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NAFTA and the Canadian Insurance Industry

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Résumé de l'article

L'Accord de libre-échange nord-américain (ALENA) ne sera pas sans avoir des répercussions sur l'industrie canadienne de l'assurance. Entré en vigueur le 1er janvier 1994, à la suite de sa proclamation par le gouvernement canadien, le traité comporte plusieurs dispositions sur la libéralisation des services financiers, notamment sur les possibilités d'implantation et sur le traitement équitable accordés par chaque pays aux assureurs des pays liés. Cet article présente les marchés d'assurance respectifs des trois pays signataires, le Canada, les États-Unis et le Mexique. L'auteur examine les effets qu'aura ce traité sur notre industrie. Il s'interroge en particulier sur l'ouverture du marché mexicain, après soixante années de protectionnisme. Il anticipe que son accès serait peu significatif à l'égard des compagnies canadiennes, pour trois raisons : l'étroitesse du marché, la forte concurrence d'autres pays et, enfin, l'importance relative que ce marché représente dans les stratégies de développement de plusieurs assureurs canadiens.

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by

Brent Sutton*

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1. Introduction

On December 17, 1992, Canadian Prime Minister Brian Mulroney, U.S. President George Bush and Mexican President Carlos Salinas de Gortari signed the North American Free Trade

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Agreement (NAFTA). The agreement, which has been ratified by all three countries, will usher in a new set of rules governing trade and investment among the three countries. NAFTA builds on the earlier Canada-U.S Free Trade Agreement (FTA) by developing more comprehensive trade and investment rules and by extending them to include Mexico. NAFTA is scheduled to come into force on January 1, 1994.

Canada's implementing legislation for NAFTA, Bill C-115, received royal assent on June 23, 1993, but had not yet been

proclaimed into force at the time of writing (November 1993). The recent election of Prime Minister Jean Chrétien has cast some doubt over Canada's participation in the agreement as the new government has been critical about the lack of formal rules on subsidiaries and anti-dumping, and it wants Canada to be subject to the same energy provisions as Mexico. Most trade experts believe that an accommodation can be reached that will enable Chrétien to accept the agreement, although Canada is unlikely to have all of its demands satisfied.

Several provisions dealing with trade in insurance (and other financial) services are included in NAFTA. One of the most important is that NAFTA opens Mexican insurance markets, among the fastest growing markets in the world, to Canadian and American insurance companies. By world standards, Mexicans are under-insured and NAFTA presents new opportunities for insurance companies in Canada and the U.S. who face mature markets at home. NAFTA also subjects trade in insurance services to trade principles, such as the right of establishment and national treatment, which will ensure that foreign insurance companies are treated in a fair and consistent manner by host countries.

Thus far, NAFTA has been met with little excitement by the insurance community in Canada. This is due in part to the fact that there are no Canadian insurance companies operating in Mexico and that there are no Mexican insurance companies active in Canada. This reaction is in sharp contrast to many U.S. insurers who view Mexico as a major business opportunity.

The purpose of this brief article is to assess the implications of NAFTA for the Canadian insurance sector to determine whether their indifferent attitude towards Mexico is a source of missed opportunity or a justifiable response to what may very well be a "non-event". The article will first provide an overview of the insurance markets in North America, with particular focus on Mexico. The key provisions in NAFTA relating to insurance services will then be described and their implications for the Canadian insurance industry will be assessed. The article will conclude with observations regarding the opportunities in insurance services presented by NAFTA.

2. Insurance Markets In North America

North America accounts for about 45 percent of the world's life and non-life insurance market, with combined premiums for Canada, Mexico and the United States of $557 billion[1] in 1992 (see Table 1). The United States has not only the largest insurance market in North America, about 15 times larger than Canada and 110 times larger than Mexico, but Americans are also the highest consumers of insurance on a per capita basis by a wide margin. The enormous size of the U.S. market has made American insurance companies among the largest in the world, although there are a number of world-class life insurance companies in Canada as well (see Table 2). In contrast, insurance companies in Mexico are small and do not operate outside the country.[2]

[1] All values in this article are expressed in U.S. dollars. Conversions were made using end of year exchange rates as set out by the International Monetary Fund (IMF). At the end of 1992, one U.S. dollar equalled 1.2711 Canadian dollars and 3.1154 Mexican new pesos.

[2] An excellent overview of Mexico's insurance industry is provided in Adrian Paez, "The Mexican Insurance Industry," presentation to the 1993 Roundtable on the Americas of the International Insurance Council, New York City, February 9, 1993.

