to which FDI is welcomed, and the extent to which it is sought to be eliminated (with securitization representing a desire to eliminate, normal politics representing a desire to permit without restriction, and riskification representing a desire to limit the potential harm). It also allows us to evaluate the more broad historical trends in FDI policy and, potentially, place the current FDI paradigm in the larger historical context and make predictions for the future.

However, there is some challenge in applying the Mattlin-Rajavuori Framework. First, it is unable to determine the origin of the riskifying rhetoric. While the proposed methodology would easily enable us to determine whether the discourse around FDI from Chinese SOEs (or from foreign enterprise in general) is the result of a causal narrative, it is not able to explain the source of the riskifying rhetoric. It can prove difficult to identify the specific origins of ideas. Even when analyzing historical events, causal links between the sources of riskifying rhetoric, narratives, and the policy outcomes are difficult to identify. As such, it can be difficult to determine if decision-makers succeeded in proliferating their ideas or if they merely adopted a popular narrative as it suited their worldview. Similarly, the proposed methodology makes it more difficult to measure the precise extent to which an issue may be the result of a causal narrative. Indeed, while the literature does not specifically explore the spectrum of influence that

a causal narrative may have on policy decisions, exploring the possibility of such a phenomenon could be quite fruitful and expand the field. However, just like with questions of causality, it will prove difficult to objectively quantify different levels of influence of narratives on outcomes. As such, while it will often be obvious if a narrative played a role in bringing about a specific policy, it will be much less clear if the narrative itself was the primary driver behind the policy adoption or if other factors, such as organizational structure or social systems, played a more important role. Finally, while the goal of the present paper is specifically to examine the shifting narratives around FDI, it will be necessary to dive deeply into Canadian History (likely before FDI was a real topic of discussion) in order to properly understand the origins of these narratives and the contexts through which they evolved and shifted.

## **A History of Foreign Direct Investment in Canada**

### *An Early Balance in Canada – FDI controls in Canada from 1867 to 1930*

Prior to the enactment of the Foreign Investment Review Act (“FIRA”) in 1973, Canada did not have in place any sort of review process of FDI. That said, the “National Policy”, enacted by John A. MacDonald’s Conservative government had an enormous impact on the investment landscape in Canada (Lefebvre, 2022, p.2-3). The National policy had three objectives – 1) to promote immigration, 2) to facilitate the construction of a cross-Canada rail line, and 3) to protect Canadian industry from foreign competition (in particular from the United States and Britain) (Alexander and Keay, 2018, p.1-2). It did this, mainly, by increasing tariffs on imported goods in a relatively targeted manner: products with little domestic production were often spared the high tariffs, while manufactured goods that could compete with Canadian businesses were among the most highly taxed (Alexander and Keay, 2018, p.2). This marked an important point

in the history of Canadian economics, as the National Policy was the first step Canada took down the path of protectionism, a path from which it would not waver for more than a century.

However, while the purpose of this policy was, in part, to protect Canadian industry, it also was quite permissive in letting foreign investors invest in Canadian businesses (Lefebvre, 2022, p.2). This permitted the government to leverage the benefits of FDI while also limiting the capacity of American businesses to undermine Canadian ones. This was in turn, vital for the early Canadian economy, as foreign investment was the driving force behind the construction of Canada's railroads, the development of the Canadian West, and the growth of Canadian exports (Lefebvre, 2022, p.2). This seemingly paradoxical trade policy is perhaps Early Canada's most defining economic policy (Lefebvre, 2022, p.2).

American FDI in Canada would continue to grow well into the late 1920s. American investors would begin to dominate the Canadian market (with over 80% of FDI coming from American Investors), with a particular interest in the manufacturing and mining sectors (Lefebvre, 2022, pp.2-3; Foreign Investment Review Agency, 1970b). The rapid shift from a resource-based economy to an industrial economy combined with the increased prosperity of the citizenry left little doubt in the public imaginary that FDI (in particular FDI from the United States) played a key role in Canada's development (Lefebvre, 2022, p.1-3).

This period in Canadian history would lay the groundwork for the paradigms that would emerge later in Canada. We can clearly see the emergence of two, if not opposed, at least competing views on the role foreign enterprise should play in the Canadian economy. I have dubbed these the "protectionist narrative" and the "openness narrative". The protectionist narrative is one of national interest. At its core, the protectionist narrative holds that it is in the best interests of the government to promote the development of Canadian enterprise and

ownership by impeding foreign business's access to the Canadians through the use of tariffs, and, later, FDI controls. Protectionism is, at its core, about protecting domestic businesses from the competition of international firms who may, at best, disregard the interests of the Canadian government and its citizenry, and, at worst, may pose a direct threat to them. On the other hand, the openness paradigm posits that the benefits brought by foreign investment can bring incredible prosperity to Canada, and as such, overly burdensome regulation may actively harm Canada's economic interests. As such, according to this narrative, the government should ensure that Canada remains as open to foreign investors as possible.

I argue that riskification occurs as a result of a compromise between the two above narratives. Indeed, if securitization is, according to Corry (2012), the use of extreme exceptional policy measures to attempt to eliminate a perceived threat (Corry, 2012, p.239), then securitization (the elimination of foreign competition for domestic enterprise, through whatever measures necessary) appears to be the end goal of the protectionist narrative. Similarly, the openness narrative appears to be an effort to completely downplay the dangers of FDI and foreign trade, which means it corresponds to "normal politics" as defined by Corry (2012). When efforts are made to regulate foreign trade and investment, without banning it entirely, to appease both the protectionists and the liberals, then, it is clear that said effort would be a riskifying endeavour.

Understanding the history and root of these two narratives is vital to understanding the ways in which our perception of FDI is fluid, and specifically how it can change as the result of threat perception. One could easily draw parallels between the perception around investment from the US in Canada's early years and how FDI from China is perceived today: Both countries dwarf Canada economically. Protectionists argue that FDI needs to be reigned in, otherwise

enterprise from the US or China may “invade” Canada and work against its interests. In other words, many of the ideas surrounding FDI from Chinese SOEs are not new, and indeed, are as old as the country of Canada itself. Even if protectionist sentiment has been exacerbated, for instance, by the fact that many of China’s most active investors are SOEs (and so are perceived as political rather than economic entities), this is only a new coat of paint on a foundation that goes back more than a century.

Overall, the National Policy is a clear demonstration that the protectionist narrative dominated Early Canada’s political imaginary. However, the fact that the government refused to bar FDI also speaks volumes about the perceived necessity of attracting foreign investors for the future prosperity of the nation. As such, 1867-1930 is one of the few periods in Canadian History where the protectionist and the openness narratives not only coexisted in their extreme forms – with totally open borders in terms of investments, while being incredibly protectionist in terms of trade. However, history would show that this precarious balance could easily be ruptured.

### *Foreign Direct Investment Controls in the Great Depression and World War 2*

It is not hard to imagine that an economic upheaval as important as the Great Depression would have such an important impact on the causal narratives that informed Canada’s trade policy. However, what is more difficult to understand is how, in a short space of time, Canada’s trade policy would reverse itself completely and go from more protectionist to more open in the space of a few years.

