

Factoring Ourselves Out: How Canada's late 20th century thinking equals a failing grade in the early 21st century global economic calculus

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Labour

Labour is the number one problem facing every industry in Canada. We have a labour shortage, and it is only going to get worse. Here is the reality of today. In Prince Edward Island we have guest workers at a fish plant because no one could be found locally. In New Brunswick today we have guest workers driving long haul trucks because no one could be found locally. In 10 years, unemployment in Nova Scotia will be zero.

Immigration is not the solution, but, done well, it can help. The current immigration pattern mirrors our existing population in age and composition. In other words, as we as a population age, so too do the immigrants who come here. To help, we need younger, entrepreneurial immigrants. We need to also consider allowing foreign students to work when they

are studying in this country. These are young and highly educated people who we should be encouraging to stay here. We also need to look at guest workers. Consider the recent invitation to enter into a guest worker program with Mexico, a ready labour pool, inside of NAFTA, at a time when both Canada and the US face severe labour shortages. We need to make that easier, not harder. And we need to consider the long term benefits of efforts to increase the domestic birth rate, as Quebec has done.

More immediately, and most urgently, we need to adjust the myriad of federal and provincial policies designed to mop up the surplus labour of the early 70's. As an example, consider the program once known as U.I., but now known as E.I. Look at the very nuts and bolts of that program, from the size of the benefits, to the access to benefits to the regionally differentiated benefits. We need to re-evaluate a

program that pays people not to work. The 70's also saw the growth of the public service, but that flush a civil service is now keeping workers that the private sector needs. We need to re-examine university and the post-secondary sector which often takes too long to attain and uses too many teachers to provide. There is also the point that not everyone needs a university degree, we need to be encouraging more people to look outside university when considering post-secondary training. Then there are the job based subsidies and forgivable loans for business. In a labour short environment we need productive enterprises, not make work projects, and maybe we need to consider rewards for eliminating jobs or tax credits based on highest production per employee.

So where can we find some of the people that we will need in a labour shortage. If we reduced the civil service in every province to the national average – we would add 133,000 people to the workforce. If we got just the five eastern most provinces to the national participation rate we would add another 156,000 workers. We also have to stop penalizing people for wanting to work. We need to re-examine any clause that reduces a retiree's pension income for working, and we should consider reducing high marginal tax rates to encourage people to move off welfare and onto the work rolls.

Capital

However, an aging population and a labour shortage is not the death knell for Canada. The answer is improved productivity, and we have been talking about that for over a decade. So why are we not basking in our foresight? Because capital drives that innovation, and we drive capital away.

Our average combined federal and provincial tax burden is somewhere between 4 and 6% better than the United States. It takes about 40%, while we take around 36%, on average.

But our effective *marginal* tax rate is among the highest on business capital investment. Others encourage the next dollar of investment, we tax it. As a result we have among the lowest total business tax receipts as a percent of GDP. And we have a 1 to 1.5% gap between Canada and the US in actual

investment, with a similar gap in R&D investment. So when capital flees and labour is in short supply, we get negative results. In fact, the GDP per capita gap between Canada and the US is widening.

Technology

With capital and labour in short supply, smart investment becomes the priority. Research and development, new technologies and new industries all result from this focus and we certainly have seen some progress in this area. Or have we?

According to one measure I saw recently, Canada offers the best tax treatment of R&D among the G7 countries. There are tax credits, accelerated tax deductions and a broader definition of allowable costs. But, our R&D investment is heavily weighted to the government and academic sector to the point that in 2003 government and academic R&D spending was effectively equal to that in the private sector. Contrast that to the US where the private sector is about 3 times the academic and government investment.

Consider that balance in the light of the regular admissions that universities are generally bad at commercialization. Sure they have gotten better – generally by partnering with the private sector. We need to rebalance our R&D investment. R&D can happen in the private sector, in fact, in terms of swift, practical commercialization and broad application – it is often better if it happens in the private sector.

Consider this recent approach suggested to me by a small manufacturer in rural Nova Scotia. He suggested increasing the R&D credit for private companies, to match it to a production tax credit. As he put it, “do R&D into something new and receive incentive, produce something innovative and receive incentive. That's innovation, that's technology and that's manufacturing!”

Transportation

Even if we had the right balance in our workforce and the right incentives for capital investment and a structure to encourage innovation and technological

advancement, we still need to get our products to market. Right now, in many cases, we can not do so. East Coast ports have been the “poor cousin” of trade expansion as Asian trade has driven growth. We have real opportunities with post-panamax and post-panamax plus and the even bigger ships now coming into service to meet that demand by using both coasts. But again, it is about markets – a twinned highway into central Canada takes us away from our market, not towards it. CN gets this. It is expanding rail service into the Midwest. So why are our road and air connections not following suit?

It is about linking markets, the east and the west coast ports can tie Asia to America and the demand is outstripping the supply on both coasts. And by tying those markets together profitably, we secure the resources and the linkages to build our own market, our own manufacturers and our own tax base. If we treat transportation as an industry and not as an add-on to manufacturing, then the existence of that strong transportation service would drive more manufacturing growth. Let’s get both more eggs and more chickens, and not worry about what comes first.

Closing advice

We need to remember the impact of government spending. Government spending in the US is roughly 2 to 1 on consumption versus investment and the ratio is getting smaller. In Canada we are close to 3 to 1, and the ratio is getting wider. Government consumption takes resources, people, money and material away from the private sector. At the same time, failure to invest sees infrastructure start to decline and innovation fade.

In brief, we need to:

- 1) **Act Now** – it will take between 5-10 years for any policy change to have an impact, we have at most 10 years to find a solution
- 2) Let people work – in the private sector – a labour shortage is a worker’s best friend
- 3) Invest in productivity: technology, innovation, commercialization and access to market
- 4) STOP trying to find everyone jobs, or paying them if the jobs don’t find them
- 5) STOP placing barriers to the free flow of the factors of production – inter provincial and international barriers to investment, trade, and labour mobility all have to be removed on an urgent basis. Why should Alberta and BC need a free trade agreement? That is why we have Canada.