Table 1

Overview of Insurance Markets in North America, 1992

Characteristic	Canada	Mexico	U.S.
Premiums (U.S.$ millions)	37,766	4,850	534,356
Life & Health	20,088	2,134	300,323
P&C	17,678	2,716	234,033
Insurance Per Capita (U.S.$)	1,376	54	2,115
Life & Health	732	24	1,189
P&C	644	30	926
Number of Insurance Companies	597	42	4,905
Life & Health	147	n/a	2,105*
P&C	450	n/a	2,800
Market Share of 5 Largest Private Insurers (%)	n/a	67.7	n/a
Life & Health	28.5	n/a	22.9
P&C	23.7	n/a	29.0
Market Share Held by Foreigners (%)	n/a	11.1*+	n/a
Life & Health	29.7	n/a	n/a
P&C	61.4	n/a	10.6
Employment	181,237	19,089*	n/a
Life and Health	63,497	n/a	2,163,000
P&C	117,749*	n/a	n/a

* 1991

\+ Market share of joint venture insurers times percentage of foreign ownership.

n/a = not available

Sources: Paez (1993), *Best's Insurance Management Reports*, *Canadian Insurance Statistics*, Canadian Life and Health Insurance Association, The Conference Board of Canada.

Table 2

Largest Insurance Companies by Country, 1992

(U.S.$ millions)

Canada	Premiums
Sun Life	3,840
Manulife	3,228
Great-West Life	2,789
Confederation Life	2,307
Mutual Life	1,739
Mexico	**Premiums**
America/Commercial*	1,004
Nacional Provincial	906
Monterrey	780
Asemex	556
Segumex	386
United States	**Premiums**
State Farm	28,212
Prudential	24,762
MetLife	19,933
Allstate	15,280
New York Life	8,595

* Based on 1993 merger of Seguros America S.A. and Seguros La Commercial S.A.

Sources: *Journal of Commerce*, August 19, 1993, *Best's Insurance Management Reports*, Company Annual Reports, The Conference Board of Canada.

Table 3

Major Insurance Lines, 1992
(Share of Premiums, Percent)

Insurance Class	Canada	Mexico*	U.S.
Life	53	44	56
Traditional Life	16	36	17
Annuities	27	n/a	26
Health	10	8	13
Property and Casualty	47	56	44
Automobile	22	31	20
Personal Property	6	i/o	4
Commercial Property	4	i/o	3
Fire	i/o	10	1
Other	15	15	16

* 1991
n/a = not available
i/o = included in other categories
Sources: Paez (1993), *Best's Insurance Management Reports*, *Canadian Insurance Statistics*, Canadian Life and Health Insurance Association, The Conference Board of Canada.

The distribution of premiums by class of insurance highlights some of the most notable features of the three countries (see Table 3). First, traditional life insurance products account for a greater share of the Mexican market than they do in Canada or the United States. In the latter two countries, savings products, such as annuities, now account for about half the premium volume of life insurance companies. Second, health insurance accounts for a larger share of total premiums in the United States than elsewhere. Mexico's lower income levels and Canada's national health care system lessen the relative demand for health insurance coverage. Third, automobile insurance is by far the largest single line of property and casualty insurance written in all three countries. It is somewhat surprising that automobile insurance accounts for such a large share of the Mexican market since it is not yet compulsory,[3] as is the case in Canada and most U.S. states.

While the Mexican insurance market has experienced tremendous growth in the past few years (see Chart 1), the market remains small, about the size of British Columbia or Arkansas. Most insurance products are "luxury goods" -- that is, the demand for them increases more than proportionately with rises in income -- and the low per capita incomes put insurance products out of reach for most Mexicans.[4] As a result, Mexico is considered to be an under-insured market, as in reflected by the fact that less than 2 percent of Mexicans have personal life insurance, only 2 percent of homes in Mexico are insured, and only 24 percent of Mexican cars are insured.[5]

3. The Insurance Provisions of NAFTA

Trade in insurance services is dealt with in Chapter 14 (Financial Services) of NAFTA.[6] The chapter establishes a comprehensive principles-based approach to trade in financial services, the first time such an approach has been adopted. Additional country-specific commitments on market access and transition periods for compliance with agreed principles, especially as they relate to Mexico, are set out in Annex VII of the agreement. The chapters on investment and dispute settlement also contain relevant provisions.