The Great Depression hit Canada particularly hard. The average price of exported goods dropped by 40%, Canadian businesses could no longer rely on American demand, and FDI plummeted dramatically (Lefebvre, 2022, p.4). In response to these shifts largely outside of

Canadian control, Canadians demanded that the government put into place protections to prevent their Industry from falling victim to similar external changes in the future. This popular movement, largely driven by civil society groups and trade unions, would ultimately have the opposite effect, for two important reasons. First, it was also feared to be a socialist or communist movement by the political elite (Lefebvre, 2022, p.4). As such, policymakers devoted themselves to finding solutions to market volatility within the capitalist framework and would ultimately land on market openness. Second, and perhaps more importantly, the attempts of the Conservative Party of the period under R.B. Bennett to use tariffs to revive the Canadian economy ended up doing more harm than good. This in turn would severely damage the perceived viability of protectionist policies in the eyes of the public (O'Brien and McDonald, 2009, p.332).

Bennett ran on an extremely protectionist platform. He routinely promised to increase tariffs on manufactured goods while also using the same tariffs as bargaining chips to expand Canadian businesses access to foreign markets (and, in particular, the markets of Great Britain and other British colonies) (O'Brien and McDonald, 2009, p.333). In 1933, however, less than two years after his election, Bennett entered negotiations with the United States to reciprocally reduce the very same tariffs (O'Brien and McDonald, 2009, p.351). The reason for this dramatic shift in economic policy was simple – Bennett failed to build sufficiently strong intra-imperial trade ties to replace trade with the United States, and, overall, failed to deliver on his promises of economic recovery (O'Brien and McDonald, 2009, pp. 332-334). This policy failed because the two pillars of Bennett's policy (reducing imports, especially from the US, and increasing exports and trade with the British Empire) were simply put, impossible to implement, and, to a certain extent, completely contradictory – attempting to protect local manufacturing while also working

to increase trade ties with largely export-based economies is, at its face, counterproductive (O'Brien and McDonald, 2009, p.336). Bennett's position was met with disbelief by British decision-makers: "Bennett's attempt to walk the fine line of encouraging empire trade while rejecting empire free trade ended up alternately baffling and enraging British politicians. This remained the case throughout Bennett's term in office." (O'Brien and McDonald, 2009, p.339).

Obviously, Bennett's balancing exercise attempting to expand exports to Britain while also refusing to make concessions that may harm Canadian enterprise was doomed to failure. But how, then, did this policy failure lead to a significant push for more openness in trade? Simply put, when Bennett failed to build sufficiently strong trade ties with the United Kingdom to offset the damage done by the precipitous drop in exports to the United States, he was forced to come back to the negotiating table with Washington just a few short years after his election (O'Brien and McDonald, 2009, p.351). This was clearly seen as a failure of protectionism at the time (O'Brien and McDonald, 2009, p.360). The fact that Mackenzie King dominated the conservatives in the 1935 election would only put the final nail in the coffin of protectionism in Canada – it would be seen as political suicide to attempt to resuscitate Bennett's policies (O'Brien and McDonald, 2009, p.360). The beginning of King's third term, then, marked the beginning of an era where the openness narrative began to creep back in and completely dominate the political discourse, perhaps best exemplified by the 1938 agreement signed by his government with the United States to promote bilateral trade (Lefebvre, 2022, p.5). While this would appear to indicate that the government would move away from economic intervention, the events of the Second World War would prove that, despite the advent of trade liberalization, Canada's government would continue to intervene in the domestic market – although, as we will see, it began to do so for different reasons.

During the Second World War, Canadian industry expanded massively due to State intervention largely overseen by C.D. Howe (Lefebvre, 2022, p.5). Howe is a particularly important figure in Canadian economic history for pioneering a much more active approach to economic governance (Nerbas, 2013, p.203). Indeed, whereas previously, laissez-faire and liberal economic policies had been the norm in Canada, the economic coordination required by the war effort forced the government to take a more active role in the economy (Nerbas, 2013, p.226). While this shift from a free-market economy to a more mixed economy was meant to be temporary, the success of the interventionist policies implemented during the war inspired Howe, now the minister of reconstruction, to continue to intervene in the economy to correct market deficiencies (Nerbas, 2013, pp.232).

This change in government policy speaks to another set of competing narratives at the heart of Canadian economic policy decision-making – the “free-market narrative” and the “interventionist narrative”. Essentially, before this period, completely unhindered economic expansion was the driving force behind much of the exponential growth behind the Canadian economy (Nerbas, 2013, p.6). As such, any form of State intervention in domestic markets would be seen as damaging to the economy. This is the basis of the free-market narrative. However, as early as the 1920s, this vision of the role of the government in the Canadian economy began to crack (Nerbas, 2013, p.6). As such, the government found it necessary to begin to intervene in the economy in order to address market deficiencies (Nerbas, 2013, p.6). These narratives are vital to understanding the debate around contemporary FDI from China, where many argue that FDI from Chinese enterprise should be more heavily regulated and academics argue that the risk that regulation may hinder Canada’s future economic growth.

The narratives that accompanied the free trade liberalization of the Great Depression era and the interventionism that rose to prominence during the Second World War both represented significant shifts in the political discourse around government intervention in the economy. However, it is important to highlight the fact that these two narratives are contradictory. The openness narrative that rose in the later years of the Great Depression rose as a repudiation of the idea that governments should intervene in international trade, as protectionist policies were shown to have been completely insufficient to reverse the economic woes of the period. The benefits of free exchange, unimpeded by governments, were made clear to all. On the other hand, on the domestic level, it was shown that government intervention can fine-tune markets and lead to better outcomes for all parties. While these narratives are not irreconcilable, there is a clear tension between the two narratives – particularly focused on the role of government: should governments intervene in the economy? Or should the government instead leave the market to its own devices to ensure maximum efficiency? This tension would contribute to the first real debate on Foreign Direct Investment in Canadian History, a debate whose echoes can still be seen in contemporary debates around FDI.

#### *1945-1963 – the Rise of Nationalist FDI policies*

In the early postwar years, Canada completely gave up its research and development capacities developed over the course of the war (Smardon, 2014, p.82-83). The reason for this change was that foreign investors were seen as having much greater technological capacities, and, while Canada could theoretically invest in creating its own R&D capacities, this would have been far less profitable than investment from abroad, and the US especially (Smardon, 2014, p.82-83). In other words, the openness narrative completely supplanted the protectionist narrative when it came to FDI in this period because investment flows from the US were booming. FDI,

according to the openness narrative, would be key in furthering Canadian Economic development (Lefebvre, 2022, p.6). Howe, now the Minister of Reconstruction, was focused on using the state tools developed during the war to boost exports across the economy, and neither he nor the government of the time cared much about the ownership of manufacturers, so long as they respected the government's policy positions and laws (Lefebvre, 2022, p.6).