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[3] Proposals have been put forward to make automobile insurance mandatory in Mexico and they are expected to be adopted (in whole or in part) in the near term.

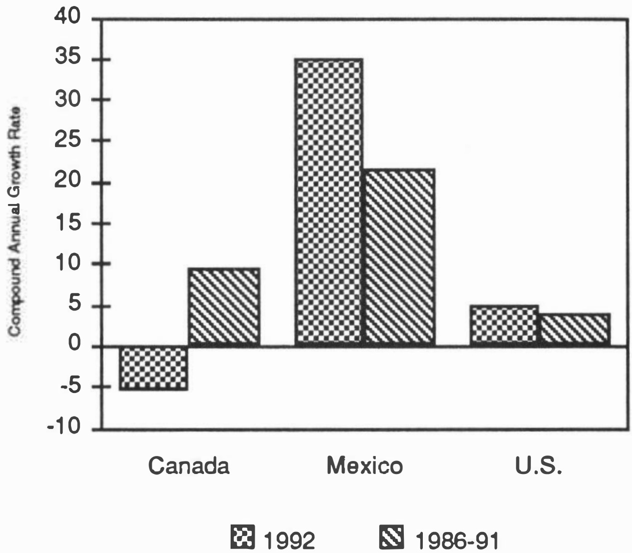
[4] Even though Mexico has a population that is fast approaching 90 million, the consensus among many industry officials is that the actual market for insurance products is probably about 8 million people.

[5] "Why Insurers are Splashing Across the Rio Grande," *Business Week* (August 9, 1993), p.68.

[6] For a broader analysis of the financial services chapter of NAFTA on Canada's financial sector, see Brent Sutton, *Business as Usual: NAFTA and the Canadian Financial Services Sector* (Ottawa: The Conference Board of Canada, 1993), Pierre Sauvé and Brenda González-Hermosillo, *Implications of the NAFTA for Canadian Financial Institutions* (Toronto: C.D. Howe Institute, 1993), and Cally Jordan, "Financial Services Under the NAFTA: The View from Canada," *The Review of Banking and Financial Services* 9(6) (March 1993): 45-55.

Chart 1

Direct Premium Growth by Country
(Compound Annual Growth Rate)



Notes: Premiums for Canada and Mexico were converted to U.S. dollars before growth rates were calculated. U.S. growth rates are for the 1988-91 period.

Sources: Paez (1993), *Best's Insurance Management Reports*, *Canadian Insurance Statistics*, The Conference Board of Canada.

Market Access to Mexico

Until very recently, Mexico's insurance markets were among the most protected in the world. Since 1935, foreign firms were limited to 15 percent ownership in Mexican insurance companies and Mexicans were prohibited from purchasing most classes of insurance from sources outside the country. In addition, competition among indigenous insurers was restricted through a complex regulatory structure, and this protection made insurance companies very profitable. Under pressure from the

United States,[7] Mexico began to liberalize its insurance sector in 1990. The most important changes brought in by the Mexican government were: (1) permitting foreigners to own up to 49 percent of Mexican insurance companies; (2) adoption of risk-based capital requirements; (3) partial deregulation of policy forms and premium rates; and (4) elimination of the requirement that foreign insurance companies cede at least half of their reinsurance in Mexico.[8]

NAFTA takes these reforms much further by opening Mexican insurance markets to insurance companies from Canada and the United States. Market access is to be phased in over a six-year period, with all barriers to be removed by the year 2000, although some types of foreign establishments will gain full access sooner than others. The use of a transition period was designed to give Mexican insurance companies time to respond to increased foreign competition and to reward those foreign insurers active in Mexico prior to the negotiation of NAFTA.

Access to Mexico's insurance markets can take one of three forms. First, insurance companies in Canada and the United States, including the subsidiaries of foreign insurance companies operating in either country, will be permitted to establish wholly-owned subsidiaries in Mexico starting in 1994. These companies will be limited to an aggregate market share of six percent in 1994, rising in specified annual increments to 12 percent in 1999. There is also an individual cap of 1.5 percent of the market during the transition period. Market share limits are based on authorized capital and are to be applied separately to life and property and casualty insurance operations, although this does not prevent both types of insurance operations from being conducted in a single company. All limits are to be removed on January 1, 2000. Insurance intermediaries, such as actuaries,

[7] See the testimony of Henry G. Parker on Hearings of the North American Free Trade Agreement before the Subcommittee on Trade of the Committee on Ways and Means of the U.S. House of Representatives on September 22, 1992.

[8] Rawle O. King, "The North American Free Trade Agreement: Liberalizing Trade and Investment in Insurance", CRS Report for Congress (January 1993), p.1.

agents, brokers and claims adjusters, are not subject to market share limits on their subsidiaries.

Second, Canadian and American insurance companies with an ownership stake of 10 percent or more in a Mexican company prior to July 1, 1992, will be permitted to increase their equity participation to 100 percent by January 1, 1996. Mexico also retains the right to permit accelerated foreign ownership when the government considers such action to be in best interest of the country. This option is of little benefit to Canada since no Canadian insurance companies are involved with joint ventures in Mexico. There are, however, six U.S. insurers with ownership interests in Mexico, including Aetna, American International Group (AIG), Chubb, Cigna, Metropolitan Life and Reliance. These joint ventures will not be subject to the aggregate or individual market share limits that apply to newly-established subsidiaries.

Third, insurance companies from Canada and the United States are permitted to form new joint ventures with Mexican insurers. In order to qualify, the percentage of the Mexican insurance company's common voting stock owned by a Canadian or American partner cannot exceed the following limits: 30 percent in 1994, 35 percent in 1995, 40 percent in 1996, 45 percent in 1997, 51 percent in 1998 and 75 percent in 1999. Ownership limits will be removed thereafter. As with existing joint ventures, these new partnerships are exempt from the market share limits.

Trade Principles[9]

In contrast to the Canada-U.S FTA, the financial services provisions of NAFTA are based on trade principles.[10] Their

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[9]This section draws heavily on my *Business as Usual: NAFTA and the Canadian Financial Services Sector*. See also, King, "NAFTA: Liberalizing Trade and Investment in Insurance."

[10]The financial services chapter of NAFTA was considered to be more of an "exchange of concessions" than a full-fledged trade agreement. Commitments were limited to the removal of specific regulatory impediments. Provisions governing insurance services were broader because they were not exempt from the services and

presence provides a foundation on which to evaluate the fairness of domestic regulatory requirements with regard to the ability of foreign financial institutions to compete in that market and will help to ensure that future changes to the domestic legislation of any signatory country will not discriminate against foreign financial institutions. Regulatory measures that are seen to affect foreign financial institutions in a discriminatory manner can be challenged under the dispute settlement system. The remainder of this section will list the most important principles, highlighting their relevance to trade in insurance services.

Right of establishment

Any insurance company in a NAFTA country has the right to establish a subsidiary in the territory of other NAFTA countries. Regulatory authorities continue to be free to set the terms and conditions of entry, subject to the other principles contained in the agreement.

Cross-border trade

Customers have the right to purchase insurance services from financial institutions located in other countries for use outside their home country. This obligation does not, however, require countries to allow foreign financial institutions to undertake or solicit business within its territory. By accepting this principle, Mexico agreed to allow the purchase of life and health insurance, accident/tourist insurance, cargo insurance and reinsurance from companies in Canada and the United States. However, due to foreign exchange concerns, Mexico reserved the right to control the underwriting and sale of insurance denominated in Mexican pesos.[11]

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dispute settlement chapters. See Paul Rachon, *Strengthening Market Access in Financial Services: The Financial Services Provisions of the Canada-U.S. Free Trade Agreement* (Ottawa: The Conference Board of Canada, 1989).

[11]King, "NAFTA: Liberalizing Trade and Investment in Insurance," pp. 7-8.

National treatment

NAFTA countries are required to treat foreign insurers no less favourably than domestic insurers. However, the provision goes a step beyond traditional notions of national treatment by defining it in terms of "equality of competitive opportunity". This provision recognizes that even when foreign insurance companies are accorded identical legal treatment in a host country, foreign insurers may be disadvantaged because of differences in the business and regulatory structure of national financial systems. This provision will permit insurance companies to challenge regulations that, while applied equally to foreign and domestic firms, have the effect of giving domestic insurance companies an advantage in the local market.[12]

Most-favoured-nation treatment

NAFTA countries must accord the insurance companies of other NAFTA countries no less favourable treatment than that extended to the insurance companies of all countries, regardless of whether they are from a contracting state. This means that if either the United States or Mexico offer preferential treatment to insurance companies from countries outside North America, this treatment must also be extended to Canadian insurance companies.