As a result of this political stance, investment in Canada from American firms skyrocketed (Lefebvre, 2022, p.6). These investors were primarily focused on the manufacturing and energy industries (Foreign Investment Review Agency, 1970a, p.i). By the mid-fifties, however, a new narrative would emerge, where the notion that foreign investors should be able to invest in Canada as they please would be challenged. Indeed, in response to the sharp rise in investment from American firms and exacerbated by the fact that the 1950s boom was not accompanied by an increase in GDP per capita among the Canadian population, Canadians began to question the wisdom of letting foreign enterprise control strategic sectors of the Canadian economy (Lefebvre, 2022, p.8). Indeed, some feared that, should the government refuse to put measures into place to protect Canadian enterprise, then the domestic ownership of firms would plummet, and the owners of said enterprises would use Canada's resources to further their own home country's interests rather than those of Canada (Lefebvre, 2022, p.8). As is perhaps evident, this represented a resurgence of the protectionist narrative, albeit in a different context. Whereas previously, the protectionist narrative had been primarily focused on protecting Canadian businesses from foreign competition, by the mid-fifties, the narrative had adapted. Now, the biggest threat to Canadian business was not foreign competition – as the recent triumph of the openness narrative had shown, the benefits of free trade outweighed the dangers. The biggest threat to Canadian business was in fact the threat of foreign ownership and the control

that foreign businesses could exercise over the economy for their own interest, without regard to the best interests of Canada. This rose to a fever pitch in 1954 as Statistics Canada revealed that foreign ownership of Canada's mining, oil, and manufacturing skyrocketed, while, on the other hand, stories of American-owned businesses that completely disregarded the damage they were doing to their communities became increasingly common (Lefebvre, 2022, pp.8-9; Azzi, 1999, p.44). Azzi (1999) argues that the fall of McCarthyism also played an enormous role, in that it demonstrated quite clearly to the Canadian public that the agendas of the U.S. decision-makers were not always benevolent (Azzi, 1999, pp.35-36).

Seeing their government's inaction, despite the fact that the government had begun to participate more actively in markets to correct deficiencies, Canadians began to feel immensely frustrated with the state of things (Lefebvre, 2022, p.9). As a result, political pressure on the government to do something about the dominance of American firms in the domestic market and otherwise reduce Canada's dependence on their southern neighbors. In light of this building pressure, Howe recommended to American investors a number of criteria that they should take into account when investing in Canada: 1) provide opportunities for Canadians to become minority shareholders, 2) provide Canadian employees with an opportunity for advancement, 3) to be transparent about their activities and publish more on the same, and 4) enable Canadian subsidiary plants to increase their exports (Lefebvre, 2022, p.9).

However, this move would not prove sufficient to alleviate the pressure on the Liberal government and, facing increasing pressure from the opposition and his own ministers, Prime Minister Louis St-Laurent created the *Royal Commission on Canada's Economic Prospects* (the "Gordon Commission") (Lefebvre, 2022, p.9). Walter Gordon, the head of the commission, was perhaps the most prominent critic of the role the United States played in Canadian politics, if not

on the global stage. Having sent a draft article in which Gordon proposed the creation of such a commission to the finance minister in 1955, it is perhaps unsurprising that he was chosen as the Commission's chair (Azzi, 1999, p.38).

While the stated goal of the report was to provide an overview of the Canadian economy as a whole and identify the challenges the country will face in the near future, for Gordon, FDI and tariffs were the focus of the analysis (Azzi, 1999, p.40). Indeed, while Gordon would exaggerate the extent to which the average Canadian citizen was against FDI, he heard testimony from quite vocal critics of Canada's lack of FDI controls (Azzi, 1999, p.42). These critics were professional organizations, investment dealers, and organized labor, with the two former fearing the impact of American ownership on their respective industries (Azzi, 1999, p.42). Trade unions, however, were the most vocal critics of FDI investment, primarily concerned with the impact of FDI from the states on their workers and job market (Azzi, 1999, p.42). However, for the labor movement, another narrative was emerging:

*The struggle between labor and capital had become a conflict between Canadian and American interests. When owners made decisions that did not benefit workers, union members often ignored the obvious profit motive, alleging that these decisions were made for reasons of nationality. (Azzi, 1999, p.42).*

What we see here then, is the beginning of a shift in the narrative of US and Canada relations, where the openness narrative would, to many, begin to be laced with imperial undertones. When the hearings of the commission ended in 1956, the issue of foreign ownership of Canadian enterprise rose to the forefront of the public debate (Azzi, 1999, p.43). Commentators would largely reproduce this new "US imperial narrative" and even go so far as to frame FDI from the US as being an "invasion" (Azzi, 1999, p.43). Politicians followed suit, and whereas the issue of foreign ownership of enterprise had hardly been the subject of discussion, by 1956, it became a common topic of discussion (Azzi, 1999, p. 43). In response to this perceived increase in the role

of American interests in Canadian business decisions, many began to clamor for Canadian economic independence (Azzi, 1999, p.43). This shift in the narrative would be one of the primary impacts of the Gordon Report.

Against many of the Commissioners' wishes, Gordon decided to publish a preliminary report in January 1957 (Azzi, 1999, p.51). Curiously, the Commission found that there was little evidence that foreign-owned enterprises operated in a manner contrary to the Canadian interest (Azzi, 1999, p.52). Despite this, the report indicated that FDI could become a problem in the future and recommended that the government put into place "mild legislation to limit foreign investment, not because it had found any problems with foreign ownership but to prevent a future demand for more extreme measures" (Azzi, 1999, p.52). The report also made three recommendations to foreign-controlled businesses:

- a) Wherever possible, they should employ Canadians in senior management and technical positions, should retain Canadian engineering and other professional and service personnel, and should do their purchasing of supplies, materials and equipment in this country.*
- (b) They should publish their financial statements and make full disclosure therein of their Canadian operations.*
- (c) The larger Canadian subsidiaries should sell an appreciable interest (perhaps 20% to 25%) in their equity stock to Canadian investors and should include on their boards of directors a number of independent Canadians.* (Azzi, 1999, p.52).

To achieve these goals, the commission recommended the government use tax incentives (Azzi, 1999, p.52). It is important to note that Gordon sought to use tax incentives as, in his view, FDI was not to be controlled, but rather, to be reduced significantly (Azzi, 1999, p.49). In Gordon's eyes, foreign-owned firms were fundamentally different from Canadian-owned firms because of their nationality, and not because of the changes to the profit motive (Azzi, 1999, p.49).

Many of the ideas in the Gordon Commission's report are similar to popular ideas around Chinese FDI today. For instance, while research has consistently shown that new legislation and stricter criteria are not necessary to promote responsible investment in Canada, the federal government has consistently moved to apply regulation more strictly to SOE activity in Canada to prevent them from working against the national interest.

Whereas economists sharply criticized the preliminary report, primarily because the suggested solution would do next to nothing to change the behavior of foreign-controlled enterprise or strengthen the grip of Canadians on domestic firms, support from the public and the press was more nuanced (Azzi, 1999, pp.53-57). Some newspapers praised the recommendations on foreign ownership, while others wrote that the minimum 25% ownership clause would only further the interests of Canadian investors and do little to protect the national interest (Azzi, 1999, p.55). Politicians similarly argued that the preliminary report failed to present its arguments convincingly, and only succeeded in provoking discussion (Azzi, 1999, p.57). Finally, and perhaps most damningly, many of the researchers who contributed to the commission felt that the preliminary report did not reflect their work and instead focused on restating Gordon's preconceived conclusions (Azzi, 1999, p.57). There would be some truth to this claim, as John H. Young's analysis of the cost of tariffs to the Canadian economy was contested in the final version of the very report it appeared in, although Gordon would not directly intervene in the findings of the research (Azzi, 1999, p.61).