Transparency

NAFTA countries are required to publish all regulations that affect trade and investment in insurance services, to circulate for public comment copies of proposed legislative changes, and to provide administrative decisions within 120 days regarding the application for license of a foreign insurance company. Mexico's history of "discretionary" decision-making and

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[12]Opportunities to challenge host country regulations on these grounds may be limited, however. First, existing regulatory barriers by sub-national governments can be grandfathered under the agreement. Second, the concept of "equality of competitive opportunity" is not defined. Third, national regulatory authorities are free to establish any regulations on "reasonable" prudential grounds and, again, the term is not defined. See Brent Sutton, *Business as Usual*, pp.15-16.

tendency to promulgate new regulations without prior notification makes this an important gain for foreign insurers operating in Mexico.

Dispute settlement

The dispute settlement procedures are set out in Chapters 14 and 20 of NAFTA. Disputes are to be heard by a panel of five members, generally chosen exclusively from a roster of 15 financial experts appointed unanimously for terms of three years. Retaliation for measures deemed to be inconsistent with the obligations of the agreement must be restricted to suspending benefits in the financial sector. This means that a Mexican insurance regulation judged to violate NAFTA could be punished by a loss of benefits to Mexican banks operating in Canada or the United States.

4. Implications for Canadian Insurers

The insurance provisions of NAFTA are essentially about opening the Mexican market to insurance companies from Canada and the United States. NAFTA leaves prevailing market access conditions between the United States and Canada largely untouched. As well, there is little prospect that Mexican insurance companies will move to establish a presence north of the Rio Grande. Mexican insurance companies are small, less efficient than their competitors in Canada and the United States, and will need to focus closely on their home operations with the Mexican financial services industry in a period of substantial restructuring due to market liberalization.[13] Thus, the chief benefit of NAFTA to Canadian insurance companies rests almost exclusively with the possibility of new business opportunities in Mexico. The remainder of this article will assess the value of this opportunity.

[13]This is not to deny the possibility of Mexican insurers targeting certain segments of the U.S. insurance market. The large hispanic communities located in California, Texas, New York and other major urban centres do offer Mexican insurance firms new business opportunities. Any moves along these lines, however, are likely to be of a long-term strategy.

As noted above, Mexican insurance markets are small. This is due to several of factors, not the least of which is that Mexico is, and will continue to be for the immediate future, a third-world country with low per capita disposable incomes, a high incidence of poverty, and a relatively small middle class. Although Mexico has a population more than three times Canada's, the current market for insurance is much smaller than in Canada. Other factors that have kept insurance markets small in Mexico include a long history of protectionism, stringent domestic regulations on product offerings and pricing, and a lack of familiarity (and perceived need) for insurance protection among the general population.

Despite this current state of affairs, the questions of greatest importance relate to the *future* development of Mexican insurance markets in response to NAFTA. First, will Mexico become a large insurance market that is attractive to a wide array of international insurance companies? Second, are Canadian insurance companies able *and* willing to capitalize on new opportunities in a growing Mexican insurance market? As will become clear in the analysis that follows, I think the answer to both questions is no.

There is little doubt that Mexican insurance markets are poised for substantial growth. If economists are correct in their predictions regarding the impact of NAFTA on economic growth in Mexico,[14] then rising income levels and a larger middle class are sure to stimulate the demand for insurance products. Chart 2 provides three estimates of how quickly insurance premiums may grow in Mexico between 1993 and 2000. The figures are direct premiums written expressed in real U.S. dollars. The estimates are based on assumptions of economic growth in Mexico and increases to "insurance penetration" (direct premiums expressed as a percentage of gross national product).[15]

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[14]See, among many others, Gary C. Hufbauer and Jeffrey J. Schott, *NAFTA: An Assessment* (Washington: Institute for International Economics, 1993).

[15]Insurance penetration is a frequently used measure to compare the development of insurance markets in different countries. Empirical work has showed that insurance penetration is positively correlated with national income. In 1991, insurance penetration

The low growth estimate assumes annual real GNP growth of 2.5 percent and insurance penetration of 3.0 percent by the year 2000.[16] The corresponding figures for the medium and high growth estimates are 3.0 percent and 4.0 percent for GNP growth and 3.5 percent and 4.0 percent for insurance penetration.

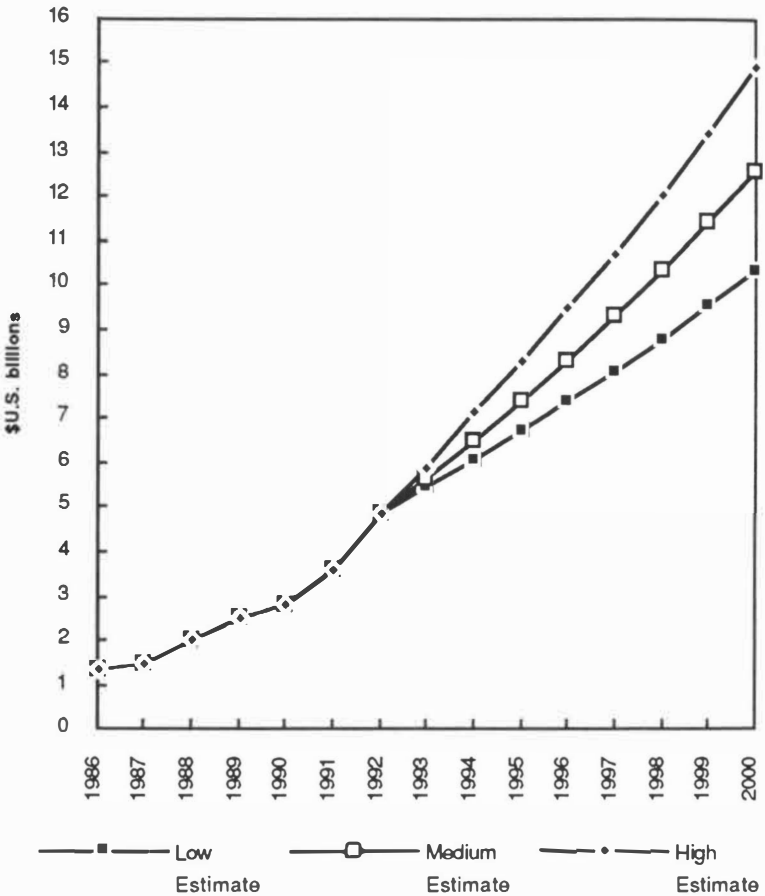
Under the medium growth estimate, insurance premiums (as expressed in real U.S. dollars) are expected to grow by 12.6 percent per year, reaching $12.5 billion by the year 2000. Such growth is impressive but, because it is on top of a relatively small base, it would still leave Mexican insurance markets in 2000 much smaller than the insurance markets in Canada and the United States in 1992! Looking at this in another way, the Mexican insurance market is expected to increase in absolute terms by between $6 and $10 billion over the next seven years. In comparison, insurance premiums grew by almost $11 billion in the past five years in Canada and by $25 billion in the past year in the United States. Given the relative size of the three insurance markets, it seems unlikely then that Mexico is to become a major source of new business growth.

was 1.3 in Mexico, compared with 5.8 in Canada and 8.6 in the United States. See Swiss Re, "World Insurance in 1991," *Sigma*, Economic Studies No. 4/93.

[16]The level of insurance penetration depends on a number of factors. They include: product knowledge and familiarity among the population, the availability of substitute products from non-insurance companies, confidence in and acceptability of insurance companies as financial intermediaries, product innovation and flexibility, regulatory constraints on business powers, compulsory insurance schemes and their enforcement, and the structure of social insurance, health and pension programs.

Chart 2

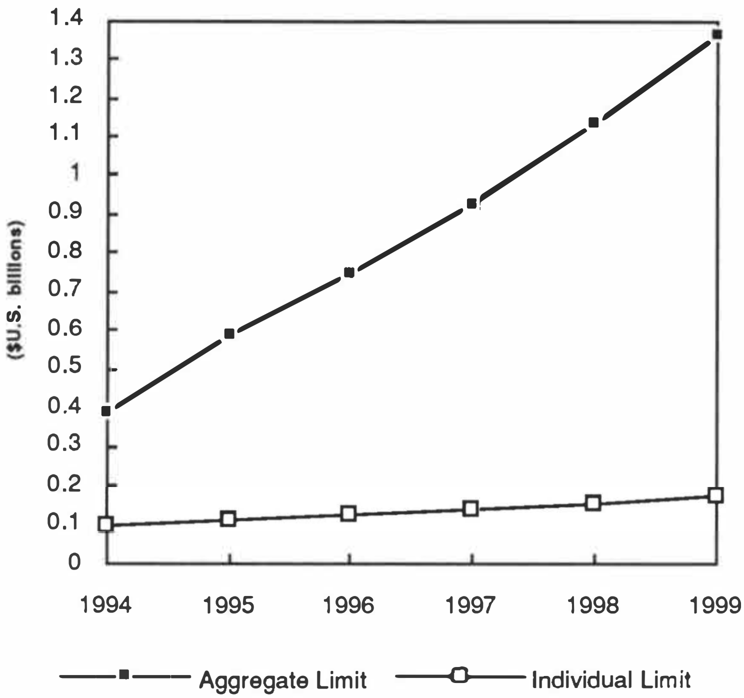
Forecast of Premium Growth in Mexico
($U.S. billions)



Source: The Conference Board of Canada.