Despite the criticism surrounding the interim report, it succeeded in perpetuating the US imperial narrative and in particular gave many Canadians the impression that something was fundamentally wrong with the way foreign investments were regulated, while the Liberal government of the era appeared to refuse to do anything about it (Azzi, 1999, p.57). Taking into

account the earlier-mentioned undermining of the US benevolence narrative due to the perpetuation of McCarthyism, (exacerbated by the suicide of Herbert Norman, a Canadian Diplomat that was widely seen as having been caused by accusations of communism against him from the US), Canadians were more than ready to reexamine the role their southern neighbor played in their politics and, more importantly, their economy, - to the point that Canada- US relations became the central focus of the 1957 election, where John Diefenbaker would win, in part due to his appeal to anti-American sentiment (Azzi, 1999, p.58). The final report was released in May of 1958, to much less media and political attention than the interim report had, largely due to the report largely containing the same conclusions as the interim report (Azzi, 1999, p.63).

Overall, despite its many flaws, the Gordon Commission report was vital to the development of FDI policy in Canada. It succeeded in perpetuating the idea that American business interests were “invading” Canada to take control of its resources to further their own interests without regard to those of Canada and gave that argument an institutional legitimacy (Azzi, 1999, p.64). This idea clearly lives on today, as is seen in the way the discussion surrounding FDI from China is framed. Even more importantly, it crystallized the vague anti-American sentiment that had grown in the postwar era into specific policy concerns that the new conservative government would capitalize on for political gain (Azzi, 1999, p.58). Diefenbaker’s government would have a vital impact on FDI controls after their election.

As a Prime Minister running on a nationalist platform, it is important to discuss the role Diefenbaker played in cementing the US imperialist narrative within Canadian discourse. Simply put, Diefenbaker saw Canada as being far too reliant on the US economically and sought to diversify trade to reduce the risks that such dependency would entail (McKercher, 2011, p.1045).

That said, Diefenbaker was not anti-American, and indeed, he recognized that it was vital to keep American-Canadian Relations in good repair (McKercher, 2011, pp.1046-1047). Of course, this tension often put the Diefenbaker government in a difficult political position (McKercher, 2011, pp.1046-1047). In the end, while Diefenbaker's election did signal a rise in Canadian nationalism and anti-American sentiment, his government was often unwilling or unable to implement any meaningful policies (McKercher, 2011, p.1059-1060). By the end of his term in 1963, Diefenbaker still sought to create an environment conducive to FDI in Canada while attempting to support Canadian subsidiaries in order to increase the role they play in business decision-making and attempting to increase research on technical capacities in Canada (Lefebvre, 2022, p.12). However, the growing concerns with FDI in Canada would have to be addressed by successive liberal governments.

#### *Lester B. Pearson 1963-1968*

When in 1963 Lester B. Pearson's Liberal government replaced Diefenbaker's Conservative one, it appeared as though the government would attempt to return the US benevolence narrative to its former position of prominence. Indeed, in his first Speech from the Throne, Pearson would attempt to explain Canada's growth with its openness to trade and foreign investment (Lefebvre, 2022, p.12). However, in part due to the support he provided to the Liberal campaign (indeed, it was argued that without his support, Pearson would not have been elected), Pearson chose to appoint Gordon as Minister of Finance (Azzi, 1999, p.92). Still adamant that his views on foreign investment were correct, Gordon was committed to reducing the scale of American FDI in Canada, even if he had failed to garner support in his party or among the population for such a move (Azzi, 1999, pp. 93, 99, 102).

When Gordon presented his budget, he essentially reiterated some of the findings of the 1958 report under his name while also attempting to remain consistent with Liberal policies. Gordon explained how, while the government was open to foreign capital, it would only be welcomed if it established new enterprises as opposed to taking over Canadian businesses, as Gordon did not believe that takeovers added any value to the Canadian economy (Azzi, 1999, p.103). In light of this, he established a 30% tax on foreign takeovers of Canadian enterprises (Azzi, 1999, p.99; Lefebvre, 2022, p.13). He also strongly believed that foreign enterprises doing business in Canada should be at least 25% controlled by Canadians so as to guarantee that Canadian's viewpoints would be heard when business decisions are being made (Azzi, 1999, p.103). In light of this, he lowered taxes on dividends from firms with at least one-quarter Canadian ownership and raised them for firms with a lower percentage of ownership (Azzi, 1999, pp. 99-100).

Similar to his Commission's report released 5 years prior, the overall reaction to Gordon's budget speech was quite mixed. Some newspapers praised the measures to protect Canadian businesses from foreign acquisition, while others argued the policies would prove ineffective (as there was no attempt to boost the creation of Canadian capital) or impractical (as companies do not always verify the country of origin of their investors) (Azzi, 1999, p.104). Politically, the Opposition focused on the relationship between the contractors Gordon retained to draft the federal budget, rather than on substantive issues (Azzi, 1999, p.105). However, critics from within industry were particularly vicious. The board of the Montreal Stock Exchange, for instance, met with Gordon and attempted to demonstrate the absurdity of his policies, and in particular, the 30% takeover tax (Azzi, 1999, pp. 105-106). The board argued that the tax actively hurt the Canadian economy as it acted as a significant to takeovers, which brought with

them new technologies, ideas, and resources that would otherwise be unavailable in Canada (Azzi, 1999, p.106). Finally, the board indicated that they would sell the markets short if the measures went forward (Azzi, 1999, p.106). Similarly, the Canadian Chamber of Commerce argued that openness and trade contributed significantly to economic growth and that the government was overstepping its bounds in the economic landscape to the point it would hurt the economy (Lefebvre, 2022, p.13). As a result of this criticism, Gordon repealed the takeover tax, a political failure which would ultimately snowball and end up severely hampering Gordon's position in government, politics, and the business community (Azzi, 1999, pp.106-109). This failure would cripple the ability of the supporters of the US imperialism narrative to propose any sort of policies that did not conform to the openness narrative until political circumstances changed (Azzi, 1999, p.110).

The move back to relative trade openness was perhaps made most evident with the implementation of the Auto Pact with the United States. In the early 60s, the Canadian automobile industry was in dire straits – as Japan and Western Europe developed and started breaking into the automobile industry, Canada largely lost its competitive advantage in the global market (Smardon, 2014, p.90). Even worse, Canada's automobile industry, due to its protection from competition by tariffs, suffered from significant inefficiencies – for example, short production runs in Canada made it so that prices in Canada were higher despite significantly lower wages for workers than in the US, and the gap was increasing (Thomas, 1997, p.129).

In light of this, the Canadian and American companies sought to overcome trade barriers and attempted to create a single North American automobile market (Thomas, 1997, p.127). However, at the negotiating table, Canada emphatically refused to implement any sort of plan that did not include production guarantees to ensure Canadian auto manufacturing would not be

left behind (Thomas, 1997, p. 135). It put into place requirements that Canadian industry would be a key part of the supply chain to the extent that American cars are purchased in Canada (Brunelle & Deblock, 1989, p.89). However, while Canada did increase its share of production in the new continental market, the factories and parts manufacturers became increasingly controlled by American enterprises (Thomas, 1997, p.143).