Chart 3

Market for U.S. & Cdn Subsidiaries
($U.S. billions)



Source: The Conference Board of Canada.

A further limiting factor, at least until the end of the decade, is the transitional aggregate and individual market share caps imposed by Mexico. Using the medium growth forecast, Chart 3 shows the amount of the Mexican market that will be available to insurance subsidiaries established by Canadian and American firms.[17] According to these calculations, it will be 1998 before Canadian and American insurance subsidiaries are able to collectively write premiums in excess of $1 billion. In addition, individual firms will be limited to writing total premiums of between $100 and $170 million during the transition period. Once again, this analysis casts doubt on the prospect of Mexico becoming a major new source of business growth for insurance, at least for the remainder of the decade.[18]

Even if Mexican insurance markets offered significant new opportunities for increased business volume by Canadian insurance companies (which does not appear to be the case), there are several reasons to doubt that Canadian firms will make significant inroads into Mexico. First, competition from other foreign insurance companies, especially those from the United States, will be intense and many of these firms are better positioned to take advantage opportunities in Mexico than their Canadian counterparts. In fact, 13 foreign firms had joint ventures with Mexican insurance companies at the end of 1991, six of them from the United States (see Table 4).[19] Moreover, these 13 firms had a combined market share of more than 40 percent in 1991. In contrast, there are no Canadian insurance

[17]Actual markets shares will be determined on the basis of authorized capital, not premiums written. However, there is a close relationship between capital size and premium volume.

[18]This finding is overstated by the fact that Mexico will also allow foreign insurance companies to enter Mexico through joint ventures that will not be subject to aggregate and individual market share limits. However, it is foreign insurance companies that are already in Mexico that are most likely to take advantage of this option and this does not include any Canadian firms.

[19]In addition, two other U.S. firms -- American Bankers Insurance and Primerica -- have expressed interest in establishing a presence in Mexico, and a third firm, New York Life, announced in August 1993 its intention to acquire a 30 percent ownership stake in Geo Compania de Seguros. See Paul Dykewicz, "U.S. Insurers Scouting for Partners To Gain Entry to Mexican Market," *Journal of Commerce*, August 19, 1993 and *Best's Insurance Management Reports*, August 30, 1993.

companies with joint ventures in Mexico at present. Insurance companies from the United States with an existing joint venture in Mexico have the advantage of being able to increase their ownership of them to 100 percent by 1996, while avoiding the market share limits that will be applied to newly-established, wholly-owned subsidiaries.

Table 4

Foreign Insurance Companies in Mexico, 1991

Insurer	Market Share in Mexico (%)	Investor	Country	Ownership Share (%)
America	14.7	Generale	Italy	24.0*
Monterrey	12.7	Aetna	U.S.	30.0
InterAmericana	3.5	AIG	U.S.	49.0
Tepeyac	3.5	Mafre	Spain	49.0
Republica	3.3	Commercial Union	U.K.	49.0
Cuauhtemoc	1.1	Allianz	Germany	49.0
Territorial	0.5	AGF	France	< 30.0
Anglo Mexicana	0.4	Generale	Italy	49.0
Equitiva	n/a	Chubb	U.S.	30.0
Seguros Génesis	n/a	Banco Santander/ MetLife	Spain/U.S.	49.0
Proteccion	n/a	Reliance	U.S.	30.0
Chapulepec	n/a	Zurich	Switz.	30.0
Progresso/Cigna	n/a	Cigna	U.S.	49.0

* applied to increase to 49 percent.

n/a = not available

Sources: Mexican Insurance Regulatory Authorities, The Conference Board of Canada.

Second, Mexican insurance companies are not standing by idly as the market is liberalized. In anticipation of increased foreign competition, Mexican insurance companies are bolstering their competitiveness through mergers, alliances, the adoption of new management practices and technology systems, and better training for professional and sales staff. For instance, two of Mexico's largest insurance companies, America and La Comercial, agreed to a stock swap in May 1993, thereby creating the largest insurance company in Mexico.[20] Mexican insurance companies with minority foreign ownership are looking to their partners for assistance in modernizing management practices and information systems. These efforts will leave Mexican insurers more efficient and innovative.