Up until this point then, Pearson's government had two important impacts on the narrative of FDI from the US. First, the 1963 debacle surrounding Gordon's budget and the loud criticism it inspired would seriously impact the legitimacy of the US imperialism narrative. Second, the integration of the Canadian and US auto markets substantially increased the number of American firms operating in Canada, while also placing Canada at a particular position in the supply chain. While the US imperialist narrative would be tamed for now, it was clear that the political climate was ripe for change – it would merely take an inciting event to precipitate a push for regulation of foreign ownership of enterprise.

#### *Trudeau and FDI controls – A push for a Canadian-oriented economy 1968-1985*

Elected in 1968 as a left-wing candidate who believed strongly in Government interventionism, Pierre-Elliott Trudeau was one of the most influential Canadian prime ministers of all time. In the context of a history of FDI controls, Trudeau represents a pivotal transition, in that, by enacting the Foreign Investment Review Act ("FIRA"), he managed to reconcile the interventionist and openness narratives in a way that has fundamentally altered the way in which Canada views FDI to this day.

The first step towards this shift was the Watkins Report of 1968, which reiterated the concerns with FDI brought up by Gordon in his own report and gave new life to the US

imperialist narrative. As Watkins would write, he felt it was time to implement a “New National Policy” in order to guarantee Canadian economic independence and reduce the risk of harm from too much American investment (Watkins, 2006, pp.117 – 118). The Report had two primary conclusions – 1) Canada’s industry had developed in a way that made it so it was merely a mini version of the American economy while also being less successful and 2) “plurinational enterprise” would become the primary economic actor and Canada would need to consider the impacts of this fact, including their potential oligopolistic power and the potential benefits their investment may bring (Lefebvre, 2022, p.15). To implement these recommendations, the report recommended that the government take a more active role in regulating FDI, in particular, by more strictly enforcing compliance with national policy objectives and enacting policies that seek to protect the national interest, increase the participation of Canadian businesses, and help improve Canadian business performance (Lefebvre, 2022, p.15). The Watkins report also recommended further study into the impacts and role of FDI in Canada (Aivalis, 2018, p.89).

The Wahn report or would be the first report to really expand on Watkin’s position, arguing that Canada risked losing its independence entirely if it did not reign in foreign ownership, due to the control the American government exercised over their businesses (Lefebvre, 2022, p.17). This report also built on many of Watkin’s ideas and suggested the creation of the Canadian Development Corporation (“CDC”) to boost local enterprise, a recommendation that would become reality in 1971 (Lefebvre, 2022, p.18).

However, perhaps the clear and impactful report on the FDI debate of the period was the Gray Report (Fayerweather, 1973, p.3). Simply put, like the reports that preceded it, the Gray Report attempted to frame the FDI debate as a balancing exercise between the benefits of FDI and the ability of Canada to control its own economy (Fayerweather, 1973, p.137). What makes

the Gray Report stand out, however, is its recommendation that the government screen all new investments in Canada (Fayerweather, 1973, p. 142). This proposition is significant in that it signifies the reconciliation of the interventionist and openness narratives that have been in tension for decades at this point. By using the power of government to rectify the market deficiencies and limit the control of American interests in the economy, it was now believed that government could reap the benefits of FDI while continuing to benefit from the incredible growth they had seen in the past decades (Fayerweather, 1973, p.137).

In the wake of these reports, it became clear to decision-makers that Canada could not in fact continue to accept extreme positions. On the contrary, it became clear that, although FDI had played a key role in Canada's development and still provided an incredible opportunity for growth, these advantages had to be weighed against the risks to Canada's economic and political autonomy (Aivalis, 2018, p.89). For Trudeau, this did not represent so much a "nationalist" realization (as nationalism was to him a very emotional and tautological emotion), as much as a logical conclusion focused on the betterment of the individuals within the nation (Aivalis, 2018, p.90). That said, considering the growth of nationalist sentiment in this period, the move did allow Trudeau to appeal to the nationalistic base and increase his electoral prospects (Fayerweather, 1973, p.137). In response to these recommendations and emboldened by a number of United Nations Declarations on the right of nations to maintain control over their natural resources (Voghel, 1979, pp.153-154) the Trudeau government enacted FIRA in December of 1973 (Bonney, 1975, p.83).

According to subsection 2(1), the purpose of FIRA was to enable the government to review proposed foreign takeovers to ensure that they were of "significant benefit to Canada" (World Trade Organization, 1983, p.2). Note that FIRA would only apply to foreign takeovers –

other forms of FDI were not required to be reviewed (Voghel, 1979, p.145). While, at its face, this would seem to imply that the government sought to prevent overseas investors from investing in Canada, the Trudeau government of the time was emphatic that this was not the goal (Bonney, 1975, p.84; Aivalis, 2018, p.91). Indeed, the government asserted that it merely wanted to ensure that any foreign investor would have to consider their impact on the Canadian economy and citizens (World Trade Organization, 1983, p.2). To do this, the law set out five factors to aid regulators in determining if an acquisition is of significant benefit to Canada: 1) the effect of the acquisition on Canadian economic activity, 2) the degree of significance of the participation of Canadians in the business, 3) the effect of the acquisition (or establishment) of the business on innovation, technological advancement, productivity, and product variety in Canada, 4) the effect of the acquisition or establishment on competition, and 5) the compatibility of the acquisition or establishment with the stated policy objectives of the government or the provinces (World Trade Organization, 1983, p.2).

Naturally, FIRA was widely criticized. The way in which the law was written was argued to have given too much latitude to the government to decide how to apply the listed criteria. As such, the way in which different governments could apply the criteria could vary wildly, making investment review difficult, if not impossible to predict, and the final decision is impossible to appeal (Bonney, 1975, p.84). Even worse, researchers have consistently found that FIRA was ineffective (Aivalis, 2018, p.91). Historians and political scientists today tend to see FIRA not as a regulation seeking to meaningfully curb international investment or change its shape – it was merely meant to meet a political need, and, in this case, the political demand for more controls over FDI in Canada (Aivalis, 2018, p.91). Indeed, this is perhaps best shown by the fact that FIRA only applied to foreign takeovers and later the establishment of new businesses, which

represented roughly 20% of all FDI in Canada (Voghel, 1979, pp.145-146). To Trudeau and his government, there was no economic need for the government to intervene in the economy (Aivalis, 2018, p.91).

However, regardless of its failings, FIRA represents an important turning point in the history of FDI. Specifically, not only was it the culmination of the reconciliation of the openness and interventionist narratives (as mentioned previously), but also was the birth of the most important criteria for determining what constitutes “good” and “bad” FDI - the extent to which the investment is in the national interest (Lefebvre, 2022, p.20). Not only would this model of foreign investment control based on the national interest become central to Canada’s FDI regime, even after FIRA, but it also represented a new idea about the responsibilities of businesses towards their host country and would completely reshape the relationships between foreign enterprise and government (Voghel, 1979, p.151).

This new relationship closely represents the riskification framework proposed by Corry (2012). Corry argues that there are three core characteristics of a riskified phenomenon – a focus on the constitutive and permissive causes of harm, the governance of the conditions of harm and a more open and long-term oriented political environment (Corry, 2012, pp.246-248). We see that the Federal Government had, in this case through FIRA, replicated the first two of these characteristics. The permissive causes in this case are evident – the fact that foreign business would often focus solely on the profit motive without regard to the impact they might have on the Canadian economy or Canadian sovereignty. The government would attempt to manage these permissive causes by screening FDI and ensuring all investors take into account their impact on Canada by proving a significant benefit to the economy. However, regarding the long-term oriented political environment and openness of discussion, this was clearly less present under

FIRA. Indeed, as mentioned previously, FIRA enabled the government to unilaterally make decisions on the legality of investments, and indeed often focused on the short term benefits to the economy without regarding the long term benefits an acquisition might bring (Bonney, 1975). As such, to a certain extent, FIRA also has some characteristics of securitization in that debate regarding individual acquisitions was often limited. That said, overall, the topic of FDI was widely disputed in parliament and by commentators, and so it would be a stretch to say that FIRA represented a securitization of FDI.

FIRA is important then, as it represents the first instance in which FDI would become riskified as opposed to merely being discussed as a normal political topic. In the mid to late 70s, however, Canada would once again endure an economic crisis that would temporarily offset this new philosophy.

The late 70s were characterized by a high inflation rate and high unemployment (Lefebvre, 2022, p.21; Voghel, 1979, pp.149-150). As a result of this economic shift, the government faced significant pressure, as further FDI was seen as an effective way to reverse these economic trends by the population and by policymakers (Lefebvre, 2022, p.22; Voghel, 1979, pp.149-150). However, in the wake of these liberalizing trends, the fear of an oil shortage and a broader debate on natural resource allocation, which would temporarily offset these trends.

After their 1980 re-election, Trudeau's government prioritized the development of an industrial policy that would focus on supporting Canadian energy companies. This was spurred by a decline in the level of control exercised by oil Multi-National Corporations ("MNCs") following a perceived strengthening of the Organization of Petroleum Exporting Countries ("OPEC") (Fossum, 1997, p.118). Trudeau would reveal this National Energy Program (the "NEP") in October of 1980. Simply put, the NEP has three objectives:

*1) to provide for energy security, meaning greater Canadian self-sufficiency in oil and less dependence on the world market; 2) to establish fairness in pricing and revenue sharing, which translated into a much lower consumer price for domestic crude than foreign oil and a larger haul of energy revenues for the federal government; and 3) to increase opportunities for Canadian participation in the oil industry, meaning more Canadian ownership of an industry that at the time was more than 70 percent foreign-owned (Jenkins, 1986, p.143).*

In short, then, the purpose of the NEP was to ensure Canadian energy self-sufficiency, to “Canadianize” the energy sector, and to ensure that the federal government received a fair share of the profits from oil and gas development (Fossum, 1997, pp.118-129). The main mechanism put into place to support the Canadianization objective was the Petroleum Incentive Program (“PIP”), which was a grant-based program where the size of payments depended on the extent to which the company was owned and controlled by Canadians, the location of the energy activity, the type of energy activity (ie, exploration, development, or eligible assets) and the year in which the expenses were incurred (Fossum, 1997, p.138). The government also enacted a new land management system in the areas of the country it exercised control (the “Canada Lands”) which better enabled it to exercise control over the nationality of the companies that sought to procure land licenses for exploration or development (Fossum, 1997, pp. 142-143). Of course, the purpose of the NEP was not only to ensure Canadian control of the oil sector, but more specifically, to increase the control of the federal government on the development of Canada’s oil and gas sector (Fossum, 1997, p.146).

Both FIRA and the NEP represent significant departures from previous policies in that they both signaled a shift in the narrative surrounding FDI and the role of the state in the economy. Before Trudeau’s election, Canada’s policy regarding FDI was largely liberal – while there were fears of American MNCs controlling Canada’s economy through their investments, proponents of the US imperial narrative would lack the political capital to enact meaningful

policies. However, with both FIRA and the NEP, the government demonstrated a willingness to directly intervene in the economy to guarantee its continued control over its industry. This clearly represents a renewal of the interventionist narrative, where the government can be seen as an actor who not only can but must take steps to redress market deficiencies limit negative externalities, and increase positive ones. That is not to say that foreign enterprise was not welcome in Canada, however. The government specifically stated that FIRA was not designed to completely remove FDI from the Canadian economy – but rather, it was designed to ensure that the Canadian economy would remain in the control of Canadians. The NEP, on the other, while at first glance appearing hostile to FDI, was more of a measure aimed at promoting the presence of Canadian SOEs in the oil sector, and indeed, it was possible for Foreign-owned companies to retain significant control over developments (Fossum, 1997, p.143). As a result, it is also clear that the openness narrative remained intact, and it was clear to many that market liberalization and the removal of trade barriers had a significant positive impact on the economy. This era instead heralded a more conscious effort to balance the interests of Canadians with those same economic benefits. That said, the perceived protectionist bent of FIRA and the NEP would begin to plant the seed of a policy reversal that would flower in the wake of neoliberalism.

### *The Rise of Neoliberalism – 1985-2008*

The seeds of liberalization already having been planted after the advent of the NEP and the economic woes of the late 70s, economic conservatism and more liberal economic policies were being more openly pushed by advocates and stakeholders, who tried to demonstrate the importance of business to the Canadian economy (Lefebvre, 2022, p.27). Academics also began to push for further liberalization in light of the economic benefits a more open FDI landscape would bring (Lefebvre, 2022, p.27). This, coupled with the worsening Canadian economy, would

set the stage for a new leader to emerge, one that would reverse the course of interventionism that has been dominating the political scene up to this point – Brian Mulroney.

Mulroney made job creation the focus of his electoral campaign, and argued the best way to create jobs was to dismantle FIRA and the NEP, while otherwise creating incentives for more foreign enterprise to invest in the country (Waddel, 2007, p.20). Indeed, during this time, Canada was placed last among industrialized nations in terms of attractiveness to investors (Lefebvre, 2022, p.28). This messaging resonated with the voters so that he would win the first conservative majority government in decades, and indeed the largest electoral victory the nation had ever seen (Blake, 2007, p.3).

As the first step in their plan to revitalize the investment landscape in Canada, the Mulroney government enacted the Investment Canada Act (“ICA”). The ICA was enacted to replace FIRA as the law that would regulate FDI in Canada, and indeed, contained many of the same ideas as its predecessor (Frigon, 2011, pp.1-2). However, the ICA was also intended to make Canada a much more welcoming destination for businesses by narrowing types of investments it can review and lowering its “significant benefit to Canada” test to a “net benefit” test (Frigon, 2011, pp.1-2). Under the ICA, investments were placed under one of two categories – Reviewable Investments and Investments Subject to notification (Frigon, 2011, p.2). Reviewable Investments are essentially investments made by non-Canadians that either acquires a Canadian business (or a sufficiently large MNC doing business in Canada) or creates a new business (Evans, 1987, p.90). All other investments are merely subject to notification (Evans, 1987, p.87).