Third, Canadian insurance companies do not view expansion into Mexico as an important strategic imperative, at least in the short to medium term. Such indifference among property and casualty insurers is not surprising given their inexperience in markets outsisde of Canada, but it does seem an unusual response from Canada's internationally-active life insurance sector. So far, only two insurers in Canada have expressed an interest in Mexico[21] and neither have any investment in the country nor have they revealed any plans to make an investment. The cautious reaction of the Canadian insurance community to opportunities in Mexico stands in stark contrast to the enthusiastic support given to NAFTA by the U.S. insurance industry. One reason for the "wait-and-see" strategy towards Mexico is that the current pace of restructuring in the Canadian financial services marketplace is keeping senior management busy with domestic concerns. Another factor is that other parts of the world, particularly markets in the Asia-Pacific region, are seen to offer more attractive opportunities (e.g., faster growth, larger potential markets) than Mexico.

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[20]The merger will be completed through the creation of a holding company. Both companies, which operate in different market segments, will continue to operate independently and the holding company will be responsible for developing strategic alliances between the two. See Paul Dykewicz and Kevin Hall, "Merger to Create Largest Insurer in Mexican Market," *Journal of Commerce*, May 9, 1993.

[21]Lyndsay Barrett, "Reinsurer Looks to Mexico," *Canadian Insurance* (July 1993), pp.14,34.

In sum, Mexico does not represent a major source of future earnings for Canadian insurance companies. The Mexican market is small, and while it is expected to grow much more quickly than the mature insurance markets of Canada and the U.S., such growth is from a very small base. Competition for insurance premiums is expected to be intense, especially from foreign insurers that are already active in Mexico. For these and other reasons, Canadian insurance companies have not made expansion into Mexico a high priority.

5. Conclusion

The passage of NAFTA will mark a new era in trade and investment relations between Mexico on the one hand and the United States and Canada on the other. The result will be a more integrated North American economic space where goods, services and investment have greater mobility among the three countries. NAFTA represents the culmination of Mexican efforts to bring its national economic policies more in line with those of the advanced industrialized economies, a process that began with Mexico's accession to the General Agreement on Tariffs and Trade (GATT) in 1986. This process has brought rising prosperity to the country.

Insurance, as well as other financial services, are an important part of NAFTA. Despite the fact that NAFTA was the product of negotiations among three countries, the provisions on insurance services are really about greater access to Mexican markets for financial institutions in Canada and the United States. After almost 60 years of protectionism, Canadian and American insurance companies will be permitted to operate in Mexico on a limited basis at first, receiving full national treatment at the conclusion of the transition period. Free trade in insurance services already exists between Canada and the United States, as reflected by the high degree of involvement by

American insurance companies in Canada and Canadian insurance companies in the United States.[22]

Unlike their American counterparts, Canadian insurance firms have so far paid little attention to Mexico. Is this a case of missed opportunity or a reflection of the modest opportunity that actually exists in Mexico for Canadian insurers? This article supports the latter contention. There is no question that Mexican insurance markets are poised for rapid growth and that they will grow more quickly than insurance markets in the United States or Canada. However, the Mexican market is small, and even with high levels of growth, the transitional market share limits will prevent any Canadian insurance subsidiaries from capturing a large share of the market. In addition, there are a number of foreign insurance companies already established in Mexico, including six from the United States, that are better positioned to take advantage of the Mexican market. This is not to deny the prospect of one or two Canadian insurance companies establishing profitable franchises in Mexico, in fact, given the considerable level of insurance expertise that resides in Canada, it would be very surprising if this were not to happen. Rather, the point is that Mexico does not represent an oasis of new business growth and the cautious strategy of the Canadian insurance industry seems entirely appropriate.

[22]In 1992, American insurance companies wrote 16.3 percent of life insurance premiums in Canada and 23.0 percent of property and casualty insurance premiums. Canadian life insurance companies wrote premiums of $9.5 billion in the United States in 1992. See Brent Sutton and Lorraine Pigeon, *The Canadian Financial Services Industry: 1993 Edition* (Ottawa: The Conference Board of Canada, 1993) and Christopher Robey, "Property and Casualty Insurance: Will it Remain the Most International Canadian Financial Services Market?" presentation to The Conference Board of Canada, Ottawa, October 20, 1993.