We can clearly see here that many of the ideas behind FIRA are still present – however, the number of applications that can be reviewed is greatly diminished. Similarly, the organisation

that would replace the Foreign Investment Review Agency (the organization that regulated FDI under FIRA), *Investment Canada*, would have in its mandate not only a responsibility to regulate investment but also, to facilitate it (Lefebvre, 2022, p.28).

While the Mulroney Government appeared to have completely replace the FIRA era interventionism with a full liberalism, it is important to understand that the fears surrounding foreign control and the US imperialism narrative never really went away, and would continue to be the subject of numerous parliamentary debates (Lefebvre, 2022, p.29). Liberals and New Democrats alike both criticized the ICA for failing to sufficiently regulate FDI in Canada (Lefebvre, 2022, p.29). Indeed, the ICA would not refuse to approve any foreign investments until 2008, leading many to refer to the ICA as a “paper tiger” (Collins, 2011, p.153).

In the early 1990s, a number of economic reports indicated that Canada was no longer a competitive economy – a notion in part inspired by the flight of manufacturing jobs that took place in the 80s and 90s (Lefebvre, 2022, p.30). The Mulroney Government was quick to adopt this narrative – in his speech to the throne in 1991, Mulroney explicitly tied the economic woes being experienced to Canada’s failure to promote a globally competitive economy (Lefebvre, 2022, p.30). The proposed solution for this problem was to develop the Canadian economy to once more become an attractive destination for investors (Lefebvre, 2022, p.31). Both the Mulroney and Chrétien governments would continue this trend, and continue to develop policies that sought to attract foreign enterprise to Canada by making the Canadian economy as competitive as possible, by, for example, promoting the development of human capital and supporting the creation of private-public sector relationships to promote innovation (Lefebvre, 2022, p.31).

The Mulroney government (and to a lesser extent, Jean Chrétien's government) then, played an important role in the history of FDI regulation in Canada for two reasons. First, the replacement of FIRA by the ICA represented a significant shift in public perceptions towards the liberalization and openness narratives, offsetting much of the progress towards a more interventionist state narrative that had been accomplished in the past decades. That is not to say, however, that Mulroney's government completely reverted the changes brought to Canada's investment landscape in the past decades – indeed, the ICA does, at least on the surface, represent a real way the government could have limited the expansion of FDI in the economy. However, the moves taken by the Mulroney government do represent an important shift in the narrative surrounding FDI, where the fears of foreign subjugation were seen to be overblown and worth less consideration than the economic benefits that liberalization would bring. The second contribution would be the creation of the ICA itself. Indeed, to this day, the ICA is the framework that the government uses to evaluate proposed FDI projects in Canada. While it was considered to be a “paper tiger” in the Mulroney years, the very same law would enable the ICA to, after a number of amendments, effectively screen the entry of foreign enterprise to the Canadian market.

#### *The Paper Tiger Finds Its Teeth – 2008-Present*

While under Mulroney, the ICA was seen as a paper tiger, a regulation without any significant enforcement, this has decidedly shifted. In 2008, Stephen Harper's conservative government used the ICA to block the takeover of a Canadian aerospace company (Macdonald, Dettwiler, and Associates or “MDA”) (Collins, 2011, p.152). This would be significant in that it represents the first time an organization's proposed foreign investment would be refused (with the exception of a small number of refusals regarding the appropriation of certain cultural

industries) (Collins, 2011, p.152). This would open the floodgates and usher in a new era of FDI control the likes of which the country had not seen before. In 2009, the government sued an American company to enforce the guarantees the company had made when it acquired a Canadian enterprise, and in 2010, the government refused a proposed acquisition on the grounds that there was no net benefit to Canada (Collins, 2011, pp.152-153). Fast forward to the 2022-2023 fiscal year, and 22 investments were reviewed under s.25.3, which is a national security review (among which 8 would be withdrawn, and 3 would result in a divestment order) (Industry, Science, and Economic Development Canada, 2023, p.3). It is clear then, that there has been a significant shift in the way the government has begun to review foreign investments. To understand this shift, it is necessary to examine the precipitating incident – the proposed acquisition of MDA by an American tech Company, as well as the blocked investments of 2009 and 2010.

Founded in 1969, MDA is Canada's largest aerospace manufacturer (Macdonald, Dettwiler, and Associates, 2023). The company was well known for its Radarsat-2 technology, which was used to monitor Canada's Arctic, among other things (Collins, 2011, p.153). When Alliant Techsystems proposed to acquire MDA (and specifically, the Radarsat-2), critics argued that the transaction, if approved, would essentially represent a donation of hundreds of millions of taxpayer dollars, as the federal government had given MDA 445 million CAD\$ in funding specifically to develop the technology (Collins, 2011, p.154). Similarly, there were public fears that the transaction would severely hamper Canada's ability to defend its Arctic territory (Collins, 2011, p.154). In light of this, the government decided to block the transaction, despite the fact that MDA itself greatly favored it (Collins, 2011, pp.153-154).

To many, this apparent reversal of decades of government policy came out of the blue. While the Harper government attempted to assure the business community that this was a unique situation and did not represent a larger shift in government policy, the ICA was amended shortly thereafter to enable the government to review any proposed investments if they could be injurious to the national security of Canada (Collins, 2011, pp.253-154). This, of course, would greatly increase the discretionary powers of the Minister of Industry, who is in charge of the review process (Collins, 2011, p.155).

Shortly after having blocked the MDA acquisition, in May of 2009, the Canadian government also filed legal action in the Federal Court of Canada against United States Steel Corporation (“USSC”) as the company had failed to increase Canadian steel production and maintain employment levels, promises which USSC had made as a condition for government approval (Collins, 2011, pp.155-156). Despite those promises, USSC closed most of its steel factories in Canada and laid off 1,500 employees (Collins, 2011, p.156).

In response to this legal action, USSC asserted that the enforcement proceedings brought against them were unconstitutional as they violated USSC’s right to a fair trial (Collins, 2011, p.156). In June of 2010, the Court ruled in favour of the government, and this decision was upheld by the Court of Appeal in 2011 (Collins, 2011, p.156). This decision sent a loud message to foreign investors – not only was it possible for the ICA to review their proposed investments on the grounds of national security, but the government had shown a willingness to hold investors accountable to the promises they made during the investment review process (Collins, 2011, pp.156-157).

The final of the formative ICA actions was the blocking of BHP Billiton’s takeover of Potash, a Saskatchewan-based mining and manufacturing company. BHP Billiton’s proposed 39

billion CAD\$ bid was one of the largest of 2010 (Collins, 2011, p.157). Before the federal government would refuse the bid, the provincial government of Saskatchewan would commission a report that would find that the acquisition would cost the provincial government roughly 2% of its annual revenue over 10 years (Collins, 2011, p.158). Despite this, the report did advise allowing the transaction, as it projected significant economic benefits in the long run and the deal was favorable compared to the deal proposed by the Chinese SOE Sinochem (Collins, 2011, pp.158-159). However, to the shock of the global business community, the government blocked the transaction on the basis that BHP Billiton failed to demonstrate that it would provide a net benefit to Canada (Collins, 2011, p.159). This development was particularly shocking as it appeared to the international community that Canada was taking a protectionist stance, while being one of the fiercest advocates against protectionism (Collins, 2011, p.160). Following the government's decision, BHP Billiton withdrew its application (Collins, 2011, p.157).

Taking the three above decisions together, it is clear that the narrative has once again shifted. Indeed, whereas the openness narrative was the driving force behind the ICA, it is now one of the biggest barriers to entry to foreign enterprises. The protectionist and US imperialist narratives have once again emerged and begun to take a larger place in the minds of Canadian decision-makers. Of course, this is not to say that the liberalization narrative has disappeared. Indeed, the fact that, of the 1,010 applications for review and notification in 2023, only a handful were denied, strongly indicates that Canada is in fact still open to business (ISED, 2023b). Instead, it is better to say that this shift in the narrative merely represents a willingness to evaluate FDI projects and determine if they are in the interests of Canada.

In that sense, then, the ICA represents then, a more definitive riskification than FIRA did. Much like FIRA, the ICA is a clear attempt by the government to address the permissive causes of harm (business practices that fail to take into account the interests of Canada) by screening investors and forcing them to demonstrate their benefits and the steps they will take to mitigate potential harms. The ICA also presented an opportunity for more open debates on individual acquisitions than FIRA (although, as Dobson (2014) would state, the process was still somewhat opaque) as well as putting the government in a position to better appreciate the long-term benefits of FDI by reducing barriers to market entry.

Of course, if there is one type of FDI that would be especially demonized and seen as a risk to be avoided, it is FDI from SOEs, and in particular, Chinese SOEs. The first hint of fear of SOEs in the context of FDI is the guidelines published by the government in 2007. Simply put, the Guidelines emphasized the need for SOEs seeking to invest in Canada to follow the standards of corporate governance and to operate on a commercial basis (Campbell, Musgrove, and Wortley, 2012). In other words, the statement strongly implied the government would use the ICA to prevent investments that were made by companies seeking to fulfill non-market objectives. This sentiment would be echoed in the report commissioned by the Saskatchewan government in response to the BHP Billiton acquisition. The report specifically called out the risks of SOEs being incentivized to work against the interests of Canada (Bloom and Hodgson, 2010, pp. iii-iv). The guidelines would be updated in 2012, where the government expressed a further desire for Canadian participation in the SOE's Canadian operations, while also expanding the definition of SOE to include businesses influenced by States rather than companies that are merely owned by them (Campbell, Musgrove, and Wortley, 2012). The statement also made

clear that the proposed acquisitions of Canadian holdings in oil sands would only be found to be of a net benefit in exceptional circumstances (Sroka, 2017, p.188).

It is clear then, that at least since 2007, SOEs have been targeted as a particularly dangerous investor. Indeed, while it is widely argued that ICA's decisions are opaque and unpredictable, the fact that SOEs are subject to a much more stringent review means that they are far more likely to suffer adversely from this review process (Sroka, 2017, p.194). In the next section, then, we shall examine how the narrative surrounding FDI from Chinese SOEs in particular has changed and look at parallels within Canada's history, as well as the wider literature to determine if there is something new about FDI from Chinese SOEs.

### **Risk Management and Containment – Canada's old (and new) FDI Policy**

It is clear that in recent years, FDI from SOEs has been particularly scrutinized by the Canadian government. Despite this, researchers have consistently found that the risks surrounding FDI from Chinese SOEs are overblown (Sroka, 2017, pp.205-207; Cornish, 2012; Dobson, 2014, pp.16-19; Globerman & Shapiro, 2009, p.180; Du, 2014, p.1159). Taking this into account, then, it is important to explore why FDI from SOEs continues to be seen as a greater security risk than other corporations.

This differential treatment is best explained not by the risk these enterprises pose themselves, but rather, by their perceived risk and how this perceived risk weighs on the calculation of risk in the riskification framework that the ICA is built upon. SOEs have long been seen as investors worthy of suspicion, largely due to the support they are perceived as receiving from the government and the non-market objectives that they are believed to be working towards (Cuervo-Cazurra, 2018, pp.138-140). Specifically, State-owned multinationals from developing

economies (especially China) are seen as working directly against the national interest (Cuervo-Cazurra, 2018, p.140). This fear is clearly echoed in the 2007 and 2012 statements issued by the Minister of Industry, where the government explicitly stated that SOEs would have to demonstrate their commercial orientation and their freedom from foreign government influence in their decision-making (Sroka, 2017, pp.186-188).

Taking into account the above, it is not the inherent risk of investment from Chinese SOEs that has pushed the government down this path, but rather, it is the narrative surrounding Chinese SOEs. As has been made clear throughout this paper, shifting risk perceptions and precipitating incidents have been the driving force behind FDI policy change since Confederation. As such, the increased control the government is seeking to exercise over Chinese FDI should not be considered a reflection of the “new and unique dangers” posed by these investors, but rather, as a continuation of a much longer trend of fear of foreign subjugation that has existed in Canada since day one.

## **Conclusion**

In conclusion, the role of foreign enterprise in the Canadian economy (and by extension, Canadian society as a whole) has been highly contested since the early days of the country. Two competing pairs of narratives (the openness-protectionist narratives and the free-trade-interventionist narratives) have largely been the center of the debates around FDI and trade in Canada – while Canada’s investment landscape has changed dramatically since its inception, the ideas around how Canada should (or should not) protect itself from the dangers of the outside world have not changed at all. Many of Canada’s most important policy decisions of the past century can be explained by a precipitating incident shifting the balance between these

narratives, resulting in a new policy being developed at the political equilibrium. As a result, we can see the increased scrutiny towards FDI from SOEs is not a historical outlier that represents the “unique danger” that these firms pose to national security, but rather, we can see it as a continuation of the debates that have informed Canadian economic policy since Confederation. We can also see how, much like the other debates on economic policy throughout history, the reality of a situation is much less powerful than the narrative surrounding it – regardless of whether or not FDI from SOEs poses a unique threat, to the extent they are seen as such, policies will be put into place that “riskify” them.

Despite the unwarranted negative attention that they have received, then, it is clear that FDI from SOEs can bring significant benefits to Canada, while posing a significantly lower threat to Canada than the conventional wisdom would seem to indicate. As such, it would be worth revisiting Canada’s FDI policy to ensure that it does not merely reflect the causal narrative that has been thrust upon it, but rather reflects the reality of FDI. Canada should move to reduce barriers to FDI from SOEs to promote its growth and to better position it to benefit from the future of FDI, which appears to be increasingly dominated by SOEs, from China specifically.

In terms of future research, it would be fruitful to examine the origins of the fearmongering surrounding FDI from Chinese SOEs. In particular, conducting discourse analyses of anti-China rhetoric may enable social scientists to better explain where the origins of this fear of SOEs are and, potentially, enable decision-makers to develop strategies to render FDI more palatable for the general population. Similarly, further research into the extent to which narratives contribute to the formulation specific policies would be welcome, as it would enable researchers to paint a much more fulsome picture of how political decision-making works on the individual level. Finally, a further analysis into the role of narratives in the development of

Canadian economic policy would enrich the field and breathe new life into historical analyses of Canadian policy.

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